National Audit Office

Financial Audit Manual 2024-25

Issued October 2024

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Section 1: Introduction

Chapter 1: Using the FAM

Purpose of the Financial Audit Manual

1.1 The Financial Audit Manual (FAM) sets out requirements and policy for those working on NAO financial audit engagements. The policy and requirements in the FAM must be adhered to for all financial audit engagements undertaken by the NAO, in addition to and in compliance with the requirements of applicable legislation, auditing and ethical standards and pronouncements from the Financial Reporting Council.

Reporting periods covered by this version of the FAM

1.2 A new version of the FAM is issued for each audit cycle. This version was issued in October 2024 and supersedes the version issued in April 2024. It should be applied for financial audit engagements covering reporting periods commencing on or after 15 December 2023 (which includes the financial year 1 April 2024 to 31 March 2025).

1.3 For engagements covering previous periods that remain ongoing after the current version has been issued, the version of the FAM applicable to the period under report should continue to be applied. For example, ongoing 2023-24 engagements should continue to apply the 2023-24 FAM issued in April 2024.

Format

1.4 Each Chapter begins with a section entitled 'Relevant standards and guidance'. This highlights the auditing standards and other sources of guidance (such as Financial Reporting Council Practice Notes) that are relevant to the topic of that Chapter. Compliance with these standards and guidance should be considered an integral part of the NAO's audit methodology.

1.5 The FAM does not repeat the full requirements of auditing standards and other relevant guidance and teams should refer to the hyperlinks included in the 'Relevant standards and guidance' sections and elsewhere. Some specific requirements are referenced or quoted in order to enhance the understandability of the FAM and for emphasis. However, whether or not the text of particular parts of auditing standards or other guidance appears in the body of the FAM has no bearing on the applicability of those requirements to NAO audits.

1.6 Paragraphs that include a mandatory requirement for the engagement team to consult or obtain approval from FAPQ or another relevant team (such as the Money Laundering Reporting Officer or Centres of Expertise) are marked with a ***Consultation required*** flair.

1.7 Queries relating to the FAM should be directed to the Financial Audit Practice and Quality team (FAPQ) using the Financial Audit Support Tool (FAST) on Sharepoint (except where queries relate to a specific engagement, in which case they should be raised using the Consultation functionality in

Apex). Follow up emails after a FAST ticket has been raised should be sent to Z3-FAPQ@nao.org.uk.

1.8 The FAM is intended only for the use of NAO staff and others as agreed with FAPQ. Any request to share the document with external parties should be directed to the FAPQ email address above.

Structure

1.9 The FAM is divided into Parts, which are themselves divided into Sections, as set out in ***Table 1A***. Each section contains Chapters as set out in the Contents Page and ***Table 1B***.

Table 1A: Structure of the FAM

Part	Section	
Overview	1	Introduction
	2	NAO functions
Service Line-level functions	3	Quality management
	4	Ethics
	5	New engagements and standing information
	6	Engagement teams
Engagement-level process	7	Audit workflow
	8	Financial statements-level procedures
Testing instructions	9	Testing techniques
	10	Contracted-out work
	11	Specialist areas
	12	Use of experts
Completion	13	Concluding and reporting

Table 1B: Chapters in the FAM

Section		Chapter	
1	Introduction	1	Using the FAM
		2	Compliance with standards
2	NAO functions	3	Status and functions of the Comptroller and Auditor General
3	Quality management	4	Quality monitoring
		5	Direction and review of the engagement
		6	Technical support and consultation
		7	Engagement Quality Review
4	Ethics	8	Ethical considerations
5	New engagements and standing information	9	Engagement acceptance (statutory and non-statutory)
		10	Determining the form of opinion
		11	Determining the framework of authorities
6	Engagement teams	12	Roles, delegations and licences
7	Audit workflow	13	Process summary for NAO audits of financial statements
		14	Audit engagement approval
		15	Gathering entity initial information
		16	Materiality, performance materiality and trivial threshold
		17	Risk assessment and response planning
		18	Regularity risk assessment and response planning
		19	Continuous risk assessment
		20	Evidence assessment and evaluation
		21	Perform certification activities

		22	Finalise, close and destroy audit file
		23	Follow-up: Ensure continuous improvement of the audit
		24	File management: Store documents and information and manage evidence
8	Financial statements-level procedures	25	Group audit procedures
		26	Combined financial statements of components with no parent
		27	Going concern
		28	Related parties
		29	Comparative information
		30	Fraud responsibilities
		31	Consideration of laws and regulations and reporting to regulators
		32	Other information and other reporting responsibilities
9	Testing techniques	33	Analytical procedures
		34	Tests of detail
		35	Controls testing
		36	Accounting estimates
		37	Other specific audit procedures
10	Contracted-out work	38	Contracting with partner organisations
		39	Role of the contractor auditor
		40	Role of the NAO engagement team in contracted-out audits
11	Specialist areas	41	Parliamentary Supply
		42	Companies
		43	Charities
		44	Pension schemes
		45	Public Interest Entities
		46	Service organisations and shared service centres
		47	Interim audit procedures, including hard close audits
12	Use of experts	48	Assessing the need for an auditor's expert
		49	Obtaining internal expertise
		50	Obtaining external expertise
		51	Scoping and evaluating the work of an expert
13	Concluding and reporting	52	Evaluating the results of procedures, including identified misstatements and irregular transactions
		53	Submission, signing and printing of annual reports and accounts
		54	Overall conclusions and preparing the certificate or report
		55	Modified certificates and reports
		56	Management representations
		57	Reporting to those charged with governance
		58	Reporting to Parliament
		59	Reporting to the devolved legislatures and in other UK languages
		60	Reporting to the members or shareholders of a company and filing with Companies House
		61	Events after the auditor's report but before issue of the financial statements
		62	Events after issue of the financial statements

Chapter 2: Compliance with standards

Relevant standards and guidance

2.1 ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independence auditor and the conduct of an audit in accordance with International Standards on Auditing (UK)* deals with the independent auditor's overall responsibilities when conducting an audit of financial statements in accordance with ISAs (UK). Specifically, it sets out the overall objectives of the independent auditor and explains the nature and scope of an audit designed to enable the independent auditor to meet those objectives. It also explains the scope, authority and structure of the ISAs (UK), and includes requirements establishing the general responsibilities of the independent auditor applicable in all audits, including the obligation to comply with the ISAs (UK).

Compliance with standards

2.2 The majority of NAO audits are conducted in accordance with International Standards on Auditing (UK) (ISAs (UK)) and Practice Note 10 (Revised 2022) *Audit of financial statements and regulator of public sector entities in the United Kingdom* (PN 10). The standards applicable to other types of engagement are set out in the NAO's terms of engagement with the audited entities (see Chapter 9: Engagement acceptance (statutory and non-statutory)).

2.3 The FAM does not repeat all the requirements of ISAs (UK) and PN 10. Full compliance with these standards is inherently part of the NAO's audit methodology and nothing in the FAM should be taken to override the requirements of ISAs (UK) or PN 10, except where specifically agreed in the terms of individual engagements. NAO engagement teams conducting audits under ISAs (UK) must comply with all ISA (UK) requirements unless the entire ISA (UK) is not relevant or the requirement is conditional and the condition does not exist.

2.4 ***Consultation required*** Any apparent conflict between the requirements of the FAM and ISAs (UK) and/or PN 10 should be raised with the Financial Audit Practice and Quality team (FAPQ), who are responsible for writing and updating the FAM.

2.5 Those working on NAO financial audits have a personal responsibility to maintain a familiarity with ISAs (UK) and PN 10 appropriate to their grade and position in the engagement team. This includes:

- completing mandatory training and other training appropriate to their role and the characteristics of the audits they are working on;
- undertaking other Continuing Professional Development activities;
- familiarising themselves with the content of communications to the Financial Audit Service Line; and
- discussing their work with peers and colleagues.

2.6 ***Table 2A*** sets out where NAO-specific policies on applying ISAs (UK) are covered in the FAM.

Table 2A: List of ISAs (UK) and where guidance is provided in the FAM

International Standard on Auditing (UK)	NAO-specific guidance included in the FAM?	FAM chapter link
ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements*	✓	Chapter 4: Quality monitoring Chapter 38: Contracting with partner organisations Chapter 39: Role of the contractor auditor Chapter 40: Role of the NAO engagement team in contracted-out audits
ISQM (UK) 2 (Updated March 2023) Engagement quality reviews	✓	Chapter 5: Direction and review of the engagement Chapter 7: Engagement Quality Review Chapter 17: Risk assessment and response planning Chapter 45: Public Interest Entities
ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards on Auditing (UK)*	✓	Chapter 2: Compliance with standards Chapter 5: Direction and review of the engagement Chapter 8: Ethical considerations Chapter 14: Audit engagement approval Chapter 17: Risk assessment and response planning
ISA (UK) 210 (Revised June 2016) (Updated May 2022) *Agreeing the terms of audit engagements*	✓	Chapter 9: Engagement acceptance (statutory and non-statutory)
ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*	✓	Chapter 4: Quality monitoring Chapter 5: Direction and review of the engagement Chapter 6: Technical support and consultation Chapter 7: Engagement Quality Review Chapter 8: Ethical considerations Chapter 9: Engagement acceptance (statutory and non-statutory) Chapter 12: Roles, delegations and licences Chapter 14: Audit engagement approval Chapter 15: Gathering entity initial information Chapter 17: Risk assessment and response planning Chapter 39: Role of the contractor auditor Chapter 40: Role of the NAO engagement team in contracted-out audits Chapter 42: Companies Chapter 45: Public Interest Entities Chapter 48: Assessing the need for an auditor's expert Chapter 49: Obtaining internal expertise Chapter 50: Obtaining external expertise

		Chapter 51: Scoping and evaluating the work of an expert Chapter 54: Overall conclusions and preparing the certificate or report
ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation*	✓	Chapter 5: Direction and review of the engagement Chapter 14: Audit engagement approval Chapter 15: Gathering entity initial information Chapter 17: Risk assessment and response planning Chapter 22: Finalise, close and destroy audit file Chapter 24: File management: Store documents and information and manage evidence Chapter 30: Fraud responsibilities Chapter 36: Accounting estimates Chapter 54: Overall conclusions and preparing the certificate or report Chapter 55: Modified certificates and reports Chapter 56: Management representations
ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements*	✓	Chapter 5: Direction and review of the engagement Chapter 6: Technical support and consultation Chapter 15: Gathering entity initial information Chapter 17: Risk assessment and response planning Chapter 18: Regularity risk assessment and response planning Chapter 30: Fraud responsibilities Chapter 34: Tests of detail Chapter 35: Controls testing Chapter 37: Other specific audit procedures Chapter 45: Public Interest Entities Chapter 47: Interim audit procedures, including hard close audits Chapter 49: Obtaining internal expertise Chapter 52: Evaluating the results of procedures, including identified misstatements and irregular transactions Chapter 54: Overall conclusions and preparing the certificate or report Chapter 56: Management representations Chapter 57: Reporting to those charged with governance
ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements*	✓	Chapter 6: Technical support and consultation Chapter 11: Determining the framework of authorities Chapter 15: Gathering entity initial information Chapter 30: Fraud responsibilities Chapter 31: Consideration of laws and regulations and reporting to regulators Chapter 40: Role of the NAO engagement team in contracted-out audits Chapter 42: Companies Chapter 43: Charities Chapter 54: Overall conclusions and preparing the certificate or report Chapter 56: Management representations Chapter 57: Reporting to those charged with governance
ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and*	✓	Chapter 11: Determining the framework of authorities Chapter 27: Going concern Chapter 30: Fraud responsibilities Chapter 31: Consideration of laws and regulations and reporting to regulators

duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector		Chapter 40: Role of the NAO engagement team in contracted-out audits Chapter 42: Companies Chapter 43: Charities Chapter 44: Pension schemes Chapter 45: Public Interest Entities Chapter 54: Overall conclusions and preparing the certificate or report Chapter 61: Events after the auditor's report but before issue of the financial statements
ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance*	✓	Chapter 17: Risk assessment and response planning Chapter 21: Perform certification activities Chapter 22: Finalise, close and destroy audit file Chapter 43: Charities Chapter 45: Public Interest Entities Chapter 46: Service organisations and shared service centres Chapter 51: Scoping and evaluating the work of an expert Chapter 57: Reporting to those charged with governance
ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management*	✓	Chapter 15: Gathering entity initial information Chapter 18: Regularity risk assessment and response planning Chapter 21: Perform certification activities Chapter 22: Finalise, close and destroy audit file Chapter 28: Related parties Chapter 32: Other information and other reporting responsibilities Chapter 35: Controls testing Chapter 46: Service organisations and shared service centres Chapter 48: Assessing the need for an auditor's expert Chapter 57: Reporting to those charged with governance Chapter 61: Events after the auditor's report but before issue of the financial statements
ISA (UK) 300 (Revised June 2016) (Updated May 2022) *Planning an audit of financial statements*	✓	Chapter 14: Audit engagement approval Chapter 15: Gathering entity initial information Chapter 17: Risk assessment and response planning
ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement*	✓	Chapter 13: Process summary for NAO audits of financial statements Chapter 14: Audit engagement approval Chapter 15: Gathering entity initial information Chapter 17: Risk assessment and response planning Chapter 19: Continuous risk assessment Chapter 29: Comparative information Chapter 30: Fraud responsibilities Chapter 33: Analytical procedures Chapter 34: Tests of detail Chapter 35: Controls testing Chapter 36: Accounting estimates Chapter 46: Service organisations and shared service centres Chapter 48: Assessing the need for an auditor's expert
ISA (UK) 320 (Revised June 2016) (Updated May 2022)	✓	Chapter 16: Materiality, performance materiality and trivial threshold Chapter 40: Role of the NAO engagement team in contracted-out audits

Materiality in planning and performing an audit		Chapter 44: Pension schemes
ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks*	✓	Chapter 17: Risk assessment and response planning Chapter 18: Regularity risk assessment and response planning Chapter 19: Continuous risk assessment Chapter 30: Fraud responsibilities Chapter 33: Analytical procedures Chapter 34: Tests of detail Chapter 35: Controls testing Chapter 36: Accounting estimates Chapter 37: Other specific audit procedures Chapter 45: Public Interest Entities Chapter 46: Service organisations and shared service centres Chapter 47: Interim audit procedures, including hard close audits Chapter 54: Overall conclusions and preparing the certificate or report
ISA (UK) 402 (Updated May 2022) *Audit considerations relating to an entity using a service organisation*	✓	Chapter 10: Determining the form of opinion Chapter 15: Gathering entity initial information Chapter 46: Service organisations and shared service centres
ISA (UK) 450 (Revised June 2016) (Updated May 2022) *Evaluation of misstatements identified during the audit*	✓	Chapter 28: Comparative information Chapter 34: Tests of detail Chapter 36: Accounting estimates Chapter 52: Evaluating the results of procedures, including identified misstatements and irregular transactions Chapter 56: Management representations
ISA (UK) 500 (Updated May 2022) *Audit evidence*	✓	Chapter 17: Risk assessment and response planning Chapter 18: Regularity risk assessment and response planning Chapter 20: Evidence assessment and evaluation Chapter 31: Consideration of laws and regulations and reporting to regulators Chapter 34: Tests of detail Chapter 36: Accounting estimates Chapter 37: Other specific audit procedures Chapter 44: Pension schemes Chapter 48: Assessing the need for an auditor's expert Chapter 49: Obtaining internal expertise Chapter 50: Obtaining external expertise Chapter 51: Scoping and evaluating the work of an expert Chapter 54: Overall conclusions and preparing the certificate or report
ISA (UK) 501 (Updated May 2022) *Audit evidence – specific considerations for selected items*	✓	Chapter 34: Tests of detail Chapter 36: Other specific audit procedures

ISA (UK) 505 (Updated July 2017) (Updated May 2022) *External confirmations*	✓	Chapter 34: Tests of detail Chapter 36: Other specific audit procedures
ISA (UK) 510 (Revised June 2016) *Initial audit engagements – opening balances*	✓	Chapter 28: Comparative information Chapter 45: Public Interest Entities
ISA (UK) 520 (Updated May 2022) *Analytical procedures*	✓	Chapter 32: Analytical procedures Chapter 54: Overall conclusions and preparing the certificate or report
ISA (UK) 530 (Updated May 2022) *Audit sampling*	✓	Chapter 34: Tests of detail Chapter 35: Controls testing
ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures*	✓	Chapter 6: Technical support and consultation Chapter 15: Gathering entity initial information Chapter 17: Risk assessment and response planning Chapter 32: Analytical procedures Chapter 35: Accounting estimates Chapter 55: Modified certificates and reports Chapter 56: Management representations
ISA (UK) 550 (Updated May 2022) *Related parties*	✓	Chapter 15: Gathering entity initial information Chapter 27: Related parties Chapter 56: Management representations
ISA (UK) 560 *Subsequent events*	✓	Chapter 22: Finalise, close and destroy audit file Chapter 61: Events after the auditor's report but before issue of the financial statements Chapter 62: Events after issue of the financial statements
ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern*	✓	Chapter 5: Direction and review of the engagement Chapter 6: Technical support and consultation Chapter 15: Gathering entity initial information Chapter 27: Going concern Chapter 42: Companies Chapter 54: Overall conclusions and preparing the certificate or report Chapter 55: Modified certificates and reports
ISA (UK) 580 (Updated May 2022) *Written representations*	✓	Chapter 29: Comparative information Chapter 45: Public Interest Entities Chapter 56: Management representations
ISA (UK) 600 (Revised September 2022) *Special considerations – audits of group financial statements (including the work of component auditors)*	✓	Chapter 8: Ethical considerations Chapter 10: Determining the form of opinion Chapter 18: Regularity risk assessment and response planning Chapter 25: Group audit procedures Chapter 29: Comparative information Chapter 57: Reporting to those charged with governance

ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors*	✓	Chapter 17: Risk assessment and response planning Chapter 18: Regularity risk assessment and response planning Chapter 48: Assessing the need for an auditor's expert Chapter 50: Obtaining external expertise Chapter 51: Scoping and evaluating the work of an expert
ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert*	✓	Chapter 9: Engagement acceptance (statutory and non-statutory) Chapter 18: Regularity risk assessment and response planning Chapter 31: Consideration of laws and regulations and reporting to regulators Chapter 36: Accounting estimates Chapter 48: Assessing the need for an auditor's expert Chapter 49: Obtaining internal expertise Chapter 50: Obtaining external expertise Chapter 51: Scoping and evaluating the work of an expert
ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements*	✓	Chapter 5: Direction and review of the engagement Chapter 8: Ethical considerations Chapter 10: Determining the form of opinion Chapter 21: Perform certification activities Chapter 22: Finalise, close and destroy audit file Chapter 32: Other information and other reporting responsibilities Chapter 38: Contracting with partner organisations Chapter 39: Role of the contractor auditor Chapter 40: Role of the NAO engagement team in contracted-out audits Chapter 45: Public Interest Entities Chapter 53: Submission, signing and printing of annual reports and accounts Chapter 54: Overall conclusions and preparing the certificate or report Chapter 55: Modified certificates and reports Chapter 58: Reporting to Parliament Chapter 61: Events after the auditor's report but before issue of the financial statements
ISA (UK) 701 (Revised November 2019) (Updated May 2022) *Communicating key audit matters in the independent auditor's report*	✓	Chapter 10: Determining the form of opinion Chapter 45: Public Interest Entities Chapter 54: Overall conclusions and preparing the certificate or report Chapter 57: Reporting to those charged with governance
ISA (UK) 705 (Revised June 2016) *Modifications to the opinion in the independent auditor's report*	✓	Chapter 54: Overall conclusions and preparing the certificate or report Chapter 55: Modified certificates and reports
ISA (UK) 706 (Revised June 2016) *Emphasis of matter paragraphs and other matter paragraphs in the*	✓	Chapter 54: Overall conclusions and preparing the certificate or report Chapter 55: Modified certificates and reports

independent auditor's report		
ISA (UK) 710 *Comparative information – corresponding figures and comparative financial statements*	✓	Chapter 29: Comparative information Chapter 54: Overall conclusions and preparing the certificate or report Chapter 55: Modified certificates and reports
ISA (UK) 720 (Revised November 2019) (Updated May 2022) *The auditor's responsibilities relating to other information*	✓	Chapter 10: Determining the form of opinion Chapter 15: Gathering entity initial information Chapter 22: Finalise, close and destroy audit file Chapter 32: Other information and other reporting responsibilities Chapter 52: Evaluating the results of procedures, including identified misstatements and irregular transactions Chapter 54: Overall conclusions and preparing the certificate or report Chapter 56: Management representations
ISA (UK) 800 (Revised October 2016) *Special considerations – audits of financial statements prepared in accordance with special purpose frameworks*	✓	Chapter 10: Determining the form of opinion Chapter 46: Service organisations and shared service centres
ISA (UK) 805 (Revised October 2016) *Special considerations – audits of single financial statements and specific elements, accounts or items of a financial statement*	✓	Chapter 10: Determining the form of opinion Chapter 46: Service organisations and shared service centres

The objectives of an audit

2.7 The NAO performs the majority of financial statement audits under International Standards on Auditing (UK) ("ISAs (UK)") issued by the Financial Reporting Council. The main exception to this is that most international audits are performed in accordance with ISAs issued by the International Auditing and Assurance Standards Board.

2.8 This Chapter sets out the overall objectives of the NAO in performing financial statement audits and explains the nature and scope of an audit designed to enable the NAO as independent auditor to meet those objectives. It also explains the scope, authority and structure of the ISAs, and includes requirements establishing the general responsibilities of the NAO applicable in all audits, including the obligation to comply with the ISAs.

2.9 For most of the NAO's audits, the C&AG will also express an opinion on the regularity of the entity's income and expenditure (i.e., whether they accord with Parliamentary intention). Throughout this

Manual, the term "risks of material misstatement" should be read as including risks of material irregular transactions, unless clearly not relevant from context. Further guidance is available in Chapter 18: Regularity risk assessment and response planning.

2.10 The NAO also considers propriety, which comprises wider issues than regularity such as fairness, integrity, the avoidance of waste and extravagance and open competition in the letting of contracts. Where issues identified are of sufficient significance, the C&AG may report on them to Parliament, based upon a consideration of whether any reporting by the audited entity has given sufficient prominence to the issue. Further guidance is available in Chapter 58: Reporting to Parliament.

2.11 ***Consultation required*** If the engagement team considers that reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient in the circumstances for the purpose of reporting to the intended users of the financial statements, the engagement team should consult FAPQ on whether disclaiming the opinion or withdrawal from the engagement (where withdrawal is possible under applicable law or regulation) is required.

2.12 ***Consultation required*** If an objective in a relevant ISA (UK) cannot be achieved and the engagement team's evaluation under paragraph 24 of ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards on Auditing (UK)* has concluded that this prevents them from achieving the overall objectives of the auditor, the engagement team should consult FAPQ on whether a modification to the opinion or withdrawal from the engagement (where withdrawal is possible under applicable law or regulation) is required.

2.13 In relation to the preceding two paragraphs, which deal with circumstances where the engagement team may be required to consider withdrawal from the engagement where possible under applicable law or regulation, paragraphs 1-5 and 1-6 of Practice Note 10 (Revised 2022) provide guidance on interpretation of the requirement to withdraw from or decline to accept an engagement where the appointment is made in statute.

The responsibilities of those charged with governance and auditors

2.14 The financial statements subject to audit are those of the entity, prepared by management of the entity with oversight from those charged with governance.

2.15 For UK audits, those charged with governance are ultimately responsible for the financial statements. In the context of the NAO's audits, the Accounting Officer is typically responsible for the governance of the entity, advised by the Audit Committee, and so is ultimately responsible for the financial statements. However, this will differ for company audits, with the board responsible for governance.

2.16 As part of the NAO's wider role, the engagement team should also seek to build on the NAO's knowledge of the business, to identify and deliver targeted interventions aimed at enabling NAO audited entities to improve public service delivery.

2.17 In conducting an audit of financial statements, the engagement team's overall objectives are:

- to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the C&AG to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and
- to report on the financial statements, and communicate as required by ISAs (UK), in accordance with the engagement team's findings.

Audit judgements

2.18 ISAs (UK) consider misstatements, including omissions, to be material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. The accounts of public sector bodies are seldom used for economic decisions, but the NAO interprets this requirement to take account of the audited entity and their circumstances, and the interests of Parliament as the usual addressee of the C&AG's audit opinion. There will be other stakeholders with an interest, such as the audited entity's customers, regulators and the general public. As public auditors, the NAO must take these additional interest groups into consideration.

2.19 Judgements about materiality are made in the light of surrounding circumstances and are affected by the engagement team's perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement or irregular transaction, or a combination of both. The C&AG's opinion deals with the financial statements as a whole and therefore the engagement team is not responsible for the detection of misstatements that are not material to the financial statements as a whole.

2.20 For the majority of the NAO's audited entities, the form of C&AG's opinion will be a conclusion on whether the financial statements give a true and fair view and are prepared in accordance with the FReM, and whether the entity's income and expenditure are regular in all material respects.

2.21 There is no statutory definition of the "true and fair" concept in UK law. However, the Financial Reporting Council has obtained a legal Opinion regarding the nature of this concept which confirms the overarching nature of the true and fair requirement to the preparation of financial statements in the UK, whether they are prepared in accordance with international or national accounting standards. The Opinion states that "The preparation of financial statements is not a mechanical process where compliance with relevant accounting standards will automatically ensure that those financial statements show a true and fair view, or a fair presentation. Such compliance may be highly likely to produce such an outcome; but it does not guarantee it."

2.22 The NAO has adopted the professional judgement framework set out in the Financial Reporting Council's Professional Judgement Guidance (June 2022) for its financial audit work. The Guidance contains a framework for making professional judgements, followed by a series of illustrative examples showing how professional judgement might be used in practice. Engagement teams are not expected to refer directly to the Guidance when making every professional judgement, but it may be referenced where a structured approach is appropriate, particularly for the most complex or difficult judgements. The principles set out in the Guidance are incorporated into the NAO's training, methodology and other intellectual resources (including this Manual) and have been considered in the design, implementation and operation of the NAO's system of quality management (see Chapter 4: Quality monitoring).

Professional scepticism

2.23 In arriving at a conclusion in support of the C&AG's opinion, engagement teams will be required to review all relevant audit evidence which has been obtained with professional scepticism and paragraph 14(d) of ISA (UK) 220 (Revised July 2021) requires the Engagement Director to establish and communicate the expected behaviour of engagement team members, including emphasising the importance of each engagement team member exercising professional scepticism throughout the audit engagement. Professional scepticism includes being alert to, for example:

- audit evidence that contradicts other audit evidence obtained;

- information that brings into question the reliability of documents and responses to inquiries to be used as audit evidence;
- conditions that may indicate possible fraud; and
- circumstances that suggest the need for audit procedures in addition to those required by ISAs (UK).

2.24 Professional scepticism is necessary to the critical assessment of audit evidence. This includes questioning contradictory audit evidence and the reliability of documents and responses to inquiries and other information obtained from management and those charged with governance. It also includes consideration of the sufficiency and appropriateness of audit evidence obtained in the light of the circumstances, for example in the case where there is a significant risk of fraud and a single document, of a nature that is susceptible to fraud, is the sole supporting evidence for a material financial statement amount. Paragraphs 7 and A33 to A36 of ISA (UK) 220 (Revised July 2021) set out matters relating to the engagement team's exercise of professional scepticism and demonstration thereof through their actions and communications, including possible impediments to the exercise of professional scepticism at the engagement level and possible actions that the engagement team may take to mitigate such impediments.

2.25 The engagement team cannot be expected to disregard past experience of the honesty and integrity of the entity's management and those charged with governance. Nevertheless, a belief that management and those charged with governance are honest and have integrity does not relieve the engagement team of the need to maintain professional scepticism or allow the engagement team to be satisfied with less than persuasive audit evidence when obtaining reasonable assurance.

2.26 The exercise of professional judgement in any particular case is based on the facts and circumstances that are known by the engagement team. Consultation on difficult or contentious matters during the course of the audit, both within the engagement team and between the engagement team and others at the appropriate level both internal and external to the NAO, such as that required by ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*, assist the engagement team in making informed and reasonable judgements.

2.27 Professional judgement needs to be exercised throughout the audit. It also needs to be appropriately documented. The engagement team is required to prepare audit documentation sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the significant professional judgements made in reaching conclusions on significant matters arising during the audit. Professional judgement is not to be used as the justification for decisions that are not otherwise supported by the facts and circumstances of the engagement or sufficient appropriate audit evidence.

2.28 Each ISA (UK) (and Practice Note 10 (Revised 2022) in respect of regularity) contains one or more objectives which are intended to focus the engagement team on the desired outcome of the ISA (UK), while helping them to:

- understand what needs to be accomplished and, where necessary, the appropriate means of doing so; and
- decide whether more needs to be done to achieve them in the particular circumstances of the audit.

2.29 As the circumstances of audit engagements vary widely and all such circumstances cannot be anticipated in the ISAs (UK), the engagement team determine the audit procedures necessary to fulfil the requirements of the ISAs (UK) and to achieve the objectives. In the circumstances of an engagement, there may be particular matters that require audit procedures in addition to those required by the ISAs (UK) to meet the objectives specified in the ISAs (UK).

2.30 The engagement team uses the objectives to evaluate whether sufficient appropriate audit evidence has been obtained in the context of the overall objectives of the auditor. If the engagement team concludes that the audit evidence is not sufficient and appropriate, then they may take one or more of the following approaches:

- evaluate whether further relevant audit evidence has been, or will be, obtained as a result of complying with other ISAs (UK);
- extend the work performed in applying one or more requirements; and
- perform other procedures judged by the engagement team to be necessary in the circumstances.

2.31 Where none of the above is expected to be practical or possible in the circumstances, the engagement team will not be able to obtain sufficient appropriate audit evidence and should determine the effect on the C&AG's opinions or on the NAO's ability to complete the engagement.

Compliance with ISAs (UK)

2.32 In some cases, an ISA (UK) (and therefore all of its requirements) may not be relevant in the circumstances. For example, if an entity has not used a shared service centre or outsourced any processing, nothing in ISA (UK) 402 *Audit considerations relating to an entity using a service organisation* is relevant.

2.33 The ISAs (UK) refer to the "objectives of the auditor", by which the ISAs (UK) mean the audit engagement partner. In the NAO context, the Engagement Director has overall responsibility for the audit, and should be regarded as the "engagement partner" or "auditor" as defined in the ISAs (UK).

2.34 Accordingly, although all members of the engagement team are responsible for performing their allocated roles in accordance with the ISAs (UK), the Engagement Director has overall responsibility for ensuring the objectives of the audit are met or concluding upon the impact if they are not.

2.35 ***Consultation required*** If, in exceptional circumstances, the engagement team judges it necessary to depart from a relevant requirement in an ISA (UK), as described in paragraph 23 of ISA (UK) 200 (Revised June 2016) (Updated May 2022), the engagement team should:

- consult FAPQ, setting out:
    - why they consider that, in the specific circumstances of the audit, the specific procedure required to be performed would be ineffective in achieving the aim of the requirement; and
    - the alternative audit procedures to be performed to achieve the aim of that requirement; and
- in accordance with paragraph 12 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation*, document:
    - how the alternative audit procedures performed achieve the aim of that requirement; and
    - the reasons for the departure; and
    - any proposed modifications to the audit certificate or report (to be discussed with FAPQ as part of the consultation referred to above).

Key definitions

2.36 The following terms are used throughout this Manual:

- Portfolio Director – the NAO Director allocated overall responsibility by the C&AG for a portfolio of audits within a Group.
- Key Audit Partner – a Key Audit Partner (KAP) is defined in UK legislation as (FRC Glossary of Terms – Ethics and auditing):
    - the statutory auditor designated by an audit firm for a particular audit engagement as being primarily responsible for carrying out the statutory audit on behalf of the audit firm; or

  - in the case of a group audit, the statutory auditor designated by an audit firm as being primarily responsible for carrying out the statutory audit at the level of the group and the statutory auditor designated at the level of material subsidiaries; or
  - the statutory auditor who signs the audit report.
- Engagement Director – the NAO Director or Senior Audit Manager who fulfils the role of "Engagement Partner" in the ISAs (UK). As such, the Engagement Director is responsible for the audit engagement and its performance, and for the audit certificate/report that is issued. The Engagement Director is also a Key Audit Partner.
- Engagement Quality Review – an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon, performed by the engagement quality reviewer and completed on or before the date of the engagement report.
- Engagement Quality Reviewer – a Director, other individual in the NAO, or an external individual, appointed by the NAO to perform the engagement quality review.
- Audit Panel – a meeting with relevant Executive Directors and the Director, Audit Quality and the engagement team to discuss the most contentious or judgmental matters.
- Engagement team – All Directors and staff performing the engagement, including contractors and any other individuals engaged by the Office who perform audit procedures on the engagement. This excludes an NAO external expert engaged by the Office. Component auditors are also part of the engagement team for group audits.

2.37 For the purpose of the NAO's compliance with ISAs (UK) and the Financial Reporting Council's Revised Ethical Standard 2019, the 'firm', as defined in paragraph 12(e) of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*, is interpreted as the Comptroller and Auditor General.

2.38 The term 'partner' as defined in paragraph 12(h) of ISA (UK) 220 (Revised July 2021) is interpreted in the NAO context to refer to any individual with authority to bind the NAO with respect to the performance of a professional services engagement. As only the C&AG has the authority to bind the NAO with respect to the performance of engagements, it is considered that in the NAO context, only the C&AG meets the definiion of a 'partner'.

2.39 The term 'personnel' as defined in paragraph 12(i) of ISA (UK) 220 (Revised July 2021) is interpreted in the NAO context to refer to the C&AG and employees of the NAO.

2.40 The term 'staff' as defined in paragraph 12(m) of ISA (UK) 220 (Revised July 2021) is interpreted in the NAO context to refer professionals, other than the C&AG, including any experts the NAO employs.

Section 2: NAO functions

Chapter 3: Status and functions of the Comptroller and Auditor General

Background

3.1 This Chapter explains the status and functions of the Comptroller and Auditor General (C&AG) in respect of audits of financial statements. These are derived from a series of Acts of Parliament and provide the C&AG with the authority to audit accounts. The basis on which the C&AG is appointed is, for most audits, different from other auditors in the United Kingdom, such as the auditors of limited liability companies and local government. This impacts on certain areas of our audits such as the nature of the opinion given and the format of the resulting report.

Methods by which the Comptroller and Auditor General is appointed as auditor

3.2 Through his responsibilities as Auditor General of Public Accounts, the C&AG provides Parliament with independent assurance on the way in which the Executive has used and accounted for funds voted by Parliament. The importance Parliament attaches to his independence is reflected in the fact that for most audits he is appointed by statute and cannot be replaced as auditor by the management or political head of the audited body.

3.3 The C&AG also audits some accounts where he is not appointed by statute. These are called agreement or non-statutory audits.

3.4 Where the C&AG undertakes the audit by statutory appointment, the terms of the statute may require the C&AG to:

- examine, certify and report on;
- examine and report on;
- examine and certify; or
- audit

the financial statements.

3.5 The statutory wording adopted does not reflect any difference in the nature of the audit required, which should be carried out in accordance with this Manual. The wording in statute does, however, affect whether the C&AG may include a discretionary report alongside his opinion.

Types of opinion provided by the C&AG

3.6 For audit engagements, the C&AG generally provides an opinion on the financial statements.

3.7 In many cases, but not always, the C&AG also provides an opinion on regularity. Regularity is the concept that transactions that are reflected in the financial statements of an audited entity must be in accordance with the relevant framework of authorities. The C&AG's audit of regularity is carried out in accordance with the guidance in Part 2 of Practice Note 10 (Revised 2022).

3.8 The C&AG may further use his powers to report to Parliament alongside his audit certificate or audit report (these additional reports are known as Reports on Accounts). These reports are discretionary and may cover issues of propriety that he decides to draw to the attention of Parliament, as well as matters impacting the financial statements and the use of public funds. More detail can be found in Chapter 58: Reporting to Parliament.

3.9 The C&AG also carries out other types of assurance and other engagements which involve reporting to different parties. Examples of these types of engagements can be found in Chapter 10: Determining the form of opinion.

The C&AG's ability to report on accounts

3.10 In many cases, the C&AG has a statutory duty to issue a report to Parliament on his examination of a set of accounts. In addition, the C&AG may choose to issue a report on an entity which he audits. The C&AG's reports are used to bring Parliament's attention to matters which have a direct or indirect effect on public expenditure. He is not restricted to reporting on transactions included in the accounts of the year under review. Nor is he barred from reporting by the fact that the accounts are in order and there are no apparent errors or irregularities.

The C&AG's access to books and records

3.11 For the entities where he is the appointed auditor, the terms of the audit engagement reflect that the C&AG's statutory rights to access all the records of the entity that he needs to examine in order to reach an opinion on the financial statements.

3.12 Under Sections 8(1) and 8(2) of the Government Resources and Accounts Act 2000 (GRAA) and Section 8 of the National Audit Act 1983, the C&AG has statutory rights of access to all documents relating to a department's or agency's accounts, including those held or controlled by a contractor responsible for compiling or handling the department's or agency's financial records. The phrase "relating to the accounts" has acquired in practice a very wide application.

3.13 Departments do not generally attempt to restrict it to a narrow bookkeeping context and an unqualified audit certificate is dependent upon the C&AG having obtained all the information and explanations that he has required.

3.14 The C&AG alone is competent to say what information he requires in order to discharge his statutory duty. An Accounting Officer may legitimately withhold information or papers if he considers the information does not directly relate to either the account or the use of resources or is not in his view reasonably required. He must be prepared to defend his actions before the Public Accounts Committee. Departments therefore do not generally deny access and it is very rare for information which the C&AG considers necessary to his audit to be withheld.

3.15 The directors and officers of companies have a responsibility to provide information required by the auditor, to which they have a legal right of access. Section 501 of the Companies Act also provides that it is a criminal offence to give to the auditor information or explanations which are misleading, false or deceptive.

Records held by entities not audited by the C&AG

3.16 The C&AG also has statutory rights of access to information held by entities which he does not audit but which spend public money provided by entities that he does audit. These entities are[1]:

[1] All except the first two of this list are under the Government Resources and Accounts Act 2000 (Rights of Access of Comptroller and Auditor General) Order 2003.

- further and higher education bodies;
- NHS bodies, including NHS Foundation Trusts;
- recipients of grant provided by entities that the C&AG audits, other than individuals in receipt of social security grants;
- train operating companies;
- registered social landlords;
- contractors and sub-contractors of entities that the C&AG audits; and
- the regulator of the Landfill Tax Credit Scheme (Entrust).

Table 3A: Documents to which the C&AG has statutory access

Entity to which the C&AG has access	Documents to which the C&AG has access
Grant recipients	Those which relate to the grant or grants received
Contractors	Those which relate to contractual obligations to supply goods and services
Train operating companies	Those which relate to the functions of the franchisee
Registered social landlord	Those which relate to the functions of the registered social landlord

3.17 In addition to this, the Local Audit and Accountability Act 2014 makes the C&AG responsible for the preparation, publication and maintenance of the Code of Audit Practice. The Code sets out what local auditors are required to do to fulfil their statutory responsibilities under the Act. The C&AG can also issue guidance to auditors which may explain or supplement the provisions of the Code. The Act also says the C&AG may examine the economy, efficiency and effectiveness with which local authorities and other local public bodies use their resources.

3.18 Over recent years central government has increasingly devolved decisions about spending priorities for its funding to the local level. However, there is no change in Parliamentary accountability for spend. Depending on the funding route, accountability is shared between the Accounting Officers of the Department for Communities and Local Government and individual funding departments.

3.19 There is a danger that accountability needs may be overlooked in the development of these new arrangements, and the work of other auditors may not be sufficient for our needs. Client departments should have in place audit trails that provide assurance that funds have been spent for the purposes intended and make appropriate arrangements to provide the NAO with access to spending bodies.

Table 3B: Legislation requiring the preparation and audit of the accounts of each type of entity for which the C&AG undertakes the audit (excluding international engagements)

Type of entity	Preparation	Audit	Considerations for audits
Department (resource accounts)	Section 5(1) of the Government Resources and Accounts Act 2000	Section 6 of the Government Resources and Accounts Act 2000	No cash fee – a notional audit fee is charged (the C&AG can only charge a cash fee with the consent of a Minister of the Crown for government departments and other bodies operating on behalf of the Crown).

Type of entity	Preparation	Audit	Considerations for audits
			The C&AG is required under the legislation to report on regularity.
Supply-financed Executive Agency or other departmental account (for example, some Trust Statements)	Section 7(1) of the Government Resources and Accounts Act 2000	Section 7(3)(b) of the Government Resources and Accounts Act 2000	No cash fee – a notional audit fee is charged (the C&AG can only charge a cash fee with the consent of a Minister of the Crown for government departments and other bodies operating on behalf of the Crown). The C&AG is required under the legislation to report on regularity.
Trading Fund (most Trading Funds are also Executive Agencies)	Section 4(6)(a) of the Government Trading Funds Act 1973	Section 4(6)(b) of the Government Trading Funds Act 1973	A cash fee is charged. A regularity opinion is given by convention.
Consolidated Fund and National Loans Fund	Section 21(1) of the National Loans Act 1968	Section 21(2) of the National Loans Act 1968	No cash fee – a notional audit fee is charged (the C&AG can only charge a cash fee with the consent of a Minister of the Crown for government departments and other bodies operating on behalf of the Crown). The C&AG reports on regularity by convention.

Type of entity	Preparation	Audit	Considerations for audits
Revenue accounts (including some Trust Statements)	An accounts direction given by HM Treasury which refers to Section 2 of the Exchequer and Audit Departments Act 1921. The Treasury's power to direct Departments to prepare accounts in relation to any specified matter is codified in Section 7 of the Government Resources and Accounts Act 2000.	*Examination of financial statements* Section 7(3)(b) of the Government Resources and Accounts Act 2000 *Examination of regulations and procedure for the assessment, collection, and proper allocation of revenue* Section 2 of the Exchequer and Audit Departments Act 1921	The C&AG is required to examine and certify revenue accounts/Trust Statements as with any other accounts prepared by a Department. Separately, the C&AG is also required to ascertain that adequate regulations and procedure have been framed to secure an effective check on the assessment, collection, and proper allocation of revenue. This examination is referred to as a 'Section 2' audit. No cash fee – a notional audit fee is charged (the C&AG can only charge a cash fee with the consent of a Minister of the Crown for government departments and other bodies operating on behalf of the Crown).
Non-Departmental Public Bodies (except those that are companies)	The specific statute governing the entity	Appointment under: the specific statute governing the entity or, where this does not appoint the C&AG and the entity is not a company, The Government Resources and Accounts Act 2000 (Audit of Public Bodies) Order 2003 or subsequent orders. Audit performed under: the specific statute governing the entity or, where this does not appoint the C&AG and the entity is not a company, Section 7(3)(b) of the	A cash fee is charged. A regularity opinion is given by convention.

Type of entity	Preparation	Audit	Considerations for audits
		Government Resources and Accounts Act 2000.	
Non-Departmental Public Bodies (NDPBs) that are non-profit making companies and subsidiary non-profit making companies	The specific statute governing the entity	Appointment under: The Government Resources and Accounts Act 2000 Orders (Audit of Non-profit-making Companies and Audit of Public Bodies) Audit performed under: Section 7(3)(b) of the Government Resources and Accounts Act 2000	A cash fee is charged. A regularity opinion is usually given by convention.
NHS England and Special Health Authorities	Paragraph 16(1) of Schedule 1A to the Health and Social Care Act 2012 Section 232 of, and Paragraph 3 of Schedule 15 to, the National Health Service Act 2006	Paragraph 16(4) of Schedule 1A to the Health and Social Care Act 2012 Section 232 of, and Paragraph 6 of Schedule 15 to, the National Health Service Act 2006	A cash fee is charged. A regularity opinion is given by convention.
Whole of Government Accounts (WGA)	Section 9(1) of the Government Resources and Accounts Act 2000	Sections 11(2) and 11(3)(a) of the Government Resources and Accounts Act 2000	No cash fee – a notional audit fee is charged for the WGA (the C&AG can only charge a cash fee with the consent of a Minister of the Crown for government departments and other bodies operating on behalf of the Crown). There is no regularity opinion given on the Whole of Government Accounts.
Other bodies, including White Paper accounts and National Loans Fund accounts.	The specific statute governing the entity.	The specific statute governing the entity.	A regularity opinion is given by convention. Whether a cash fee is charged or not depends on the status of the entity preparing the accounts.
Profit-making Company Accounts*	Section 394 of the Companies Act 2006 N.B. Exemptions may apply	Part 42, Chapter 2 of the Companies Act 2006 for profit making companies (see also Sections 1226-1238 re C&AG eligibility).	A cash fee is charged. A regularity opinion is normally not given.

Type of entity	Preparation	Audit	Considerations for audits
Charity Accounts (not NDPBs)*	Section 132 of the Charities Act 2011 (S132) N.B. Exemptions may apply	Part 8, Chapter 3 of the Charities Act 2011 N.B. Exemptions may apply Note that the C&AG is eligible for appointment as a statutory auditor under Part 42 of the Companies Act 2006. He is therefore able to be appointed auditor of a charity as per Section 144(2)(a) of the Charities Act 2011.	A cash fee is charged. A regularity opinion may be given.
Pension Scheme accounts (not Pension Scheme Resource Accounts)*	Regulation 3 of, and the Schedule to, the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, made under the Pensions Act 1995	Appointment under Section 47 of the Pensions Act 1995. Audit under Regulations 3 and 4 of the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, made under the Pensions Act 1995.	A cash fee is charged. A regularity opinion may be given.
Accounts which have no statutory requirement to be audited*	The specific statute governing the entity (if any).	No statutory basis for the audit. The terms will be governed by the letter of engagement.	A cash fee is charged. A regularity opinion may be given.

* Types of audit marked with an asterisk are where the C&AG is not named in legislation as the auditor. He can nevertheless be appointed as auditor, by agreement. These audits are known as "non-statutory" audits and are deemed "NAO-approved services" under the Budget Responsibility and National Audit Act 2011.

Delegations of the C&AG's powers

3.20 Paragraph 6 of Schedule 3 to the Budget Responsibility and National Audit Act 2011 provides for the C&AG to prepare a scheme for the delegation of functions to NAO employees. The scheme (including any revision) must be approved by the Public Accounts Commission. The C&AG may delegate functions in accordance with the approved scheme although this does not prevent the C&AG from doing anything personally. The current scheme provides for the C&AG, where he judges it appropriate, to allow named employees of the NAO to sign the financial audit certificate on his behalf for audits where the C&AG is appointed by the competent authority (i.e. audits where the C&AG is not named as the auditor in statute).

International and Commonwealth audits

3.21 The C&AG audits a wide variety of organisations and funds with international or Commonwealth responsibilities. Many of these organisations or funds are financed on a multi-

national basis by member nations and are subject to procedures and regulations laid down by their governing bodies.

3.22 ***Consultation required*** In respect of all international and Commonwealth audits, engagement teams adopt the principles outlined in this manual, modified as necessary to take account of individual circumstances and such matters as the requirements or financial regulations of their governing bodies. Most international audits will be performed in accordance with International Standards on Auditing issued by the International Auditing and Assurance Standards Board. Guidance on this can be obtained through templates and other advice issued by FAPQ. Engagement teams preparing to undertake a new international engagement must consult FAPQ on the differences between standards in force in the UK and elsewhere and what amendments may be required to standard templates to account for this.

Section 3: Quality management

Chapter 4: Quality monitoring

Relevant standards and guidance

4.1 ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* deals with a firm's responsibilities to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements.

4.2 Paragraphs 1-3 to 1-27 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISQM (UK) 1 in the public sector.

4.3 ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deals with the specific responsibilities of the auditor regarding quality management at the engagement level for an audit of financial statements, and the related responsibilities of the engagement partner. The objective of the auditor under ISA (UK) 220 (Revised July 2021) is to manage quality at the engagement level to obtain reasonable assurance that quality has been achieved such that:

- the auditor has fulfilled the auditor's responsibilities, and has conducted the audit, in accordance with professional standards and applicable legal and regulatory requirements; and
- the auditor's report issued is appropriate in the circumstances.

Individual and team responsibilities for quality

4.4 Every member of an engagement team has a personal responsibility for quality and is expected to comply with NAO policy and procedures which support this. In accordance with paragraph 4 of ISA (UK) 220 (Revised July 2021), the engagement team, led by the Engagement Director, as engagement partner, is responsible, within the context of the NAO's system of quality management and through complying with the requirements of ISA (UK) 220 (Revised July 2021), for:

- implementing the NAO's responses to quality risks (i.e., the NAO's policies or procedures) that are applicable to the audit engagement using information communicated by, or obtained from, the NAO;
- given the nature and circumstances of the audit engagement, determining whether to design and implement responses at the engagement level beyond those in the NAO's policies or procedures; and
- communicating to the NAO information from the audit engagement that is required to be communicated by the NAO's policies or procedures to support the design, implementation and operation of the NAO's system of quality management.

Leadership responsibilities for quality within the NAO

4.5 The C&AG is the individual assigned ultimate responsibility and accountability for the system of quality management as defined in paragraph 21-1(a) of ISQM (UK) 1 (this individual is required to be eligible for appointment as a statutory auditor – the C&AG is eligible for appointment as a statutory auditor under Section 1226 of the Companies Act 2006 and more broadly is appointed as the

statutory auditor of many public bodies by various other Acts of Parliament, such as the Government Resources and Accounts Act 2000).

4.6 The Executive Director of Financial Audit (ED FA) is the Executive Team member responsible for quality, reporting to the C&AG, the wider Executive Team and the NAO Board as appropriate. They are the individual assigned operational responsibility for the system of quality management, as defined in paragraph 20(b) of ISQM (UK) 1. The ED FA leads the Financial Audit Management Team (FA MT, which also includes the Deputy Head of Financial Audit (DH FA), the Director, Audit Quality; the Director, Audit Risk and Compliance; the Director, Audit Operations and the Director, Audit Transformation and Change), which has an oversight role for the quality of financial audit.

4.7 In accordance with paragraph 1-27 of Practice Note 10 (Revised 2022), which relates to the interpretation of the requirements of paragraphs 20 and 21-2 of ISQM (UK) 1, the ED FA, as the individual assigned operational responsibility for the system of quality management, is considered to have levels of experience, knowledge, influence and authority within the NAO such that they are capable of fulfilling the role of engagement partner for an audit engagement as defined in ISAs (UK), which is considered to be equivalent to the levels required to achieve eligibility for appointment as a statutory auditor.

4.8 The ED FA, who is operationally responsible for the relevant ethical requirements component of the system of quality management is also the individual assigned operational responsibility for compliance with independence requirements, in accordance with paragraph 20(c)(i) of ISQM (UK) 1.

4.9 The Director, Audit Risk and Compliance is assigned operational responsibility for the monitoring and remediation process, in accordance with paragraph 20(c)(ii) of ISQM (UK) 1.

4.10 In accordance with paragraph 22 of ISQM (UK) 1, the ED FA has a direct line of communication to the C&AG, as the individual assigned ultimate responsibility and accountability for the system of quality management. The Director, Audit Risk and Compliance also has a direct line of communication to the C&AG.

4.11 This Manual sets out the roles and responsibilities for managing quality risk within the NAO, including corporate business quality risk and individual assignment quality risk. Further details are set out in Chapter 9: Engagement acceptance (statutory and non-statutory).

4.12 The C&AG, advised by the Executive Team, allocates each Portfolio Director the responsibility for a portfolio of clients. This allocation is based upon their capabilities, competence, authority and availability to undertake the task. Each year, the ED FA and the DH FA, supported by the People Development Directors, undertake a review of Engagement Director workloads and availability as part of the annual Director rotations. This will consider whether Engagement Directors have appropriate competence and capability, including sufficient time to adequately discharge their responsibilities.

4.13 In accordance with paragraphs 13 and 14 of ISA (UK) 220 (Revised July 2021), the Engagement Director, in the role of Engagement Partner, should take responsibility for creating an environment for the engagement that emphasises the NAO's culture and expected behaviour of engagement team members. In doing so, the Engagement Director should be sufficiently and appropriately involved throughout the audit engagement such that the Engagement Director has the basis for determining whether the significant judgements made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement. In creating such an environment, the Engagement Director should take responsibility for clear, consistent and effective actions being taken that reflect the NAO's commitment to quality and establish and communicate the expected behaviour of engagement team members, including emphasising:

- that all engagement team members are responsible for contributing to the management and achievement of quality at the engagement level;
- the importance of professional ethics, values and attitudes to the members of the engagement team;
- the importance of open and robust communication within the engagement team, and supporting the ability of engagement team members to raise concerns without fear of reprisal; and
- the importance of each engagement team member exercising professional scepticism throughout the audit engagement.

4.14 All personnel within the NAO who are responsible for establishing and maintaining the firm's system of quality management should have an understanding of the entire text of ISQM (UK) 1. These include the C&AG, the ED FA, the DH FA, members of FAPQ and FA Compass.

The system of quality management – objectives

4.15 The NAO's objective under paragraph 14 of ISQM (UK) 1 is to design, implement and operate a system of quality management for audits or reviews of financial statements, or other assurance or related services engagements performed by the firm, that provides the firm with reasonable assurance that:

- the NAO and its personnel fulfil their responsibilities in accordance with professional standards and applicable legal and regulatory requirements, and conduct engagements in accordance with such standards and requirements; and
- engagement reports issued by the C&AG, by Senior Statutory Auditors on the C&AG's behalf or by Directors under a delegation arrangement, are appropriate in the circumstances.

The system of quality management – components

4.16 In accordance with paragraph 6 of ISQM (UK) 1, the NAO's system of quality management addresses the following components, in addition to the NAO's risk assessment process:

- Governance and leadership;
- Relevant ethical requirements;
- Acceptance and continuance of client relationships and specific engagements;
- Engagement performance;
- Resources (including human, intellectual and technological resources);
- Information and communication; and
- the Monitoring and remediation process.

The system of quality management – feedback

4.17 The NAO recognises the importance of obtaining feedback on its system of quality management from its employees and encourages staff to communicate their views or concerns on quality management matters. Any comments may be addressed to FAPQ using the Financial Audit Support Tool (FAST).

4.18 As set out in paragraph 5 of ISA (UK) 220 (Revised July 2021), complying with the requirements in other ISAs (UK) may provide information that is relevant to quality management at the engagement level. Paragraph 39 of ISA (UK) 220 (Revised July 2021), requires that the Engagement Director takes responsibility for:

- remaining alert throughout the audit engagement for information that may be relevant to the NAO's monitoring and remediation process; and
- communicating such information to those responsible for the process.

Any such information should be communicated by raising a Consultation within Apex and directing it to FAPQ. Examples of information that may be relevant to the NAO's monitoring and remediation process include, but are not limited to:

- New or emerging quality risks.
- Information which may affect the Likelihood or Impact risk placement of existing quality risks as recorded in the Quality Risk Registers.
- Indications that existing responses to quality risks are ineffective.
- Indications that the monitoring and remediation process is ineffective.

Such information will be passed to the individuals operationally responsible for the monitoring and remediation process through the forum of Component Quality Management meetings.

The system of quality management – stakeholders

4.19 The following individuals and teams have defined roles within the system of quality management:

- The C&AG: the individual assigned ultimate responsibility and accountability for the system of quality management.
- The ED FA: the individual assigned operational responsibility for the system of quality management.
- The Audit Quality Board (AQB): an advisory committee to the C&AG on audit quality. Its terms of reference can be found on the NAO website.
- Director Leads: individuals who provide Director-level oversight for each component of the system of quality management. They hold responsibility only for the operation of the component of the system, not the individual risks or responses within the component, which may be owned by others. Director Lead roles are held by the Director, Audit Quality, the Director, Audit Operations and the Director, Audit Risk and Compliance.
- Component Managers: individuals who have day-to-day responsibility for managing each component of the system of quality management. Component Managers are appointed by the Director Lead for their component.
- Representation from functional teams, corporate service teams and the Service Lines as appropriate.
- FA Compass: an independent assurance function within the NAO, which is responsible for the monitoring and remediation process.

The system of quality management – business process

4.20 The business process associated with the NAO's system of quality management is structured around the following high-level steps:

- Risk assessment: performed through periodic meetings of relevant stakeholders.
- Identification of responses: the periodic quality management meetings also consider the adequacy of proposed responses and whether agreed responses have been actioned and are effective.
- Monitoring: led by FA Compass in respect of financial audit engagements, who use ongoing quality review activities and quality indicators which inform the overall quality risk assessment.
- Evaluation: an annual evaluation of the system of quality management is required.
- Communications: matters relating to quality and risk assessment are communicated formally among relevant stakeholders and outcomes and actions are communicated to the Service Lines.

4.21 These processes are described in more detail in the following sections.

The system of quality management – business process – risk assessment and identification of responses

4.22 The risk assessment process is concerned with the establishment of quality objectives, the identification and assessment of quality risks and the design and implementation of responses to address the quality risks.

4.23 The NAO's quality risk assessments are documented in:

- a risk register for each component of the system of quality management (the Component Quality Risk Registers);
- a summary risk register covering all components (the Master Quality Risk Register); and
- the NAO's overall Corporate Risk Register, which is informed by the Master Quality Risk Register in respect of audit quality risks.

4.24 The Component Manager is responsible for overseeing the risk assessment process for each component of the system of quality management (except Monitoring and remediation, which is an ongoing process rather than requiring a risk review).

4.25 The process is structured around periodic quality management meetings. There is a quality management meeting for each component either annually, six-monthly, quarterly or monthly, depending on the component. If critical matters impacting quality arise outside the cycle of the periodic component quality management meetings that may warrant formal consideration, the Director lead and the individual operationally responsible for the component may decide to arrange an ad hoc quality management meeting for the component.

4.26 The Component Manager drafts an agenda for each component quality management meeting, which should be informed by the results of the monitoring process and also by observations raised by functional teams, corporate service teams or the wider Service Line, which the Component Manager collates (FA Compass also raises observations by exception with the Component Manager). The agenda should include proposals for changes to the Component Quality Risk Register, including to the responses where appropriate and should be shared with the Director Lead for the component. The agenda will also involve a consideration of on-going actions and responses to address quality risks.

4.27 The quality management meetings should be attended by:

- the individual operationally responsible for the component;
- the Director Lead for the component;
- the Component Manager for the component;
- representative(s) from corporate services teams;
- representative(s) from FA Compass; and
- by exception, representative(s) as appropriate from functional teams and the Service Line.

4.28 The risk assessment meeting for the Governance and leadership component is carried out within a meeting of the Executive Team.

4.29 If any of the required attendees cannot attend any risk assessment meeting, the Component Manager determines whether the meeting should go ahead or should be rearranged and how those unable to attend should be given the opportunity to contribute to the risk assessment and be made aware of the points discussed in the meeting. The Component Manager may choose to consult the Director Lead for the component in making this determination.

4.30 In addition to updating the Component Quality Risk Register with the outcome of the risk assessment meeting, the Component Manager prepares a minute of the risk assessment discussions, which forms a formal record of the discussion.

4.31 The revised Component Quality Risk Register following each risk assessment meeting is subject to approval by the Director Lead and the individual operationally responsible for the component.

4.32 FAPQ maintains protocols for:

- ensuring that the Master Quality Risk Register is kept up to date based upon the latest individual Component Quality Risk Registers
- sharing the Master Quality Risk Register with the team responsible for the Corporate Risk Register and with the Executive Team; and
- publishing the Master Quality Risk Register and the individual Component Quality Risk Registers on the Quality Management pages on Sharepoint.

4.33 The Audit Quality Board receives and discusses the Master Quality Risk Register from time to time – the form and frequency of these discussions is determined by the Audit Quality Board.

The system of quality management – business process – monitoring

4.34 The monitoring process is concerned with the obtaining of relevant, reliable and timely information about the design, implementation and operation of the system of quality management.

4.35 FA Compass formulates an annual monitoring plan for the Financial Audit Service Line, which is informed by the content of quality risk registers, feedback from the Executive Team and the Audit Quality Board, the findings of the previous year's monitoring process and other inputs as appropriate.

4.36 FA Compass submits the annual monitoring plan for approval by the individuals operationally responsible for the system of quality management. It is then submitted for approval by the Audit Quality Board.

4.37 In-year amendments to the annual monitoring plan may be made where appropriate.

4.38 FA Compass executes the annual monitoring plan as approved.

4.39 FA Compass collates the findings of the monitoring activities carried out and identifies where these may constitute deficiencies in the system of quality management, as described in the following section entitled 'The system of quality management – business process – evaluation'.

4.40 Paragraph 39 of ISA (UK) 220 (Revised July 2021) requires that the Engagement Director, as engagement partner, takes responsibility for obtaining an understanding of the information from the NAO's monitoring and remediation process, as communicated by the NAO, and determining the relevance and effect on the audit engagement of such information and taking appropriate action.

The system of quality management – business process – evaluation

4.41 The evaluation process is concerned with the evaluation of findings from the monitoring process to determine whether deficiencies in the system of quality management exist and with the taking of appropriate actions to respond to identified deficiencies such that deficiencies are remediated on a timely basis. As defined in paragraph 16(a) of ISQM (UK) 1, deficiencies in the system of quality management exist when:

- a quality objective required to achieve the objective of the system of quality management is not established;
- a quality risk, or combination of quality risks, is not identified or properly assessed;

- a response, or combination of responses, does not reduce to an acceptably low level the likelihood of a related quality risk occurring because the response(s) is not properly designed, implemented or operating effectively; or
- another aspect of the system of quality management is absent, or not properly designed, implemented or operating effectively, such that a requirement of ISQM (UK) 1 has not been addressed.

4.42 FA Compass identifies findings from the monitoring process which may constitute deficiencies in a specific engagement or in the system of quality management. For each of these findings, the FA Compass facilitates the carrying out of a Root Cause Analysis in accordance with paragraph 41(a) of ISQM (UK) 1 and the associated application guidance – this process is described in more detail in the section later in this Chapter entitled 'Root Cause Analysis'.

4.43 FA Compass then asks the relevant engagement team, functional team or corporate services team to formulate a response to the finding and collates the deficiencies and proposed responses, then submits a summary of deficiencies and proposed responses to the individual(s) operationally responsible for the component(s) in which the deficiencies arise, who will approve or request amendments to these.

4.44 Paragraph 45 of ISQM (UK) 1 requires responses to circumstances when findings indicate that there is an engagement(s) for which procedures required were omitted during the performance of the engagement(s) or the report issued may be inappropriate, which shall include:

- taking appropriate action to comply with relevant professional standards and applicable legal and regulatory requirements; and
- when the report is considered to be inappropriate, considering the implications and taking appropriate action, including considering whether to obtain legal advice (if legal advice is required, this should be discussed with the Legal and Policy team).
- ***Consultation required*** In addition to the required responses in the preceding bullet point, the engagement team should consult FAPQ regarding what actions are appropriate to address the deficiency on the engagement.

4.45 The procedures set out in the preceding paragraph in accordance with paragraph 45 of ISQM (UK) 1 should be undertaken where a monitoring review (either on an individual engagement or on firmwide procedures) concludes that more than limited improvements are required.

4.46 FA Compass considers the identified deficiencies within the ongoing monitoring process as described in the preceding section entitled 'The system of quality management – business process – monitoring'.

4.47 FA Compass communicates the remediations which have been approved by the ED FA to relevant engagement teams, functional teams and/or corporate services teams in a manner which indicates clearly which team(s) or individual(s) are responsible for implementing them.

4.48 The identified deficiencies are considered within the periodic quality management meetings for the relevant component(s) as described in the earlier section entitled 'The system of quality management – business process – risk assessment and identification of responses'.

The system of quality management – business process – communications

4.49 The communication process is concerned with the communication between internal parties and to external parties of information regarding the outcomes of the other aspects of the business process associated with the system of quality management.

4.50 Paragraph 46 of ISQM (UK) 1 requires that the individuals assigned operational responsibility for the monitoring and remediation process (the Director, Audit Risk and Compliance) shall communicate on a timely basis to the individual assigned ultimate responsibility and accountability for the system of quality management (the C&AG) and the individuals assigned operational responsibility for the system of quality management:

- a description of the monitoring activities performed;
- the identified deficiencies, including the severity and pervasiveness of such deficiencies; and
- the remedial actions to address the identified deficiencies.

4.51 Paragraph 47 of ISQM (UK) 1 requires that these matters are communicated to engagement teams and other individuals assigned activities within the system of quality management to enable them to take prompt and appropriate action in accordance with their responsibilities.

4.52 The responsibilities under paragraphs 46 and 47 of ISQM (UK) 1 as described above are exercised via a standing report from the Director, Audit Risk and Compliance to the C&AG, copied to the ED FA and the DH FA (the 'ISQM 1.46 report'), which is also published on the Quality Management pages on Sharepoint.

4.53 Paragraph 53 of ISQM (UK) 1 requires that the individual assigned ultimate responsibility and accountability for the system of quality management (the C&AG) shall evaluate at a point in time at least annually the system of quality management. This responsibility is exercised via a report (the 'ISQM 1.53 report') drafted using the ISQM 1.46 reports from FA Compass as the evidence base to form the conclusion.

4.54 If the conclusion of the ISQM 1.53 report under paragraph 54 of ISQM (UK) 1 is either "*except for matters related to identified deficiencies that have a severe but not pervasive effect on the design, implementation and operation of the system of quality management, the system of quality management provides the NAO with reasonable assurance that the objectives of the system of quality management are being achieved*" or "*the system of quality management does not provide the NAO with reasonable assurance that the objectives of the system of quality management are being achieved*", then the relevant Director Leads should meet to agree prompt and appropriate actions to address the identified deficiencies in accordance with paragraph 55(a) of ISQM (UK) 1 – these actions should be approved by the ED FA and the DH FA. The relevant Director Leads should also arrange for the identified deficiencies and agreed actions to be communicated to the Service Line via the Quality Management pages on Sharepoint and to relevant external parties (including, where appropriate, the Financial Reporting Council and the Public Accounts Commission) in accordance with paragraph 55(b) of ISQM (UK) 1.

The system of quality management – service providers

4.55 A service provider in the context of ISQM (UK) 1 is an individual or organisation external to the firm that provides a resource that is used in the system of quality management or in the performance of engagements. Service providers exclude the firm's network, other network firms or other structures or organisations in the network.

4.56 ISQM (UK) 1 gives the following examples of where service providers may be used:

- component auditors from other firms not within the firm's network;
- individuals engaged to perform the firm's monitoring activities or engagement quality reviews, or to provide consultation on technical matters;
- a commercial IT application used to perform audit engagements;
- individuals performing procedures on the firm's engagements, for example, component auditors from other firms not within the firm's network or individuals engaged to attend a physical inventory count at a remote location; and

- an auditor's external expert used by the firm to assist the engagement team in obtaining audit evidence.

4.57 It makes clear that assessments of service providers should be reflected in firm-level quality management documentation and factored into the firm's system of quality management and that firms should consider the quality risks that may arise from or be affected by the use of service providers.

4.58 FAPQ carries out bi-annual analysis of the NAO's service providers and their impact on the NAO's quality risks. This analysis is informed by categorisation of suppliers meeting the definition of a service provider based on their assurance requirement placement (a measure of what degree of central assurance is proportionate to identify and assess quality risks associated with each service provider)., as set out in ***Table 4A*** below. Where the table indicates that a category is presumed to include suppliers meeting certain definitions, this presumption may be rebutted where there is appropriate justification for this (for example, where the NAO has control over the outcomes of work undertaken by a service provider such that the service provider has a marginal impact on the NAO's quality risks).

Table 4A: Categories of service provider by assurance requirement

Category (assurance requirement placement)	Description	Presumed to include
High assurance required	Most strategically important service providers with a significant impact on quality objectives. Regular assurance required across all aspects of quality management for service providers.	Any supplier which is supporting a response to a 'High' rated quality risk on the Component Quality Risk Registers. Any supplier supporting more than 5 engagements. Any supplier supporting engagements or the system of quality management with total spend over £1m, except where assessed as Low Impact as the NAO has ultimate control over decisions which mitigate the associated quality risks.
Medium assurance required	Limited impact on quality objectives. Certain aspects of information relating to quality objectives are monitored based on what quality risks are impacted by the service provider.	Any supplier which is supporting a response to a 'Medium' rated quality risk on the quality risk registers or which is directly providing services to support an engagement.
Low assurance required	No material impact on quality objectives due to nature or scope of services provided. Impact rating is reconsidered if the business as usual risk assessment highlights new information.	Any supplier where spend is less than £10,000, except where scoped in as representing a response to a risk on the quality register. Any supplier where the NAO has ultimate control over decisions

		which mitigate the associated quality risks. Any supplier whose Impact is not otherwise assessed as High or Medium.

4.59 Any adverse findings from the analysis of service providers or information obtaining through the monitoring process should be communicated by FAPQ to the relevant Component Manager(s), who will incorporate these findings into the agenda for the next risk assessment meeting for the component.

The role of FAPQ in the quality monitoring process

4.60 FAPQ has a key role in the NAO's quality monitoring arrangements as part of the second line of defence. Key roles undertaken by FAPQ include monitoring:

- new developments in professional standards and legal and regulatory requirements;
- Continuing Professional Development, including training; and
- decisions related to acceptance and continuance of audited entity relationships and specific engagements.

4.61 FAPQ is also responsible for administrative activities relating to the operation of the system of quality management, such as facilitation of meetings and retaining documentation, including documentation pertaining to the assessment of service providers (see the section above entitled 'The system of quality management – service providers').

Ethical requirements

4.62 The NAO Code of Conduct outlines the ethical requirements to which NAO staff must adhere. All staff are required to complete an annual declaration stating that they have met the requirements of the Code. The returns are made online. These requirements encompass the overarching principles in the FRC Ethical Standard: Integrity and Objectivity; and Independence. They also encompass the following areas:

- Professional Competence and Due Care
- Confidentiality
- Professional Behaviour

4.63 Each member of staff has individual responsibility for compliance with ethical requirements. The fundamental principles set out in the Code of Conduct are reinforced through:

- the leadership of the Office
- education and training
- monitoring
- the NAO's processes for dealing with non-compliance

4.64 ***Consultation required*** The Code of Conduct also requires all staff to complete an annual declaration of interests. This declaration is made online and a register of interests is maintained by Human Resources. Section 5 of the Code includes requirements to declare business and financial relationships and previous and future (potential) employment with audited entities. In addition, engagement team members complete a declaration of independence for each audit engagement in Apex, in which they must consider whether there are any circumstances or relationships which may, or could be perceived to, create a threat to their independence or objectivity as a member of the engagement team. If the engagement team member becomes aware of any further such circumstances or relationships during the course of the engagement, they must notify these to the

Engagement Director, who will consult the Ethics Function and/or the Chief People Officer, as appropriate. Where an individual needs to make a new declaration in any of the above circumstances, they should complete a new Code of Conduct return as soon as possible. The Engagement Director, in consultation with the Ethics Function, must ensure the Apex audit file includes documentation of how the potential conflict has been managed, including any agreed safeguards and how they have been applied.

4.65 To safeguard against the threat of familiarity to independence, a Portfolio Director allocation is subject to a rotation at least every five years. In certain limited circumstances where there is a clear audit quality reason to do so, an individual may continue as Portfolio Director for an additional year. Where this reason remains valid after this first year, this may be extended for one more year but only after another application to do so. This means that the maximum term for a Portfolio Director, in limited circumstances, would be five-plus-one-plus-one years, conditional on approval being granted for the extensions.

4.66 ***Consultation required*** Any request for an individual to act as Portfolio Director for longer than a period of five continuous years must be approved by the Executive Director of Financial Audit based on a recommendation from the Director, Audit Operations following review and approval by the Director, Audit Risk and Compliance, following the process set out in Chapter 8: Ethical considerations.

4.67 ***Consultation required*** In accordance with paragraph 20 of ISA (UK) 220 (Revised July 2021), if matters come to the Engagement Director's attention through the NAO's system of quality management or otherwise that indicate that relevant ethical requirements applicable to the nature and circumstances of the audit engagement have not been fulfilled, the Engagement Director, in consultation with FAPQ, will determine the appropriate action.

4.68 As required by paragraph 21 of ISA (UK) 220 (Revised July 2021), prior to signing the audit certificate or report, the Engagement Director should take responsibility for determining whether relevant ethical requirements, including those related to independence, have been fulfilled.. In doing so, the Engagement Director should:

- obtain relevant information from within the NAO and, where applicable, from its contractors involved on an engagement, to identify and evaluate circumstances and relationships that create threats to independence;
- escalate any identified breaches, if any, of the NAO's independence policies and procedures, and evaluate in consultation with the Director, Audit Quality, whether they create a threat to independence for the audit engagement;
- take appropriate action to eliminate such threats or reduce them to an acceptable level by applying safeguards, or, if considered appropriate, to withdraw from the engagement, where withdrawal is possible under applicable law or regulation. The Engagement Director must report promptly to the Director, Audit Quality, any inability to resolve the matter for appropriate action.

Acceptance and continuance of audited entity relationships and specific engagements

4.69 The C&AG's independence is enshrined in statute. This underlines the need for all NAO staff to be objective and impartial in all their work, including accurate, fair and balanced reporting.

4.70 As required by paragraph 22 of ISA (UK) 220 (Revised July 2021), the Engagement Director should be satisfied that appropriate procedures regarding the acceptance and continuance of audited entity relationships and audit engagements have been followed, and should determine that conclusions reached in that regard are appropriate.

4.71 ***Consultation required*** In accordance with paragraph 24 of ISA (UK) 220 (Revised July 2021), if the Engagement Director obtains information that would have caused the NAO to decline the audit engagement had that information been available earlier, the Engagement Director must communicate that information promptly to the Director, Audit Quality, in the first instance, so that the NAO and the Engagement Director can take the necessary action.

4.72 Paragraphs 1-5 to 1-6 of Practice Note 10 (Revised 2022) provide guidance on applying the requirements of ISQM (UK) 1 in the circumstances where the NAO is required by law, regulation or statute to accept or continue an engagement.

Human resources

4.73 All staff are required to undertake continuing professional development (CPD) and to take responsibility for updating their technical knowledge. The Office has established its own targets for CPD and staff are required to adhere to these as well as ensuring that they comply with the requirements of their respective institute, including the submission of an annual CPD return where required. Guidance on CPD requirements is available on Sharepoint here. All staff are responsible for recording all their CPD shortly after it has been undertaken in the "MyHR" section in Financial Force. This will form the basis of discussions with performance coaches at the interim and final stages of the appraisal process. Completion of this record forms part of the NAO Code of Conduct.

4.74 Responsibility for each audit is assigned to an Engagement Director, whose identity and responsibilities are communicated to audited entity management and those charged with governance.

4.75 As required by paragraph 32(d) of ISQM (UK) 1, the NAO has established policies and procedures through the Resource Directors, Financial Force and the audit planning process to assign engagement team members to each engagement , including an engagement partner, who have appropriate competence and capabilities, including being given sufficient time, to consistently perform quality engagements.

4.76 The NAO has established policies and procedures designed to provide the Office with assurance that it has sufficient personnel with the capabilities, competence, and commitment to ethical principles necessary to perform its engagements in accordance with professional standards and regulatory and legal requirements. This enables the C&AG to issue audit certificates/reports that are appropriate to the circumstances. These policies and procedures are recorded in the HR Manual.

4.77 The NAO seeks to recruit the best quality candidates to meet its current and future needs, using the principles of fair and open competition in line with its policy on equal opportunities. The recruitment process aims to achieve an appropriate balance between the recruitment and retention of staff on permanent contracts, fixed-term contracts and other forms of employment. Further details can be found in the NAO's HR Manual.

4.78 In addition, the Office develops the capabilities and competence of its staff through a combination of structured and unstructured training and career development. Further information on the NAO's performance management approach can be obtained from Merlin.

4.79 The NAO is a registered trainer for the ICAEW.

4.80 The performance management framework includes a consideration of training undertaken during the period under review and a review of current developmental needs.

Quality monitoring

4.81 Obtaining audited entity feedback on the quality of the NAO's financial audit is important in ensuring that the NAO fully understands the needs and expectations of its audited entities and continues to provide the quality of audit they expect.

4.82 Paragraph 34(c) of ISQM (UK) 1 requires that the NAO has policies and procedures for receiving, investigating and resolving complaints and allegations about failures to perform work in accordance with professional standards and applicable legal and regulatory requirements, or non-compliance with the NAO's policies or procedures established in accordance with ISQM (UK) 1. The NAO Code of Conduct requires that staff discuss any such matters that come to their attention with their Director, Executive Director or the Chief People Officer.

4.83 ***Consultation required*** Complaints on the standard of audit work from audited entities should be directed to the Engagement Director and client lead in the first instance. If the issue is not satisfactorily resolved, the complaint must be raised with the Director, Audit Quality. Any complaints or allegations made against the NAO should be documented, together with the responses to them.

4.84 If differences of opinion arise within the engagement team, with those consulted or, where applicable, between the Engagement Director and the Engagement Quality Reviewer, the engagement team shall follow the NAO's policies and procedures for dealing with and resolving differences of opinion.

4.85 ***Consultation required*** Conflicts of opinion between audit staff and Engagement Directors must be resolved by discussion with the Director, Audit Quality.

4.86 ***Consultation required*** If an Engagement Quality Reviewer or Hot Reviewer or person undertaking another peer review disagrees with the Engagement Director, the matter must be referred to the Director, Audit Quality to discuss the issue. If an agreement is not reached, then the C&AG will decide.

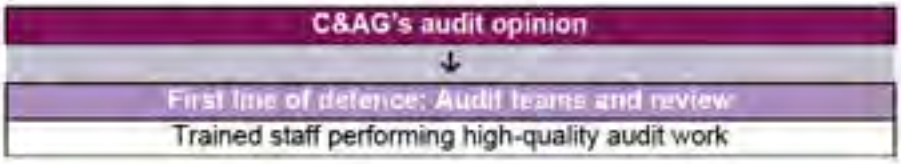
4.87 The conclusions reached in respect of differences of opinion should be documented and implemented. Once agreement is reached the working papers should be signed off by those responsible for the decision. The audit certificate/report should not be dated until the matter is resolved.

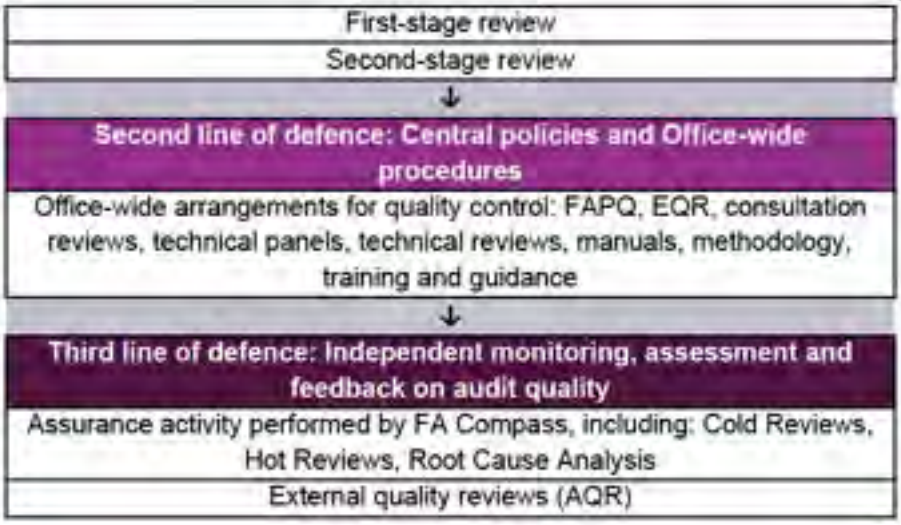
FA Compass

4.88 FA Compass is an independent assurance function within the NAO which supports the Financial Audit Service Line to deliver audits which meet the NAO's quality aspirations and professional standards. FA Compass programmes of work are designed to ensure that audits are complying with auditing standards and the requirements of this Manual and provide feedback to the Service Line on areas where the NAO can continue to improve.

4.89 ***Figure 4B*** shows the NAO's three lines of defence model and FA Compass's part in this as the third line of defence.

Figure 4B: The quality management framework – the NAO's three lines of defence





4.90 FA Compass has no direct role in the formation of audit opinions, the design of audit methodology, the design and delivery of audit work, or advising line engagement teams on their audits and underpinning judgements.

4.91 The Director, Audit Risk and Compliance has overall responsibility for the management of FA Compass within the wider leadership structure governing the Financial Audit Service Line. The Director, Audit Risk and Compliance will be supported by team members within FA Compass. However, certain functions will be undertaken by experienced managers drawn from the wider Financial Audit Service Line.

4.92 To meet its aim, FA Compass undertakes a range of activities and the following paragraphs sets these out.

Internal inspection programme

4.93 FA Compass manages the NAO's annual programme of post-certification inspection reviews (also known as "cold reviews"). These reviews will be carried out on a sample of NAO audits and will focus on whether the audit complied with professional standards and the Financial Audit Manual.

4.94 FA Compass select a sample of audits for review each year. This sample will aim to include every NAO Director each year with Senior Audit Managers selected at least every three years. It is designed to include a cross section of audits, including contracted out audits, delegated audits, and audits of different size and complexity. FA Compass will consult with the Director, Audit Quality and the Executive Director of Financial Audit in finalising the number of audits to be reviewed and the proposed sample.

4.95 Where the previous year's cold review programme graded an audit as requiring significant improvement or areas for improvements, a follow-up cold review will be performed. The review will be limited to those areas of the audit which failed to meet the quality standard in the previous year.

4.96 Each audit will be reviewed by an experienced Senior Audit Manager drawn from the service line following a checklist revised annually by FA Compass. In addition to gaining access to the audit file, the reviewer will ask the engagement team to provide key documentation which might include the accounts, the audit planning report, the testing plan, the audit completion report and any other required information. The engagement team may supplement this information with any additional documents that they believe will assist the review manager.

4.97 Cold reviewers will declare that they are sufficiently independent from the audit that they are being asked to review. To make such a positive declaration, they will:

- confirm that they have had no role in performing the particular audit for three years before the year under review;
- that they have not worked for, or in any way been line managed by, the Engagement Manager or Director of the audit for three years before the year under review; and
- that there are no personal or financial circumstances as defined in the FRC Ethical Standard which would prevent them from providing an objective assessment of the audit.

4.98 The reviewer will provide their findings in the checklist to the engagement team who will add their responses and any further evidence to the issues raised in the checklist. The review manager should discuss emerging findings with FA Compass as appropriate.

4.99 On receipt of the team's responses, the reviewer will provide a formal comment in the checklist, stating whether the issue is cleared or whether it has been confirmed. They should provide an indicative grade and draft overall comments.

4.100 Each review will be allocated a Review Director, normally the Director, Audit Risk and Compliance or another Director requested to take on this role on specific audits at the request of the Director, Audit Risk and Compliance, who will support the review manager and review issues raised and conclusions reached in the checklist. The Review Director will confirm the draft rating assigned to the audit and provide overall comments in the summary in the space provided. The completed checklist is provided to the Engagement Director who is asked to provide overall comments in the space provided.

4.101 The completed draft review should then be provided to FA Compass. At this stage, the checklist should not be provided to the engagement team, but the team should be informed that second-stage review has begun.

4.102 As part of agreeing the final rating for a particular audit, all the reviews will be considered and moderated by a Review Panel of NAO Directors drawn from the service line. This Review Panel will be chaired by the Director, Audit Risk and Compliance. It will recommend a final rating, taking into account the issues raised both in this review and across the suite of reviews, with the aim of promoting equality and consistency across the population. The Review Panel may call for additional clarification and evidence before agreeing a final rating, including asking the review manager to undertake further work where necessary.

4.103 Each reviewed audit will be awarded one of four ratings, as set out in ***Table 4C***. The Good and Only Limited Improvement Required ratings count as falling above the NAO's quality threshold. The Areas for Improvement and Significant Areas for Improvement ratings fall below this threshold and will be subject to a follow up review in the subsequent audit cycle. Audits with higher ratings may also have findings for the team to consider but will not be subject to a further review in the following year.

Table 4C: Ratings awarded to audits subject to a cold review

Grade	Definition
Significant Areas for improvement	The review has identified significant areas of non-compliance with the ISAs and/or the NAO FAM.
Areas for improvement	The audit was generally compliant with the ISAs and the NAO FAM. However, there were areas for improvement in the audit approach and/or the evidence obtained.
Only limited improvements needed	In all major areas, including documentation, the audit was compliant with the standards and principles of the ISAs and the NAO FAM and only minor issues have been identified.
Good	In all areas, the audit was consistent with the standards and principles of the ISAs and the NAO FAM and may also have demonstrated examples of good practice.

4.104 Once the grade has been confirmed by the Review Panel, the Director, Audit Risk and Compliance will write to the respective Engagement Directors to confirm the grade, with copies to the Executive Team. The final checklist will include a summary of the key reasons for the assigned grade.

4.105 When an individual audit is reviewed internally or externally as part of the monitoring process, FA Compass considers the findings from the review to identify whether deficiencies in the system of quality management exist and to determine appropriate actions to remediate these on a timely basis – this process is described in the section earlier in this Chapter entitled 'The system of quality management – business process – evaluation', which sets out that FA Compass carries out Root Cause Analysis on findings which may constitute deficiencies and collates proposed responses to these in consultation with the relevant engagement team, functional team or corporate services team. FA Compass will also raise any deficiencies with the Component Manager to be included within the agenda for the relevant component quality management meeting(s), in accordance with the business process outlined earlier in this Chapter.

4.106 Reviewers will also normally seek read-only access to the audit file being reviewed. As Information Asset Owners, Portfolio Directors should consider whether there are any appropriate restrictions on providing Review Managers with access to audit files, for example security clearance considerations and, if there are, they should discuss this with the Director, Audit Risk and Compliance.

Hot reviews

4.107 Hot reviews are a key mechanism whereby FA Compass addresses the risk to the C&AG of providing an incorrect or unsupported audit opinion. Hot reviews involve a risk-based review of the audit and consider whether these have been sufficiently evidenced within the audit file. Based on its review, FA Compass will provide negative assurance directly to the C&AG that there are no outstanding issues to resolve prior to certification by the C&AG.

4.108 The audits selected each year are determined by the Director, Audit Risk and Compliance, in consultation with the Director, Audit Quality and the Executive Director of Financial Audit and Deputy Head of Financial Audit. The audits selected are then communicated to financial audit teams in time for planning reviews to take place. The range of audits covered may encompass audits carried out by NAO staff and those carried out by contractor auditors on behalf of the NAO.

4.109 The reviews will be carried out by an experienced Senior Audit Manager (review manager), under the supervision of FA Compass. The Review Manager will be asked to declare that they are

sufficiently independent from the audit that they are being asked to review (along the lines of the declaration required from cold reviewers as set out above).

4.110 The scope of the hot review will be determined by the reviewer following discussions with the audit team and Director, Audit Risk and Compliance. Reviewers will undertake a risk focused review of key areas of judgement and whether these have been sufficiently evidenced within the audit file. Reviewers will use their judgement as to the scope of their review depending on the audit itself, its risks and the engagement team. As a minimum, the scope will cover materiality, the completeness of the risk assessment process and the proposed audit response to the significant risks. In determining the scope, the reviewer will consider the largest balances in the financial statements, examine management's own disclosures on significant judgements and estimation uncertainty in the accounts and review the prior year Audit Completion Report and the latest Audit Planning Report.

4.111 For any audits completed by contractor auditors that fall within the hot review programme, the review will focus on the NAO's monitoring role and the sufficiency of the evidence gathered by the contractor auditor against the significant audit risks, as evidenced on the NAO audit file.

4.112 The engagement team is encouraged to engage with their Review Manager throughout the audit process to reduce the burden at the certification stage. However, Review Managers are required to engage formally at two key points:

- to undertake a risk-based examination of key areas of judgement in planning and whether these have been sufficiently evidenced within the audit file; and
- to undertake a risk focused review of fieldwork, including key areas of judgement and whether these have been sufficiently evidenced within the audit file, prior to the audit being submitted to the C&AG for certification.

4.113 Engagement Directors should discuss the scheduling of their pre-certification review with their Review Manager, ensuring that there is sufficient time allowed for the review to be completed in the way intended and for any matters arising to be resolved prior to the intended certification date.

4.114 Pre-certification hot reviews will be completed at the point at which the Engagement Team and the reviewer agree that the audit work which falls within the scope of the review is sufficiently complete for the review to commence. The reviews may, therefore, take place while aspects of the audit that are outside the scope of the review are still being finalised.

4.115 On completing the planning and pre-certification stages of the hot review, the Review Manager will produce a schedule of findings. These will be shared with the responsible Engagement Director and Engagement team. The Engagement team and Director should document their responses and return the schedule to the Review Manager, who will clear the points if appropriate, or ask for further clarification if required. Review Managers may use their judgement (in consultation with the Director, Audit Risk and Compliance) in determining the significance of the findings. All points raised should be cleared before certification.

4.116 If there are significant matters that cannot be resolved between the hot reviewer and the engagement team, then these will be escalated to the Director, Audit Risk and Compliance who will determine the way forward. This may involve the Director, Audit Risk and Compliance escalating these to FAPQ and Executive Directors for them to advise and intervene, as appropriate, before the accounts can be submitted for certification. Ultimately, in concluding the review, and taking all evidence and advice into account, the Director, Audit Risk and Compliance will submit the completed review to the C&AG with appropriate advice.

4.117 FA Compass will monitor the overall results and outputs from the review process. FA Compass considers the findings from the review to identify whether deficiencies in the system of quality management exist and to determine appropriate actions to remediate these on a timely basis – this process is described in the section earlier in this Chapter entitled 'The system of quality management – business process – evaluation', which sets out that FA Compass carries out Root Cause Analysis on findings which may constitute deficiencies and collates proposed responses to these in consultation with the relevant engagement team, functional team or corporate services team. FA Compass will also raise any deficiencies with the Component Manager to be included within the agenda for the relevant component quality management meeting(s), in accordance with the business process outlined earlier in this Chapter.

Root Cause Analysis

4.118 The NAO uses Root Cause Analysis (RCA) to help drive improvements in financial audit quality. RCA is a process for identifying the cause of problems or events in order to prevent them from recurring. RCA can also be a means of identifying good practice as part of the NAO's continuous improvement programme.

4.119 In accordance with paragraph 41(a) of ISQM (UK) 1 and the associated application guidance, FA Compass conducts RCAs on each finding of the monitoring process that represents a deficiency in respect of a specific engagement or in the system of quality management (see the section earlier in this Chapter entitled 'The system of quality management – business process – evaluation'), including audits from the internal and external inspection programmes which have been assessed as being below the NAO's quality threshold. This will additionally include conducting an RCA into any matters which cause a breach of the FRC's Ethical Standard. FA Compass will also conduct RCA on a selection of audits which have met the quality threshold to identify good practice. FA Compass may also decide to undertake other RCAs covering other issues or themes which it identifies during the year.

4.120 The RCAs will be conducted by members of FA Compass team with support from other teams where required. The RCA sessions will be attended by members of the audit team including the manager and director and other team members were applicable.

4.121 FA Compass will produce a report after each RCA session which will summarise the issues identified and action required by the team and the wider NAO Service Line, where appropriate. FA Compass will share this report with the relevant Component Manager to inform the agenda for the relevant component quality management meeting(s), in accordance with the business process outlined earlier in this Chapter.

4.122 FA Compass might also undertake a more detailed investigation, using RCA principles, on a particular audit where this is deemed appropriate and report its results to the Leadership Team, who might commission such a review (for example, in instances where the AQR have determined an audit to require significant improvement).

Other FA Compass activities

4.123 FA Compass carries out other activities to assure audit quality, including:

- **Firm-wide review** – FA Compass undertakes an annual evaluation of the NAO's internal quality control system (the output of which is known as the ISQM 1.53 report – see the section earlier in this Chapter entitled 'The system of quality management – business process – communications').
- **Communication of findings to the wider NAO** – FA Compass will produce digests of its findings from its interventions to the wider office on a timely basis.

- **Promoting Transparency** – FA Compass oversees, co-ordinates and delivers a programme of transparency reporting, including the annual Transparency Report and support to the C&AG for the Public Accounts Commission's annual session on financial audit quality.
- **Supporting the NAO's Audit Quality Board** – FA Compass provides secretariat support to the Audit Quality Board.

External inspection programme

4.124 The Financial Reporting Council's Audit Quality Review (AQR) team carries out an annual review of a small sample of the NAO's financial audits. This review is a statutory requirement for the audits the NAO performs under the Companies Act, and a voluntary arrangement for audits performed under other legislation or by agreement with the audited bodies.

4.125 The AQR assesses:

- the NAO's compliance with auditing standards and the NAO's audit policies;
- the sufficiency of evidence on the audit file to support the audit opinion; and
- the effectiveness of the NAO's corporate policies and procedures for ensuring the quality of financial audit.

4.126 The Director, Audit Quality facilitates the delivery of the AQR's reviews and the NAO's responses and supports relevant audit teams as they consider their responses to the AQR's findings.

4.127 Once it has completed its annual inspection, the AQR will report to the C&AG setting out a summary of its findings from each of the financial audits reviewed. The AQR will also provide a more detailed report to each of the individual audit teams on the results of its inspection.

4.128 Responsibility for implementing the specific findings of the AQR rests with the Executive Team, the Director, Audit Quality and the relevant audit team. The Director, Audit Quality will ensure that the Executive Team and the FA Management Team are sighted on emerging issues arising from the reviews by raising these as observations to be included within the agenda for the relevant component quality management meeting(s), in accordance with the business process outlined earlier in this Chapter. The Director, Audit Quality will also seek the C&AG's approval of the draft summary reports from the AQR.

Chapter 5: Direction and review of the engagement

Revised standards and guidance

5.1 ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* includes requirements relating to the direction, supervision and review of an audit engagement.

Central policies and procedures

5.2 The NAO has policies and procedures which are designed to provide reasonable assurance that engagements are performed in accordance with professional standards and regulatory and legal requirements and to ensure that the certificate or report issued is appropriate to the engagement. These include:

- The Audit Quality Board (whose terms of reference are available on the NAO website here), which oversees the comprehensiveness, reliability and integrity of the framework supporting the technical quality of the NAO's audit work.
- Financial Audit Programme Board (FAPB) meetings, whose members oversee practice management issues and which is attended by Financial Audit Executive Directors and the Directors of FAPQ, FA Compass, Financial Audit Operations, the Audit Transformation Programme and others as required.
- A Financial Audit Directors Group (FADG), which advises the Director, Audit Quality.
- Up-to-date technical guidance that is issued by FAPQ. The team also provides continuing training for financial audit staff, including a mandatory annual update course.
- Teams may consult FAPQ on difficult or contentious matters on audits (such as complex or judgemental accounting and auditing issues), and all qualifications or proposed qualifications must be considered by the technical team.
- ***Consultation required*** All audits should be conducted within the Apex environment. If this is not considered appropriate, the engagement team must contact FAPQ who maintain a record of all accounts held outside Apex. The Apex documentation package provides standardised templates and checklists, and a consistent structure for engagement documentation and review, and records the timing and extent of the review undertaken.
- Each member of staff involved in an engagement is required to be fully briefed on their role in advance of starting work. Key objectives are agreed and feedback is provided at the end of the assignment. The Engagement Manager and Lead are responsible for ensuring that appropriate desk training is provided.
- The NAO has a two-stage review process. The first stage involves a review of all working papers and audit procedures by the Engagement Manager (or, where delegated with the approval of the Engagement Director, another team member with more seniority than the preparer) to ensure the requirements of individual procedures are met and have been completed and documented appropriately (i.e., in accordance with ISAs (UK) and this Manual). The second-stage review is undertaken by the Engagement Director and is more overarching, typically covering the major issues of judgement in the audit.
- For complex accounts or those considered high risk, or where a modification is expected to the audit opinion, independent director reviewers (Engagement Quality Reviewers) are appointed. Chapter 7: Engagement Quality Review provides further detail on these arrangements.
- Appropriate supervision is maintained throughout the audit by the Engagement Manager. This ensures that the audit is progressing to timetable; that individuals are equipped to undertake the tasks allocated; and that significant issues are considered during the course of the engagement (with technical advice being sought as appropriate). This is documented within Apex, for example through Team Tasks and Review Comments.

Responsibilities of the engagement team

5.3 The Engagement Director is responsible for ensuring that the appointed team is capable and competent to carry out the audit. In accordance with paragraph 28 of ISA (UK) 220 (Revised July 2021), the Engagement Director, as engagement partner, should take responsibility for using the resources assigned or made available to the engagement team appropriately, given the nature and circumstances of the audit engagement.

5.4 In accordance with paragraph 29 of ISA (UK) 220 (Revised July 2021), the Engagement Director should take responsibility for the direction and supervision of the members of the engagement team and the review of their work.

5.5 The Engagement Director has overall responsibility for these activities, supported by other members of the engagement team.

5.6 As stated in paragraph A85 of ISA (UK) 220 (Revised July 2021), direction of the engagement team involves informing the members of the engagement team of their responsibilities, such as:

- contributing to the management and achievement of quality at the engagement level through their personal conduct, communication and actions;
- maintaining a questioning mind and being aware of unconscious or conscious auditor biases in exercising professional scepticism when gathering and evaluating audit evidence;
- fulfilling relevant ethical requirements;
- the respective responsibilities of the C&AG, Executive Directors, Engagement Director and, where relevant, Portfolio Director and/or Engagement Quality Reviewer and/or component Engagement Director(s)/Engagement Partner(s) and/or contractor audit firm partner(s) in the conduct of an audit engagement;
- the responsibilities of respective engagement team members to perform audit procedures and of more experienced engagement team members to direct, supervise and review the work of less experienced engagement team members;
- understanding the objectives of the work to be performed and the detailed instructions regarding the nature, timing and extent of planned audit procedures as set forth in the overall audit strategy and audit plan;
- addressing threats to the achievement of quality, and the engagement team's expected response. For example, budget constraints or resource constraints should not result in the engagement team members modifying planned audit procedures or failing to perform planned audit procedures.

5.7 Discussion among members of the engagement team allows less experienced team members to raise questions with more experienced team members so that appropriate communication can occur within the engagement team.

5.8 Appropriate teamwork and training assist less experienced members of the engagement team to clearly understand the objectives of the assigned work.

5.9 As stated in paragraph A86 of ISA (UK) 220 (Revised July 2021) supervision includes matters such as:

- tracking the progress of the audit engagement, which includes monitoring:
    - the progress against the audit plan;
    - whether the objective of work performed has been achieved; and
    - the ongoing adequacy of assigned resources;
- taking appropriate action to address issues arising during the engagement, including for example, reassigning planned audit procedures to more experienced engagement team members when issues are more complex than initially anticipated;
- identifying matters for consultation or consideration by more experienced engagement team members during the audit engagement;

- providing coaching and on-the-job training to help engagement team members develop skills or competencies; and
- creating an environment where engagement team members raise concerns without fear of reprisals..

Table 5A: Key responsibilities for quality control for an individual engagement

Staff member	Key responsibilities
Portfolio Director	Responsible for assessing the risk and sensitivity of each audit engagement within the portfolio, and for ensuring that a suitable Director or Senior Audit Manager is assigned Engagement Director responsibility for that audit. Where the Engagement Director role on the audit engagement is delegated, the Portfolio Director's responsibilities include the following: • Ensuring a suitable Senior Audit Manager is assigned Engagement Director responsibility for the audit. • Maintaining dialogue with Engagement Director during the audit, coaching and acting as a sounding board as appropriate. • Considering whether the risk profile of the audit means it remains a Type X engagement (and therefore continuing delegation is appropriate). • Scan-reading the financial statements with key sector knowledge in mind, looking at primary statements and key notes. • Reading the Audit Completion Report. • Providing a short minute to be included on the Certification Journal confirming they have performed the above role and are content that the delegation of Engagement Director role to the Senior Audit Manager remains appropriate.
Engagement Director	Responsible for the audit engagement and its performance, and for the audit certificate that is issued. Overall responsibility for quality. Supported by the Engagement Manager: sets the Overall Audit Strategy; assesses materiality for the audit; determines the required risk assessment procedures Approves the audit plan. Approves the budget and audit protocols. Responsible for significant professional judgements in the audit and conclusions on risks. Determines how review should be carried out. Performs second-stage review, which includes ensuring that detailed first-stage review has been performed, although not re-performing it. **Responsibilities for managing and achieving quality on audits** Managing and achieving quality on the audit engagement. Creating an environment for the engagement that emphasises the NAO's culture and expected behaviour of engagement team members. Being sufficiently and appropriately involved throughout the audit engagement such that the Engagement Director has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the engagement. Taking clear, consistent and effective actions that reflect the NAO's commitment to quality and establish and communicate the expected behaviour of engagement team members, including emphasizing: • that all engagement team members are responsible for contributing to the management and achievement of quality at the engagement level; • the importance of professional ethics, values and attitudes to the members of the engagement team;

	• the importance of open and robust communication within the engagement team, and supporting the ability of engagement team members to raise concerns without fear of reprisal; and • the importance of each engagement team member exercising professional scepticism throughout the audit engagement. If the Engagement Director assigns the design or performance of procedures, tasks or actions related to a requirement of ISA (UK) 220 (Revised July 2021) to other members of the engagement team to assist the Engagement Director in complying with the requirements of ISA (UK) 220 (Revised July 2021), the Engagement Director should continue to take overall responsibility for managing and achieving quality on the audit engagement through direction and supervision of those members of the engagement team, and review of their work. **Responsibilities relating to relevant ethical requirements, including those related to independence** Having an understanding of the relevant ethical requirements, including those related to independence, that are applicable given the nature and circumstances of the audit engagement. Making other members of the engagement team aware of relevant ethical requirements that are applicable given the nature and circumstances of the audit engagement, and the NAO's related policies or procedures, including those that address: • identifying, evaluating and addressing threats to compliance with relevant ethical requirements, including those related to independence; • circumstances that may cause a breach of relevant ethical requirements, including those related to independence, and the responsibilities of members of the engagement team when they become aware of breaches; and • the responsibilities of members of the engagement team when they become aware of an instance of non-compliance with laws and regulations by the entity.
Engagement Quality Reviewer (where applicable)	To provide an objective evaluation of the significant judgements made by the engagement team, and the conclusions reached thereon (as required by paragraph 8 of ISQM (UK) 2 *Engagement quality reviews*). The detailed responsibilities of an Engagement Quality Reviewer are set out in ISQM (UK) 2 and Chapter 7: Engagement Quality Review.
Engagement Manager	Responsible for managing the delivery of the audit and project management. Supports the Engagement Director in: setting the overall audit strategy; assessing materiality for the audit; determining the required risk assessment procedures; and developing the audit plan, with assistance from the Engagement Team-Leader. Develops the budget and audit protocols, supported by the Engagement Team-Leader; Supports and supervises the work of the Engagement Team-Leader on significant risks and complex or judgemental areas; Ensures quality through performing detailed first-stage review.
Engagement Team-Leader	Day to day project management of team delivering the project plan and monitoring of progress. Embedding quality through supervision (and some first-stage review where delegated with agreement of Engagement Director) of the work of the team, such that the team:

	carries out the audit plan in accordance with NAO policies and procedures ensures that all work is conducted to an acceptable quality, before first-stage review, this may or may not be through a review of work remains independent and objective in the work they are performing identifies and acts on any potential conflicts of interest which may impede on the independence or perceived independence of the engagement team Identifying potential additional risks as the audit work progresses. Usually will perform testing on significant risks and other complex or judgemental areas. Providing appropriate desk training to all team members to enable individuals to undertake the allocated assignment to professional standards. This includes briefing, liaison and examining their work as appropriate. Ensuring key judgements and decisions are documented by team members ready for review, and to support the conclusions and proposed opinion.
Other engagement team members	All team members have an individual and collective responsibility for embedding quality within each assignment. This includes being aware of the objectives of the assignment and assigned tasks, reaching informed judgements based on the evidence, communicating key issues to the Engagement Team-Leader, and documenting the decisions and judgements in the Apex audit file. Raising immediately with line management any conflicts of interest which may impede on their independence, or perceived independence of the engagement team.

Review

5.10 All audit and assurance work should be subject to quality review processes which meet the requirements of ISQMs (UK) and ISAs (UK), as applicable.

5.11 The Engagement Director should take responsibility for reviews being performed in accordance with the NAO's review policies and procedures.

5.12 The NAO's procedures for review include:

- two-stage review of audit work to support the outputs of audit and assurance engagements;
- the use of central technical advice and support provided by FAPQ;
- consideration of specific matters by Audit Panels; and
- the appointment of Engagement Quality Reviewers for high-risk audits of financial statements.

5.13 The two stages of review are:

- First-stage review (detailed review) – this involves considering individual audit procedures and working papers.
- Second-stage review (overall review) – this involves review of key planning and completion documents as well as any other procedures or working papers considered appropriate.

5.14 The Engagement Director need not review all audit documentation. As required by ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation*, the Engagement Director should document the extent and timing of the reviews. This can be done using the reviewer sign-off functionality in Apex. In some circumstances, it may be appropriate to supplement the record of Apex sign-offs with a note summarising the extent of Engagement Director or other reviews.

5.15 ***Consultation required*** Apex is the NAO's audit documentation package which must be used for all engagements. Where teams wish to make alternative arrangements for audit documentation, they must consult with FAPQ.

5.16 In accordance with paragraph 31 of ISA (UK) 220 (Revised July 2021), as a minimum, the Engagement Director should review audit documentation relating to:

- significant matters, as defined in paragraphs 8(c) and A8 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) – examples of such matters include:
    - matters that give rise to significant risks;
    - results of audit procedures indicating:
        - that the financial statements could be materially misstated; or
        - a need to revise the auditor's previous assessment of the risks of material misstatement and the auditor's responses to those risks;
    - circumstances that cause the auditor significant difficulty in applying necessary audit procedures;
    - findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter paragraph in the auditor's report; and
    - concerns about the entity's ability to continue as a going concern;
- significant judgements, including those relating to difficult or contentious matters identified during the audit engagement, and the conclusions reached (this includes the relevant examples given in paragraph A92 of ISA (UK) 220 (Revised July 2021)); and
- other matters that, in the Engagement Director's professional judgment, are relevant to the Engagement Director's responsibilities.

5.17 In accordance with paragraph 32 of ISA (UK) 220 (Revised July 2021), on or before the date of the C&AG's audit certificate or report, the Engagement Director should determine, through a review of the audit documentation and discussion with the engagement team, that sufficient appropriate audit evidence has been obtained to support the conclusions reached and for the C&AG's audit certificate or report to be issued. Paragraph 40 of ISA (UK) 220 (Revised July 2021) requires that, prior to dating the auditor's report, the Engagement Director, as engagement partner, should determine that they have taken overall responsibility for managing and achieving quality on the audit engagement. In doing so, the Engagement Director should determine that:

- the Engagement Director's involvement has been sufficient and appropriate throughout the audit engagement such that the Engagement Director has the basis for determining that the significant judgments made and the conclusions reached are appropriate given the nature and circumstances of the engagement; and
- the nature and circumstances of the audit engagement, any changes thereto, and the NAO's related policies or procedures have been taken into account in complying with the requirements of ISA (UK) 220 (Revised July 2021).

5.18 All audit procedures (including Apex embedded forms, Workflow Steps, Risk Assessments and Audit Responses) must be reviewed. This is evidenced by the reviewer using the Review functionality in Apex. However, the extent of that review should reflect their professional judgement of the required level of review, reflecting the risks associated with the engagement and its performance. It is not necessary to mark individual attachments as reviewed within Apex; the review documented on individual Workflow Step Items, Risk Assessments, Audit Responses and Audit Forms is considered to extend to the attachments to that item. If the Engagement Manager or Engagement Director wishes to further clarify the extent of their review, they may add a Comment within the Review step or else add further description within the 'Engagement Director Conclusion' Audit Response on how the direction, supervision and review of the audit has been undertaken.

5.19 Where an audit is contracted-out, the NAO employee acting as Engagement Director continues to be the "Engagement Partner" for the requirements of the ISAs (UK). Section 10: Contracted-out work provides more details about the review roles in such engagements.

5.20 Where a new Engagement Director takes over the audit during the course of the engagement, they apply the review procedures described in paragraph 31 of ISA (UK) 220 (Revised

July 2021) to review the work performed to the date of a change in order to assume the responsibilities of the Engagement Director.

5.21 First-stage review is the responsibility of the Engagement Manager although elements of first-stage review may be delegated to the Engagement Team-Leader. Responsibilities should be agreed and documented at the planning stage to ensure that sufficient appropriate review is completed, but not duplicated.

5.22 It is expected to be extremely rare that it is appropriate to delegate responsibility for first-stage review of work in respect of significant documentation matters.

5.23 It is a matter of professional judgement whether an issue is a significant documentation matter, but as discussed in other Chapters and indicated in paragraph A8 of ISA (UK) 230 (Revised June 2016) (Updated May 2022), they include:

- Financial Statements-level significant risks.
- Assertion-level significant risks.
- Results of audit procedures indicating that the financial statements could be materially misstated.
- Results of audit procedures indicating that there may be a material irregularity.
- Results of audit procedures indicating a need to revise our assessment of the risks of material misstatement and our planned audit procedures.
- Significant difficulties in applying necessary audit procedures.
- Findings that could result in a modification to the audit opinion or the inclusion of an Emphasis of Matter paragraph in the C&AG's certificate.
- Concerns about the entity's ability to continue as a going concern.

5.24 Regardless of any delegated elements of first-stage review, before confirming that first-stage review is complete and that it supports the conclusions reached, the Engagement Manager should be satisfied that:

- an appropriate level of review has been performed; and
- they have a sufficient understanding of the engagement as a whole to be able to satisfy themselves with the conclusions reached and judgements taken.

First-stage review

Table 5B: Audit planning (first-stage review)

Responsibilities	Actions
To confirm that: • the audit plan reflects the Overall Audit Strategy set by the Engagement Director; • the audit plan reflects our understanding of the entity and the results of our risk assessment procedures; • the proposed approach is consistent with NAO policy and ISAs (UK); • the Engagement Director's attention is drawn to any significant changes that impact on the audit approach; and • findings from previous quality assurance processes have been appropriately reflected in the plan.	Before commencing review, an Engagement Manager should familiarise themselves with the prior financial statements and/or the latest management accounts. The subsequent review may include: • Checking that all required enquiries have been made. • Confirming that all risk assessment procedures have been completed in line with the FAM and that any newly identified risks, changes to Financial Reporting Activity scoping or our assessment of Generic Inherent Risk Factors have been raised with the Engagement Director. • Confirming all significant prior year judgment have been brought forward and re-assessed.

	• Checking that the Risk Assessment in Apex reflects the agreed procedures.
	• Ensuring that the Risk Assessment in Apex is complete.
	• Checking that the planned audit procedures are appropriate, including that:
	  • responses to significant risks are specific enough to address the risk;
	  • any planned testing provides assurance over the relevant risks of material misstatement; and
	  • where there are risks of material misstatement which are not included within the Content Library or risks of material misstatement which will not be addressed by the standard responses, these have been considered and FAPQ has been engaged to discuss bespoke content.

Table 5C: Audit fieldwork (first-stage review)

Responsibilities	Actions
To confirm that: • the audit work has been carried out in accordance with the plan, ISAs (and NAO financial audit policy) • either the original planning assumptions remain appropriate, or that where our risk assessment or other circumstances have changed, the audit approach has been amended appropriately • the working papers adequately document the work performed, particularly where we have exercised professional judgement and scepticism, and that they provide the basis for the conclusions expressed in the proposed audit opinion • that appropriate consultations have taken place and the results are documented • issues raised by the Engagement Manager, Engagement Director (and Engagement Quality Reviewer and Pre-Certification Reviewer if relevant) have been appropriately resolved • the objectives of the audit have been achieved; and the conclusions are consistent with, and supported by, the work performed.	When reviewing work, ensure • That there is a clear documented link from the final accounts figure in the accounts the tested populations on file. Tested populations should be fully reconciled to the accounts. • That materiality been updated for the latest set of accounts. • Any audit findings that indicate a change to the audit plan have been properly considered. • That the overall conclusion on significant risks is supported by the testing, which is logically documented on file. • Any controls testing supports the planning assumptions: i.e., which risks of material misstatement are covered. • That analytical procedures comply with the ISA, including: *that tolerable differences have been calculated correctly,* *that the source data has been verified,* *that any audited entity explanations have been considered in line with our understanding of the business and other testing.* • That sample sizes have been correctly derived. • The sample populations all reconcile back to the trial balance. • That all errors have been assessed and where relevant extrapolated.

Table 5D: Annual report and financial statements (first-stage review)

Responsibilities	Actions
To confirm that: • the engagement team has checked that the amounts disclosed and assertions implicit in the financial statements are consistent with the audited entity's accounting records and accounting policies, and are supported by the audit work; • the financial statements have been properly prepared in accordance with the governing legislation and relevant financial reporting framework; and • the financial statements are consistent with any other information to be published with them and our understanding of the audited entity's business.	Read the draft financial statements and annual report, including the governance statement. Do this as soon as they become available. Check the file to ensure that the latest disclosure checklist has been completed and all substantive matters resolved. Obtain the Director's review comments and ensure that these are followed up with the audited entity on a timely basis.

Table 5E: Reporting (first-stage review)

Responsibilities	Actions
To confirm that: • the audit certificate/report is in line with ISA (UK) 700 (Revised November 2019) (Updated May 2022) and NAO guidance and is appropriate to the circumstances and conclusions of the engagement; and • all relevant matters are reported to those charged with governance.	Review the draft audit certificate to ensure it is in line with the latest template and make sure that the audited entity has the latest copy. Confirm any amendments or modifications with FAPQ. Talk both to your team and review the significant areas of the audit file in conjunction before the Audit Completion Report and Management Letter are drafted, to ensure judgements and findings are accurately reflected.

Second-stage review

Table 5F: Audit planning (second-stage review)

Responsibilities	Actions

Review and approve the overall audit plan. This consists of:
• reviewing the matters listed in paragraph A92 of ISA (UK) 220 (Revised July 2021) which relate to planning, including:
  • matters related to planning the engagement, such as matters related to determining materiality.
  • the composition of the engagement team, including personnel using expertise in a specialised area of accounting or auditing and the use of personnel from service delivery centres;
	When leading the Overall Audit Strategy meeting, challenge the risk assessment and key planning assumptions.
	
	When reviewing the file:
	• check minutes of key planning meetings, particularly the Overall Audit Strategy and Stand Back Memo, to ensure all matters are appropriately documented; and
	• check the Risk Assessment in Apex to ensure that the risk assessment and responses are appropriate at the financial statement and assertion level.

• the decision to involve an auditor's expert, including the decision to involve an external expert; • the engagement team's consideration of information obtained in the acceptance and continuance process and proposed responses to that information; and • the engagement team's risk assessment process, including situations where consideration of inherent risk factors and the assessment of inherent risk requires significant judgment by the engagement team. • For group audits, the Group Engagement Director should additionally review the proposed overall group audit strategy and group audit plan and decisions about the involvement of component auditors, including how to direct and supervise them and review their work, including, for example, when there are areas of higher assessed risk of material misstatement of the financial information of a component. • considering the engagement risk and ensuring any remedial actions are in place • setting the Overall Audit Strategy • confirming that the overall nature, extent and timing of the planned procedures is appropriate in the light of the risk assessment procedures performed (this does not need to include a detailed review of planned procedures but rather confirmation of the overall approach) • confirming that adequate risk assessment procedures have been performed to form the audit plan, including: • those required to obtain an understanding of the matters in paragraph 10-2 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) that provide an appropriate basis for the identification of events or conditions that, individually or collectively, may cast significant doubt on the entity's ability to continue as a going concern; and whether or not a material uncertainty related to going concern exists;	Engagement Directors may choose to hold a meeting with the engagement team to discuss and challenge the audit approaches planned in the Risk Assessment in Apex. It is recommended that this forms an integral part of the stand-back assessment. Discuss the risk assessment with the Portfolio Director to confirm the level of involvement in the delegated audit.

• those required by paragraphs 17 to 25-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) to obtain information for use in identifying the risks of material misstatement due to fraud; and • approving any significant changes to the audit approach as the audit progresses.	

Table 5G: Audit fieldwork (second-stage review)

Responsibilities	Actions
The Engagement Director must be satisfied that: • adequate first stage has been carried out and that the audit work supports the conclusions reached; • all major review points have been addressed before the audit is signed off as complete; and • all errors have been assessed and, along with all significant matters, reported to those charged with governance. The Engagement Director should review the matters listed in paragraph A92 of ISA (UK) 220 (Revised July 2021) which relate to fieldwork, including: • the engagement team's consideration of related party relationships and transactions and disclosures; • results of the procedures performed by the engagement team on significant areas of the engagement, for example, conclusions in respect of certain accounting estimates, accounting policies or going concern considerations; • the engagement team's evaluation of the work performed by experts and conclusions drawn therefrom. • For group audits, the Engagement Director should additionally review the evaluation of work performed by component auditors and the conclusions drawn therefrom.	Second-stage review should include: • reviewing the work on significant risks; • reviewing work on significant estimates; • reviewing any significant judgments; • (where applicable) reviewing work on the Statement of Outturn against Parliamentary Supply; • other areas which are material by nature, such as the remuneration report and regularity testing; and • all tests within the 'Audit conclusions' Audit Response Group. The second-stage reviewer should also perform a risk-based review of the rest of the audit file to ensure: • adequate first-stage review has been performed • all major review points have been addressed • the objectives of the audit have been achieved • the conclusions are consistent with, and supported by, the work performed • that significant matters, including significant risks and other matters of material significance to the audit, are recorded on file (significant matters will include consultation with experts and FAPQ); • that key matters in issues logs or similar have been appropriately dealt with.; and • that any review points are cleared.

Table 5H: Annual report and financial statements (second-stage review)

Responsibilities	Actions
To confirm that: • the annual report, including the governance statement, is consistent with the financial statements; and	• Review the draft annual report and accounts as one document in order to ensure consistency.

• the financial statements are in line with the appropriate financial reporting framework.	• Confirm that the disclosure guide has been completed and all material issues resolved. • Using judgement, ask questions of the team about key balances, movements and anything else which looks unusual.

Table 5l: Reporting and conclusions (second-stage review)

Responsibilities	Actions
To confirm that: • the audit certificate/report is clearly expressed, conforms to the ISAs and the relevant NAO guidance, and is appropriate to the circumstances of the engagement; and • the report to those charged with governance is appropriate in the circumstances. The Engagement Director should review the matters listed in paragraph A92 of ISA (UK) 220 (Revised July 2021) which relate to audit conclusions, including: • how matters affecting the overall audit strategy and audit plan have been addressed; • the significance and disposition of corrected and uncorrected misstatements identified during the engagement; and • the proposed audit opinion and matters to be communicated in the auditor's report, for example, key audit matters, or a 'Material Uncertainty Related to Going Concern' paragraph.	• Read the final draft audit certificate, particularly in the version in the final signed accounts. Make sure it agrees with the relevant template. • Where the accounts may be issued with a modified opinion, engage with the FAPQ early in the process.

Chapter 6: Technical support and consultation

Relevant standards and guidance

6.1 Paragraphs 31(d) and A79 to A81 of ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* include requirements for the audit firm to establish quality objectives such that consultation on difficult or contentious matters is undertaken and the conclusions agreed are implemented.

6.2 Paragraphs 35 and A99-A102 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* include requirements for the engagement team to undertake appropriate consultation and implement the conclusions from this consultation.

6.3 Page 20 of the Financial Reporting Council's Professional Judgement Guidance (June 2022) includes guidance on the role of consultation in making professional judgements.

Consultation

6.4 In accordance with paragraphs 35(a) and 35(b) of ISA (UK) 220 (Revised July 2021), the Engagement Director is responsible for ensuring that appropriate consultation takes place on difficult or contentious matters, matters on which the NAO's policies or procedures require consultation (see ***Table 6A*** and ***Table 6B***); and other matters that, in the Engagement Director's professional judgement, require consultation; and for determining that members of the engagement team have undertaken appropriate consultation during the audit engagement, both within the engagement team, and between the engagement team and others at the appropriate level within or outside the NAO. The Engagement Director and Engagement Manager should ensure that sufficient resources are available within the engagement team to enable appropriate consultation to take place.

6.5 In accordance with paragraph 35(c) of ISA (UK) 220 (Revised July 2021), when there has been consultation outside the engagement team (whether with FAPQ or from other sources), the nature and scope of, and conclusions resulting from, such consultations should be documented and agreed by both the individual seeking consultation and the individual consulted.

6.6 In accordance with paragraph 35(d) of ISA (UK) 220 (Revised July 2021), the Engagement Director is responsible for ensuring that conclusions resulting from consultations are implemented and documented on the audit file.

6.7 As per paragraph A100 of ISA (UK) 220 (Revised July 2021), effective consultation on significant technical, ethical and other matters requires those consulted to:

- be given all the relevant facts that will enable them to provide informed advice; and
- have appropriate knowledge, seniority and experience.

6.8 The first line of advice for engagement teams on general technical areas of matters or significant judgement will normally be through the engagement team up to and including the Engagement Director. Engagement Directors may wish to consult with FAPQ and must do so in particular circumstances as described in ***Table 6A*** later in this Chapter.

6.9 Paragraph 35(c) of ISA (UK) 220 (Revised July 2021) requires that the Engagement Director be satisfied that the nature and scope of consultations on difficult or contentious matters are agreed with the party consulted. The engagement team should therefore obtain the Engagement Director's agreement to the nature and scope of a consultation request before it is issued – this is evidenced

through the Engagement Director's being automatically copied into all Consultations raised within Apex on their engagements.

6.10 **Consultation required** Where ethical matters are identified, a team member may wish to discuss the issue outside the engagement team or their line management. This is an exception to the normal consultation practice. In such cases, team members must consult the Director, Audit Risk and Compliance or HR.

6.11 **Consultation required** In all cases where a modification to an audit opinion is a consideration or a substantive C&AG's report is possible, FAPQ must be consulted. Consultation should occur at an early stage of the issue developing so that full consideration can be given.

6.12 **Consultation required** If an opinion is modified, the certification journal must include a minute from the Director, Audit Quality or a named deputy confirming that appropriate consultation has taken place and that if necessary, an audit panel has convened and agreed on the recommended opinion. Specialist expertise may be required during an audit, for example where there are specialised or unusual transactions, or where management experts have been used. This may not be available within the engagement team. FAPQ can provide or access specialist advice on a wide range of technical areas, both within the NAO and from external sources. Any referral of technical matters to external experts or audit firms must be made through FAPQ.

Consultation with FAPQ and others

6.13 The Financial Audit Practice and Quality team act as the first point of contact for consultation on technical matters during the course of an audit. FAPQ may be contacted via either the Consultation functionality in Apex (for consultations pertaining to a specific engagement) or the Financial Audit Support Tool (FAST) (for other queries).

6.14 **Consultation required** Engagement teams must consult with FAPQ, the Director, Audit Quality or others as indicated in the 'Consult' column, where any of the circumstances included in ***Table 6A*** arise.

Table 6A: Circumstances when engagement teams must consult with FAPQ or others as indicated

FAM paragraph	Consult	Matter
Compliance with standards		
2.4	FAPQ	Any apparent conflict between the requirements of the FAM and ISAs (UK) and/or Practice Note 10 (Revised 2022).
2.11	FAPQ	The engagement team considers that reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient in the circumstances for the purpose of reporting to the intended users of the financial statements.
2.12	FAPQ	An objective in a relevant ISA (UK) cannot be achieved and the engagement team's evaluation under paragraph 24 of ISA (UK) 200 (Revised June 2016) (Updated May 2022) has concluded that this prevents them from achieving the overall objectives of the auditor.
2.35	FAPQ	The engagement team judges it necessary to depart from a relevant requirement in an ISA (UK).
4.44	FAPQ	Findings indicate that there is an engagement(s) for which procedures required were omitted during the performance of the engagement(s) or the report issued may be inappropriate.
Disagreements		

4.83	Director, FAPQ	Complaints on the standard of audit work from audited entities that are not satisfactorily resolved by the Engagement Director and client lead.
4.85	Director, FAPQ	Conflicts of opinion between audit staff and Engagement Directors.
4.86	Director, FAPQ	An Engagement Quality Reviewer or Hot Reviewer or person undertaking another peer review disagrees with the Engagement Director.
6.36	FAPQ	A substantive difference of opinion arises between the engagement team and the Engagement Quality Reviewer or individuals performing activities within the NAO's system of quality management other than FAPQ.
7.29	Director, FAPQ	The EQR has concerns that the significant judgements made by the engagement team, or the conclusions reached thereon, are not appropriate, and such concerns are not resolved to the EQR's satisfaction.
Ethical considerations		
4.62	Ethics function and/or Chief People Officer	An engagement team member becomes aware of circumstances or relationships which may, or could be perceived to, create a threat to their independence or objectivity as a member of the engagement team.
4.65	FAPQ	Matters come to the Engagement Director's attention through the NAO's system of quality control or otherwise that indicate that relevant ethical requirements applicable to the nature and circumstances of the audit engagement have not been fulfilled.
6.10	Director, Audit Risk and Compliance or HR	Ethical matters are identified and a team member wishes to discuss the issue outside the engagement team or their line management.
7.22	Ethics function	The nature and extent of engagement team discussions with the EQR or EQR Assistant(s) about a significant judgement give rise to a threat to the objectivity of the EQR or EQR Assistant(s).
8.32	Ethics function	Potential breaches of the FRC Ethical Standard are identified.
8.36	Ethics function	Any key judgements concerning ethical matters.
8.36	C&AG, or Executive Director in C&AG's absence	More judgemental and high-risk assessments concerning ethical matters or those which involve conflicts held by Executive Directors.
8.38	Ethics function	The Engagement Director disagrees with judgements or safeguards communicated by the Ethics Function in response to conflicts of interest or ethical issues.
8.40	Ethics function	The Engagement Director is unable to introduce suitable safeguards to reduce the threat to independence arising from an ethical issue to a suitable level.
8.68	Line manager, Group People Development Director, Chief People Officer and Director, Audit Risk and Compliance or Director, Value for Money Practice and Quality	Audit staff are considering applying for a role with any NAO audited entity they have worked on within the last two years; are currently performing work on; or expect to be allocated to in the current audit cycle,.

8.69	Line manager, Group People Development Director, Chief People Officer and Director, Audit Risk and Compliance or Director, Value for Money Practice and Quality	Any potential employment with an entity audited by the NAO by staff in grades at and above Audit Manager/Band 1, and colleagues responsible for managing projects and engagements.
8.70	Line manager, Group People Development Director, Chief People Officer and Director, Audit Risk and Compliance or Director, Value for Money Practice and Quality	Any probable employment with an entity audited by the NAO by staff in grades below Audit Manager/Band 1.
8.75	Ethics function	Individuals within any of the following position are former employees of the NAO and consultation with the Ethics Function has not already occurred: • A key management position at the entity, where they can influence the strategic or operational decision making of the entity. • Audit committee member. • Director of the entity (or equivalent). • Member of the entity's management board (or equivalent). Consultation is not required for staff below Director level who have been promoted to more senior levels in the audited entity, or other ex-NAO staff members who left the NAO over two years ago, unless the Engagement Director considers there to be a threat and is in doubt as to the action they should take. The audit file should document the audit team's assessment supporting the decision not to consult.
8.79	Ethics function	The C&AG leaves the NAO to take up a senior position at an NAO audited entity (responsibility to consult rests with the Engagement Director for the audit of the entity concerned).
8.82 8.86	Ethics function	The Engagement Director or a person closely associated with them or a 'close family member' becomes aware that either they or a closely associated person have either: • acquired a financial interest in; or • entered into a business relationship with an audited entity or the Engagement Director is in doubt as to the action they should take in relation to declarations made by a member of their team.
8.85	Engagement Director, HR and Director, Audit Risk and Compliance	Arrears exist on any loans made by an audited entity, its parent body or the audited entity's subsidiaries to a covered person or a person closely associated with them.

8.89	Group Executive Director	Secondments to audited bodies.
8.90	Group Executive Director	Inward secondments from audited bodies and their connected bodies.
8.95	Ethics function	The Engagement Director becomes aware that a person closely associated with them becomes employed in a position at an audited entity where they can influence the accounting records or financial statements or other subject matter information or subject matter of such an engagement.
8.115	Ethics function	There is any doubt as to the acceptability of gifts, favours or hospitality offered to the Engagement Director, or the Engagement Director has any residual doubt about the acceptability of gifts, favours or hospitality to other individuals.
8.120	Ethics function	Fee deficit or over-recovery is over 50% of the audit fee.
8.121	Ethics function	Fees for any additional or non-audit services performed by the NAO that are provided to an audited entity and its group exceed the statutory audit fee charged to the audited entity for the year.
8.122	Ethics function	Audit fees from an individual audited entity and its subsidiary bodies or a collection of entities with the same beneficial owner or controlling party (which is not a corporate holding entity) exceed 5% of the NAO's total audit fee income (approximately £1,000,000) on a regular basis.
8.126	Ethics function	There is outstanding litigation or legal matters between the NAO and an audited entity and the Engagement Director is uncertain as to whether this poses a threat to integrity, objectivity and independence.
8.125	Ethics function	The audit fee charged is likely to be less than 50% of projected audit costs.
8.135	Ethics function	A management threat is identified in connection with the provision of non-audit services or advice or support provided to the audited entity. These services need to be approved by the Ethics Function before the work is agreed to.
8.151	Ethics function	The Engagement Manager and Engagement Director have determined it would be inappropriate in the circumstances to provide assistance to an audited entity, or safeguards have been put in place.
8.168	Ethics function	Contractor audit firms are providing, or propose to provide, any of the non-audit services listed in Section 5 of the Ethical Standard to audited bodies. Contractor audit firms are required to report these services directly to FAPQ on a quarterly basis or provide a nil return, but engagement teams should nevertheless notify these to FAPQ where they become aware of them.
8.173	NAO's independent non-executives	In the case of a Public Interest Entity audit, any instances where the person consulting and the Ethics Function disagree on the appropriate action in response to an ethical matter and it is ultimately concluded that the Ethics Function's advice should not be followed.
8.162	Ethics function	Any significant facts or matters arise that bear upon the auditor's objectivity and independence (including in relation to any services or support other than statutory audit) or any inconsistencies between the Ethical Standard and the entity's policy on the supply

		of non-audit services, or any apparent breach of that policy, which the engagement team is required to communicate in writing to those charged with governance.
Resources		
12.25	FAPQ	There is a need to change the designation of Key Audit Partner (regardless of grade) during an engagement, except changes of Key Audit Partner external to the NAO.
15.70	Financial Audit Operations	The Engagement Director determines that Human resources assigned or made available are insufficient or inappropriate in the circumstances of the audit engagement.
15.70	FAPQ	The Engagement Director determines that Technological or Intellectual resources assigned or made available are insufficient or inappropriate in the circumstances of the audit engagement.
Engagement acceptance and scope		
3.22	FAPQ	Engagement teams preparing to undertake a new international engagement.
4.69 9.33	Director, FAPQ	The Engagement Director obtains information that would have caused the NAO to decline the audit engagement had that information been available earlier and had the option of declining the engagement been available.
9.14	Director, FAPQ	An outgoing auditor on an agreement (non-statutory) audit engagement provides reasons why a new assignment should not be accepted.
9.49	FAPQ	The Engagement Director proposes to agree non-standard terms of engagement (including where management seeks the inclusion of a non-standard term or clause in a letter of understanding or letter of engagement) or there are judgements as to whether the preconditions for an audit are met.
9.51	FAPQ	Management seeks to amend the terms of the engagement during the course of the engagement.
9.57	FAPQ	The engagement team proposes not to re-accept an engagement or the NAO otherwise ceases to hold office as statutory auditor of an audited entity.
10.8	FAPQ	None of the proforma audit certificate/report templates are relevant to the circumstances of a particular entity, or significant changes or customisations to the templates are required.
10.20 42.11 42.70 42.73 42.78	FAPQ	A regularity opinion is requested by the entity either through management or those charged with governance, or by the entity's sponsoring Department in support of their own regularity opinion, or the entity is a company and so the engagement team needs to consider whether a regularity opinion should be provided.
10.28	FAPQ	The NAO is asked to carry out a specific engagement designed to fulfil a particular purpose, other than the audit of a full set of entity financial statements.
46.75 ***Table 54B*** (row covering the Opinion on financial statements and paragraphs 23 to 27 and A22	FAPQ	An assignment is proposed that falls outside the ISAs.

to A31-1 of ISA (UK) 700)		
Documentation		
5.2 5.15 14.13	FAPQ	It is not considered appropriate to conduct an audit within the Apex environment and the engagement team wishes to make alternative arrangements for audit documentation.
14.14	FAPQ	The engagement team intends to adopt for the first time an arrangement whereby audit documentation is spread between more than one Apex Audit Engagement.
Materiality, performance materiality and the trivial threshold		
16.4	FAPQ	The Engagement Director wishes to set materiality outside of the ranges 0.5% to 2% of gross expenditure/turnover or gross assets and 5% to 10% of surplus or profit.
16.12	FAPQ	The engagement team plans on basing the materiality benchmark on a rolling basis over a number of years to eliminate volatility.
16.51	FAPQ	The audit team wishes to set a clearly trivial threshold in excess of £300,000 and there is no existing agreed exemption from the cap.
Risk assessment and response planning		
17.75	FAPQ	Responses to significant RoMMs that will use data analytics.
17.99	FAPQ	Where there is an expectation of material misstatement and the objective of audit procedures is to obtain reasonable assurance over the size of the misstatement in the financial statements.
17.166	FAPQ	As a result of the risk assessment process there are doubts about the entity's auditability.
40.16	FAPQ	The NAO Engagement Director considers that an Engagement Quality Review is required on a contracted-out audit.
45.12	FAPQ	An existing audited entity has become a Public Interest Entity.
IT complexity		
Table 17F	IT audit specialists	The overall assessment of IT complexity for one or more Financial Reporting Activities (FRAs) is High. The overall assessment of IT complexity for one or more FRAs is Medium or Low, but at least one of the following individual assessments has been made on the FRA: • High complexity third party hosting or outsourcing; and/or • High or Medium complexity use of emerging technology; and/or • High complexity IT environment changes/data conversions. The overall assessment of IT complexity for one or more FRAs is Medium, there are IT-dependent controls addressing RoMMs with a Financial Statement Impact (magnitude) and/or Likelihood placement of High and at least one of the following is the case: • there are more than 5 privileged users; and/or • there are fewer than 5 privileged users but the level of access provided to these users is not appropriate; and/or • there is heightened risk from IT change and the design of the IT change policy is inadequate. The engagement team plans to test the operating effectiveness of IT-dependent controls.

Regularity risk assessment and response planning		
18.71	FAPQ	The Group Engagement Team is unable to obtain right of access to a component entity or other sources of appropriate evidence to support the group regularity opinion, such that there may be a limitation of scope on the audit.
18.77	Legal and Policy team	An entity has either refused to obtain legal advice concerning a judgement as to whether a transaction complies with the entity's framework of authorities or the legal advice obtained by the entity is unclear, and the engagement team wishes to obtain a separate legal opinion on the matter.
18.87	FAPQ	Any lack of, or inadequate disclosure of, additional requirements for disclosure in the financial statements in respect of regularity introduced by the entity's framework of authorities or financial reporting framework.
42.123 43.66	FAPQ	A trading subsidiary makes gift aid payments which exceed its profits available for distribution and therefore constitute unlawful distributions.
Evidence assessment and evaluation		
20.12	One or more of: an auditor's expert; Centres of Expertise; FAPQ; and/or the Engagement Quality Reviewer	Where consultation is required by the procedures set out in Apex content or by the FAM or otherwise agreed with the Engagement Manager or Engagement Director.
20.13	FAPQ	The audit evidence obtained is not sufficient or appropriate to meet the requirements of an Apex Audit Response and the engagement team is unable to resolve the issue through discussion with management.
20.23	FAPQ	The auditor does not have a sufficient basis with which to consider the relevance and reliability of information from an external information source and sufficient appropriate audit evidence cannot be obtained through alternative procedures.
Going concern		
27.36	FAPQ	Management or those charged with governance do not provide sufficient information about the audited entity's ability to continue as a going concern or is unwilling to make or extend its assessment when requested to do so by the auditor.
27.52	FAPQ	The engagement team judges that the going concern basis is appropriate for the preparation of a public sector entity's financial statements substantially on the basis of third-party confirmations received from the department or executive body responsible for providing financial backing, and the engagement team considers that this is a matter of such significance that the confirmations are referred to in the financial statements and in the audit certificate or report as being relevant to a proper understanding of the basis of the opinion.
27.57	FAPQ	The engagement team considers it necessary to request an external confirmation (including of terms and conditions) from a third party external to government and to obtain evidence of their ability to provide support to management's plans for future actions and/or the audited entity's ability to continue as a going concern.

27.62	FAPQ	An audited entity ceases to exist and prepares its final set of financial statements, and it is considered necessary for the C&AG to report to Parliament on the distribution of assets and liabilities.
27.70	FAPQ	The auditor is required under paragraph 17-2 of ISA (UK) 570 (Revised September 2019) to consider the implications for the opinion of being unable to obtain sufficient appropriate evidence regarding going concern.
27.71	FAPQ	The audited entity's going concern status is complex or there are significant concerns with respect to the financial sustainability of the services being delivered.
27.72 27.73	FAPQ	A material uncertainty related to going concern exists.
27.74	FAPQ	The financial statements have been prepared using the going concern basis of accounting but, in the auditor's judgment, management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate.
27.76 27.77	FAPQ	Management concludes that the going concern basis is no longer appropriate and needs to prepare the financial statements on an appropriate alternative basis.
42.91 43.40	FAPQ	A company or charity is insolvent but has been established by statute and therefore could not legally cease to operate.
Comparative information and previous audits		
N/A	FAPQ	The engagement team becomes aware of a possible material misstatement in the comparative information, and the NAO audited the prior period's financial statements. Such material prior period misstatements should be reported to FAPQ for information and tracking.
29.11	FAPQ	Where the NAO audited the prior period financial statements, information regarding a possible misstatement in the prior period financial statements becomes known to the engagement team that, had it been known to the engagement team at the date of the auditor's report, may have caused the engagement team to amend the auditor's report.
29.36	FAPQ	The engagement team is considering referring to a predecessor auditor's report in the opinion and is not prohibited by law or regulation from doing so.
Fraud, laws and regulations		
30.15 30.50	FAPQ	The engagement team has identified or suspects a fraud and the responsibilities for reporting to appropriate authorities outside the entity are unclear.
30.46 30.47	FAPQ	As a result of a misstatement resulting from fraud or suspected fraud, the engagement team encounters exceptional circumstances that bring into question the engagement team's ability to continue performing the audit.
30.83	FAPQ	The Engagement Director intends to apply simplified due diligence procedures as part of the audited entity acceptance and approval process.
30.100	MLRO	The engagement team considers that the actions they plan to take, or may be asked to take, will result in themselves committing a principal money laundering offence.
30.102	MLRO	Money laundering has been reported to the NCA and the engagement team considers that making the audit report may

		generate a risk of committing a principal money laundering offence.
30.103	MLRO	Continuing to act for the entity could itself constitute money laundering; for example, if it amounted to aiding or abetting the commission of one of the principal money laundering offences, or if it amounted to one of the principal money laundering offences itself, in particular the offence of becoming involved in an arrangement under the Anti-Money Laundering Legislation.
30.104	MLRO	The Engagement Director is considering resignation from the audit as an alternative to seeking appropriate consent from the National Crime Agency to continue the engagement.
30.105	FAPQ	It has been determined that it is necessary to withdraw from the engagement, especially in circumstances where it is not possible to do so.
30.106	FAPQ	It is known that money laundering has occurred and that management or those charged with governance were involved, and the Engagement Director considers it may be necessary to modify the audit report or include an emphasis of matter paragraph.
30.107	FAPQ and MLRO	The engagement team is considering including information in the auditor's report about any identified or suspected money laundering activities.
30.108	MLRO	Issuing an audit report in circumstances where money laundering has occurred, and timing is a crucial factor.
30.109	MLRO	A money laundering offence has been committed and information relevant to that offence is required to be shared with third parties to fulfil our regulatory responsibilities (for example, successor auditors or as part of the external monitoring regime).
30.112	MLRO	The engagement team is considering making a report regarding money laundering to the audited entity's supervisory authority.
31.30	FAPQ	The engagement team is considering withdrawal from the engagement, or, if not possible, reporting to those charged with governance and/or Parliament that the C&AG would withdraw from the engagement if he were able to do so.
31.35	FAPQ	The engagement team is required to consider the need to obtain legal advice; for example, where management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements either quantitatively or qualitatively, and where there is more than one occurrence both individually and in aggregate.
31.38	FAPQ	The engagement team intends to communicate identified or suspected non-compliance with law or regulation in the auditor's report.
31.44	FAPQ	The engagement team is required to report instances of non-compliance with laws and regulations directly to the relevant authority, where they no longer have confidence in the integrity of those charged with governance or where they are prohibited from reporting to those charged with governance by law or regulation.
31.45	FAPQ	The engagement team identifies matters which may be required to be reported to a relevant authority in the public interest.

31.57	FAPQ	The engagement team requests to use the Apex content that covers documentation requirements regarding identified or suspected non-compliance with laws and regulations.
31.62	FAPQ	Additional matters specified within the legislation or regulations which the particular entity applies may give rise to the need to report to the regulator.
31.65	FAPQ	The engagement team requests to use the Apex Audit Response Group that covers investigations undertaken in order to determine whether or not a matter is of sufficient material significance to the regulator.
31.70	FAPQ	The engagement team identifies the need to make a report to the regulator of a regulated entity.
31.79 43.66	FAPQ	Unlawful distributions are made by a company and the engagement team is considering whether this should be reported to the relevant authority in the public interest in accordance with ISA (UK) 250A (Revised November 2019).
31.84	FAPQ	The engagement team identifies instances of non-compliance with tax legislation and is considering whether this should be reported to the relevant authority in the public interest in accordance with ISA (UK) 250A (Revised November 2019).
42.151 43.60	FAPQ	For a regulated entity, there are relevant matters to report to the regulator in accordance with ISA (UK) 250B (Revised November 2019).
43.7	FAPQ	An audited entity is a charity regulated otherwise than under the Charities Act 2011; the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006; the Charities Act (Northern Ireland) 2008; and the (Republic of Ireland) Charities Act 2009.
43.64	FAPQ	The engagement team is in dispute with other firms – for example, the auditors of trading subsidiaries or contractor auditors – surrounding accounting judgments on the issue of gift aid payments from a trading subsidiary to a parent charity.
45.34	FAPQ and Legal and Policy team	A further understanding of a Public Interest Entity's (PIE) regulatory environment or the obligations placed upon engagement teams by the regulatory environment is required.
45.53	FAPQ	The engagement team has reported an actual or suspected irregularity (that is, an instance of non-compliance with laws and regulations, as distinct from irregular transactions for the purpose of the regularity opinion, which are transactions that are not in accordance with the framework of authorities) to management of a PIE but management has not taken any further action to investigate the irregularity.
54.24	MLRO	The engagement team identifies the possible existence of fraud which they consider could have a material impact on the financial statements and senior management are involved in the fraudulent activity.
Other information and other reporting responsibilities		
32.13	FAPQ	A material misstatement in the Other Information is identified and management does not propose to correct the misstatement.
32.26	FAPQ	Inconsistencies between other information in the annual report and the financial statements, or material misstatements of fact, are identified, revision of the other information is necessary and management refuses.

32.62	FAPQ	Disclosure of information about a significant internal control issue might prejudice the outcome of a special investigation (possibly preventing successful prosecution of a case of fraud or inhibiting a disciplinary case against members of staff) and the engagement team is not able to agree with the Accounting Officer how the matter should be resolved.
43.50	FAPQ	A charity proposes to include disclosures of senior remuneration within the body of the financial statements rather than in the other information.
Table 54B (row covering Other Information and paragraph 32 of ISA (UK) 700)	FAPQ	Matters may be required to be reported in the audit report in relation to a material uncorrected misstatement in the Other Information, or there is anything material to add or draw attention to in respect of the Other Information, or a modified opinion on the financial statements may have implications for the opinion to be provided on the Other Information.
Tests of detail and evaluating the results of procedures		
34.27 34.67	AMT	There are multi-location issues which affect the testing approach and/or extrapolation.
34.56	FAPQ	Audit evidence supporting a balance is at a date different to the period-end date.
34.70 52.31 52.36	FAPQ	There is potential for a scope limitation to the audit because either it has not been possible to quantify the error for an identified misstatement or additional testing has not reduced the Upper Error Limit below materiality.
34.86	FAPQ (AMT)	Approval of sample sizes that do not comply with the guidance in Chapter 34: Tests of detail.
Table 34I	AMT	Having extrapolated a sample, the Upper Error Limit is greater than materiality but the Most Likely Error and the Lower Error Limit are less than materiality.
Table 34I	AMT	Having extrapolated a sample, the Upper Error Limit and the Most Likely Error are greater than materiality but the Lower Error Limit is less than materiality.
Table 34I	FAPQ and AMT	Having extrapolated a sample, the Upper Error Limit, Most Likely Error and Lower Error Limit are all greater than materiality.
34.115	FAPQ (AMT)	The engagement team proposes to use an alternative statistical method such as Monetary Unit Sampling (MUS) (where other statistical methods may be required to gain substantive assurance or the engagement team believe the standard approach is disproportionate to the identified risk).
52.41	FAPQ (AMT)	When using stratified sampling, misstatements or irregular transactions are detected in several sub-populations.
52.44	FAPQ	The sum of unadjusted misstatements is within 5% of performance materiality. The nature of the consultation will be whether the materiality level for the account needs to be reassessed and whether additional work should be undertaken.
52.45	FAPQ	In the engagement team's opinion, the level of adjusted and unadjusted misstatements is such that it provides evidence of the quality of the control environment that may call into question the judgements made when calculating performance materiality.
52.61	FAPQ	The engagement team identifies irregular transactions that they consider may be material.

Controls testing		
35.89	Digital Financial Audit team	It is necessary to test general IT controls.
35.92	Digital Financial Audit team	The engagement team believes they may need to evaluate the design, implementation and operating effectiveness of indirect general IT controls or is uncertain whether this will be the case.
Accounting estimates		
36.17	FAPQ	In respect of an accounting estimate, alternative assumptions or outcomes exist that management does not appear to have considered, or information available to the engagement team suggests that management's estimate is not the most reasonable in all the circumstances, and management may be required to undertake additional work and/or the engagement team needs to consider the impact on the audit opinion.
36.27	FAPQ	In respect of an accounting estimate, the following circumstances apply: • management has not taken appropriate steps to understand or address estimation uncertainty; • the engagement team has requested management to perform additional procedures to understand estimation uncertainty or to address it by reconsidering the selection of management's point estimate or considering providing additional disclosures relating to the estimation uncertainty; • management's response to the auditor's request does not sufficiently address estimation uncertainty; and • after considering management's response, the engagement team determines that it is not practicable to develop an auditor's point estimate or range.
36.40	FAPQ	In making the 'stand back' evaluation required by paragraphs 33 and 34 of ISA (UK) 540 (Revised December 2018) (Updated May 2022), the engagement team is unable to obtain sufficient appropriate audit evidence.
36.47	FAPQ	There is very high estimation uncertainty in an accounting estimate arising from factors within the audited entity's control (for example, management does not have sufficiently good data and it is reasonable to expect them to have such data).
Financial instruments		
49.9	Financial Instruments Centre of Expertise	A material financial instruments balance: • is derived from a complex model(s) with an unusual underlying methodology (which questions its compliance with the relevant standards and industry best practice); or • is derived from significant management's judgements (for example, complex and material post model adjustments (PMAs) or valuation techniques for unlisted equity investments); or • relies on significant assumptions from third party sources (i.e., future macroeconomic assumptions over specific and specialist industries or sectors, such as energy markets); or • relates to an unlisted equity investment and uses unobservable inputs (Level 3 inputs, as defined in IFRS

		13 Fair value measurement) and complex valuation methods such as cost as a proxy, discounted cash flows, options valuations or comparable multiples; or • relates to expected credit losses (ECLs) where subjective assumptions are made around key elements of judgement including the credit risk, discount rates and the use of forward-looking data; or • is complex and the audit team requires support in assessing the control environment within the audited entity (for example, confirming the appropriateness of credit file reviews).
Computer-assisted audit techniques (CAATs)		
17.131 ***Table 37A***	FAPQ	The engagement team does not believe they will be able to use the most recent journals analytic tool for auditing journals (or it is efficient to review 100% of journal entries due to the size of the entity).
17.156	FAPQ	The engagement team does not believe they will be able to use the most recent GL-TB application to reconcile the general ledger to the trial balance and accounts.
37.12 37.20	DART, relevant IT audit or data specialists	The engagement team proposes to use CAATs other than approved AIMS Applications, including CAATs that involve macros, scripts or other forms of coding that have not been produced and approved by DART.
Other specific audit procedures		
37.90	FAPQ	Attendance at physical inventory counting is impracticable.
37.101	FAPQ	The engagement team considers they may need to may need to consult with the NAO's own legal counsel with respect to litigation and claims.
Service organisations and shared service centres		
46.44 46.55	FAPQ	The audit plan includes an expectation of the operating effectiveness of controls operated at a service organisation, a Type 2 ISAE 3402 report is available, there is a gap between the period covered by the Type 2 report and the period of account for the user entity and the engagement team is in doubt as to what procedures are required to bridge any gap between the periods covered.
Group audit procedures		
12.24	FAPQ	A material component of a group is not audited by the NAO (consultation on identifying the Key Audit Partner).
25.13	FAPQ	The engagement team involves other external auditors (not component auditors) in their work and is uncertain as to the applicability of ISA (UK) 600 (Revised November 2019) (Updated May 2022) or Chapter 25: Group audit procedures to their engagement.
25.38	FAPQ	The Group Engagement Team considers it impracticable to review the risk assessments for all components for which the Group Engagement Team expects to use the component auditor's work for the purpose of the group audit.
25.68	Component Manager for the Resources (financial audit)	The Group Engagement Team has concerns regarding the quality of work performed by a component auditor.

	component of the system of quality management (via FAST)	
25.90	FAPQ	The Group Engagement Team is unable to obtain or gain access to a component auditor's working papers for the purposes of the group audit.
25.101	FAPQ	For a significant component, the group engagement team is unable to request or secure the agreement of the component auditor to transfer relevant documentation during the group audit.
25.125	FAPQ	The Group Engagement Team requests group management to inform component management of any matter of which the Group Engagement Team becomes aware that may be significant to the financial statements of the component, but of which component management may be unaware, group management refuses to communicate the matter to component management and the matter remains unresolved after discussion with those charged with governance of the group.
Contracted-out work		
38.19	FAPQ (except that requests for specialist expertise relating to financial instruments should initially be directed to the Financial Instruments Centre of Expertise)	The engagement team considers they require expertise outside the areas covered by the Specialist Audit Services Framework.
38.23	Director, Audit Operations and Ethics function	Proposals by contractors to provide non-audit services to NAO audited bodies.
38.26	FAPQ	The Engagement Director wishes to accept and manage an actual or perceived conflict of interest relating to a contractor auditor.
39.17	FAPQ	The contractor auditor proposes to deviate from the standard NAO templates when preparing their shadow opinion and the deviation has not been previously agreed between FAPQ and the contractor firm.
40.17	FAPQ	For a contracted-out audit, the NAO Engagement Director considers they would consult FAPQ on a matter if the audit were performed by NAO staff, including where the contractor auditor or NAO Engagement Director are considering proposing a modified audit certificate or report.
40.19	FAPQ	Substantive differences arise between the NAO engagement team and the contractor auditor that cannot be resolved.
40.21	Director, Audit Operations and Director, FAPQ	Performance issues relating to a contractor auditor.
40.22	FAPQ	The NAO engagement team proposes to amend the scope of the contractor auditor's work such that the contractor auditor would be completing less than a full ISA-compliant audit (i.e., scoping out elements of the engagement).
Use of experts		

48.15	FAPQ or the relevant Centre of Expertise	Any of the factors in paragraph A8 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) are present.
48.15	FAPQ	The engagement team wishes to rebut the presumption that economic expertise will be engaged where management makes accounting estimates that involve multiple economic scenarios (such as may be required for expected credit losses), or there are barriers to the use of an auditor's expert in these circumstances.
39.18 48.55	FAPQ	The engagement team or a contractor auditor proposes to sign a "hold harmless" letter from a private sector internal auditor that does not include the wording in paragraphs 48.53 and 48.54.
48.56	FAPQ	The engagement team proposes to agree formal protocols for working with internal audit, such as those set out in ***Figure 48B***.
48.58	FAPQ	The engagement team proposes to agree to any restrictions on the C&AG's right of access to documentation.
49.13	FAPQ and those in the Financial and Risk Management Hub who are responsible for the Hub's work on fraud and error	The engagement team identifies a misstatement due to fraud or suspected fraud and is required under paragraph 33-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) to consider whether specialised skills or knowledge are needed to investigate this.
49.14	FAPQ	The engagement team has a need for expertise not covered by the sources described in Chapter 49: Obtaining internal expertise.
50.8 50.9	FAPQ	The engagement team has a need for external expertise not covered by the arrangements described in Chapter 50: Obtaining external expertise.
51.34	FAPQ	The engagement team is required by law or regulation to refer to the work of an auditor's expert in an auditor's report containing an unmodified opinion.
Parliamentary Supply		
41.40	FAPQ	The engagement team considers that modifications to the standard procedures included in the Apex content for Departmental accounts may be required to provide substantive assurance over the classification and regularity of transactions for SOPS purposes.
41.43	FAPQ	Breaches or potential breaches of a voted control total.
41.45	FAPQ	Unadjusted misstatements have been identified that, if adjusted, would cause an Excess Vote.
Written representations		
56.53	FAPQ	Management does not provide one or more of the requested representations and/or there are doubts about the integrity of management such that the written representations are not reliable and/or written representations are inconsistent with other audit evidence.
Concluding and reporting		
2.11	FAPQ	The engagement team considers that reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient in the circumstances for the purpose of reporting to the intended users of the financial statements.
6.11 27.69	FAPQ (including the Director, Audit	The engagement team is considering whether a modification to an audit opinion, an Emphasis of Matter paragraph, an Other Matter

30.44 41.27 54.14 54.47 55.22 55.45 58.3 58.13	Quality and an Audit Panel in some cases)	paragraph, a Material uncertainty related to going concern paragraph or a substantive C&AG's report may be required.
10.10 54.74	FAPQ	Unmodified Extended Auditor Reports.
45.60	FAPQ	Additional reports to the audit committee of a Public Interest Entity where the audit is contracted out or a two-tier or joint audit.
Table 10B	FAPQ	The engagement team is issuing a report under either ISAE 3000 or ISRS 4400.
53.25	Design and Publishing team	The NAO is responsible for laying accounts on behalf of the audited entity.
54.39	FAPQ	In exceptional circumstances, it is not possible for the engagement team to submit financial statements for pre-certification technical review by FAPQ on a timetable that will enable resolution of issues before the audited entity finalises the financial statements.
54.68	FAPQ	The engagement team encounters difficulties determining the audited entity's authorising legislation and/or financial reporting framework, or either of these are ambiguous.
59.6	FAPQ	The annual report and account is presented for audit solely in English and there is no legal requirement for the C&AG to report in Welsh or on the Welsh version of the annual report and account but the entity decides to translate the annual report and accounts into Welsh and includes the translated version of the audit certificate or report therein.
59.8	FAPQ	Either the audited entity provides the annual report and account for audit in both English and Welsh or only Welsh or legislation explicitly requires the annual report and account to be laid or published in Welsh (regardless of whether or not there is a complementary requirement to lay or publish in English).
Post-certification activities and subsequent events		
22.9	FAPQ	In exceptional circumstances, the engagement team does not consider it practicable to close the audit file within 20 working days.
22.29 60.26	FAPQ	The audited entity amends, or intends to amend, the published financial statements and a new or amended C&AG's certificate or report is proposed.
22.31	FAPQ	The audited entity amends, or intends to amend, the published annual report, even where this does not impact the financial statements, and a new or amended C&AG's certificate or report may need to be re-issued.
22.32	FAPQ	Management does not take the necessary steps to ensure that anyone in receipt of the previously issued financial statements is informed of the situation and does not amend the financial statements in circumstances where the auditor believes they need to be amended.
24.14	FAPQ	A modification to documentation or addition of new documentation is required after the final audit file is archived.

24.25	FAPQ	The engagement team finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed or performs new or additional audit procedures or draws new conclusions after the date of the auditor's report and the Apex audit file for the engagement has already been closed.
42.157	FAPQ	A successor auditor wishes to review an NAO audit file using technology which is not part of the NAO's digital estate.
42.161	Legal and Policy team	The audit file to be shared with a successor auditor includes information generated by the NAO or its legal advisers over which the NAO may wish to assert legal or professional privilege.
61.15	FAPQ	A regularity matter arises once the financial statements have been issued and the engagement team considers it appropriate to consult FAPQ.
61.24	FAPQ	The circumstances envisaged by paragraph 13 of ISA (UK) 560 (management does not amend the financial statements in circumstances where the auditor believes they need to be amended) apply.

Approval from the Director, Audit Quality or Director, Audit Risk and Compliance

6.15 Engagement teams must obtain approval from the Director, Audit Quality or a named deputy where any of the circumstances set out in ***Table 6B*** arise. In addition, the Director, Audit Quality approves resourcing decisions taken centrally to assign roles outside the 'Expected' role assignments shown in ***Table 12C*** and ***Table 12D*** in Chapter 12: Roles, delegations and licences (see paragraph 12.8), which comprise the following types of role assignment:

- Assignment of the Engagement Director role on a Category A audit to a Senior Audit Manager.
- Assignment of the Engagement Director role on a Category B or C audit to a Senior Audit Manager who has been in the Senior Audit Manager grade for less than one year.
- Assignment of the Engagement Manager role on a Category A audit to an Audit Manager.
- Assignment of the Engagement Manager role on a Category B or C audit to a Senior Auditor.
- Assignment of the Engagement Team-Leader role to an individual without a General Audit Licence.

Table 6B: Circumstances when the engagement team must obtain approval from the Director, Audit Quality or a named deputy

FAM paragraph reference	Circumstances requiring approval by the Director, Audit Quality
Modified audit certificates or reports	
6.12 10.10 54.69 54.70 54.74 55.22	Modified audit certificates or reports, including modified opinions and Emphasis of Matter, Other Matter and Material uncertainty related to going concern paragraphs (DAQ Minute required).
31.39	The engagement team proposes to report on instances of identified or suspected non-compliance with laws and regulations in the auditor's report.
New engagements	
9.21 14.7	New engagement requests (DAQ recommends approval to the C&AG) – requests should be copied to the Executive Director responsible for the Financial Audit Service Line and to the Executive Director responsible for the relevant Group.

10.21	A regularity opinion is recommended or required on an existing engagement where such an opinion has not previously been provided.
10.22	The Engagement Director determines that a regularity opinion is no longer required for an existing engagement.
Roles, delegations and licences	
12.13	Individuals without a General Audit Licence performing the Engagement Director, Engagement Manager or Engagement Team-Leader role.
12.16 40.5	Requests for delegated signature of an engagement (DAQ recommends approval to the C&AG).
Reports to regulators or appropriate authorities	
30.15 30.50	Any reports to an appropriate authority outside the audited entity under paragraph 44(a) of ISA (UK) 240 (Revised May 2021) (Updated May 2022).
31.46 31.79 31.84	Reports made to the proper authorities in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022). This includes where unlawful distributions are made by companies and instances of non-compliance with tax legislation.
31.70	Reports made to the regulator of a regulated entity.
31.72	Formal written reports following up an oral report previously made to the regulator.

6.16 Engagement teams must obtain approval from the Director, Audit Risk and Compliance or a named deputy where any of the circumstances set out in ***Table 6C*** arise. If any of these matters give rise to the need for a modified audit certificate or report, the modification requires additional approval by the Director, Audit Quality in accordance with ***Table 6B*** above.

Table 6C: Circumstances when the engagement team must obtain approval from the Director, Audit Risk and Compliance or a named deputy

FAM paragraph reference	Circumstances requiring approval by the Director, Audit Risk and Compliance (in addition to Director, Audit Quality approval of any resulting modified audit certificate or report)
Engagement quality reviews	
7.31	The Engagement Director has doubts about the independence of the EQR.
Ethical considerations	
8.50	An audited entity or third party have raised concerns surrounding the objectivity, integrity and independence of the C&AG, the NAO and any covered persons.
8.77	An Executive Director or former Executive Director wishes to take up a position at an audited entity within two years of their final day of employment at the NAO.
8.118	Fees for professional services, including any audit fees, are overdue and the amount is non-trivial (i.e., more than 10% of the annual audit fee).
8.123	A cash audit fee in excess of £1,500,000 is proposed.
8.144	Any threat to the NAO's objectivity and independence arising from a non-audit service is identified and the Engagement Director considers that there are safeguards that could be applied and which would be effective to eliminate the threat or reduce it to an acceptable level, so intends for the non-audit service to be provided. These services need to be approved by the Ethics Function before the work is agreed to.
8.146	The Engagement Director concludes that no appropriate safeguards are available to eliminate or reduce to an acceptable level the threats to the NAO's objectivity, including any perceived loss of independence, related to a proposed engagement for a non-audit service for an audited entity, but the NAO is the statutory auditor and so it would not be possible to withdraw from the audit engagement.
8.177	Any auditor's reports containing disclosure of a breach in the requirements of the Ethical Standard.

45.30	A request has been made by a Public Interest Entity (PIE) to the NAO, or to a contractor firm to which the audit of the PIE or its parent undertaking or controlled undertaking has been contracted out, for prohibited non-audit services to be provided, or such a service has been provided.
45.31	A non-audit service is provided by a contractor firm involved in the audit of a PIE, its parent undertaking or controlled undertakings, to a controlled undertaking of a PIE which is audited by the C&AG which is based outside of the UK.
Role assignments	
4.64 8.106 45.26	Any request for an individual to act as Portfolio Director or Engagement Director for longer than a period of five continuous years (Director, Audit Risk and Compliance recommends approval to Director, Audit Operations and Executive Director of Financial Audit).

Submitting a query to FAPQ

6.17 Engagement teams should submit any requests for consultation to FAPQ using either the Consultation functionality in Apex (for consultations pertaining to a specific engagement) or the Financial Audit Support Tool (FAST) (for other queries). In order to receive a prompt and effective response, the following detail should be provided:

- Audited entity name.
- Situation and context – This may involve a paper setting out the situation for particularly complex queries.
- The relevant standards and other guidance.
- The engagement team's consideration of the relevant standards and other guidance.
- Where relevant, the engagement team's consideration of wider or industry practice.
- A clear query and expectation from FAPQ.
- Audited entity's judgement (where relevant).
- The engagement team's proposal for how they should proceed.
- The role of the person sending the query in.
- The Engagement Manager should be copied in to demonstrate that the engagement team have discussed the query prior to submitting it to FAPQ.

6.18 In coming to a professional judgement in consultation with FAPQ, the engagement team may also refer to the steps for structuring the way in which a judgement is carried out and documented which are set out on pages 13 to 19 of the Financial Reporting Council's Professional Judgement Guidance (June 2022).

6.19 When a request for consultation is received, FAPQ will either respond promptly or provide an expected timeframe for a response. FAPQ will provide a structured response, clearly setting out the key judgements made.

Financial Audit Director Portfolio Review meetings

6.20 Financial Audit Director Portfolio Review meetings (FADPRs) are a key component of the NAO's quality process and provide an early opportunity for engagement teams to consult on key aspects of the audit. They also provide an opportunity for collaboration across the Financial Audit Service Line, ensuring that the best of the practice is deployed on the key audit issues.

6.21 FADPRs develop a consistent approach across the practice in identifying and addressing audit risks. These meetings are also used to establish a pipeline/critical path for potential audit panels to ensure teams are well placed at an early stage to address the most significant audit judgements and matters identified.

6.22 FADPRs will be held for some audits selected by FAPQ on a risk basis, but also on audits where teams have locally elected for consultation given their risk assessment and factors like team turnover.

6.23 Where FADPRs are set centrally, these are attended by the Executive Director of Financial Audit, the Deputy Head of Financial Audit and the Director, Audit Quality as well as key engagement team members and where relevant the VFM director, the Group Executive Director and EQR.

6.24 For FADPRs set locally, within groups, it is for the FA Service Line Director of the group to determine the appropriate consultation group led by an independent financial audit director. Where relevant, financial audit specialists should attend.

6.25 FADPRs will normally be scheduled for approximately one hour and should take place prior to any substantive interim audit fieldwork commencing to allow for sufficient input into the audit planning process.

6.26 FADPRs will follow a set topic list which will be communicated by the Financial Audit Practice and Quality team on an annual basis.

Audit panels

6.27 The Director, Audit Quality (DAQ), Executive Director of Financial Audit or Deputy Head of Financial Audit may convene an audit panel to consider the significant technical issues or issues of high reputational risk further. Audit panels are called at the discretion of the Director, Audit Quality and the Executive Director of Financial Audit or Deputy Head of Financial Audit.

6.28 The panel will comprise the Executive Director of Financial Audit and/or Deputy Head of Financial Audit, the engagement team, DAQ, the Engagement Quality Reviewer (if applicable) and any other experienced senior NAO staff the Engagement Director considers appropriate in the circumstances. The Executive Director responsible for the relevant Group may be invited where relevant.

6.29 Audit panel papers should be presented to FAPQ at least one week prior to the panel meeting, in order to enable FAPQ to research the issue and form a robust technical view. Where papers are received less than a week prior to the panel meeting, the panel may be postponed at the discretion of the Director, Audit Quality.

6.30 FAPQ will provide the secretariat function for the panel and will document the judgements reached to be held on the engagement team's audit file.

Differences of opinion between the engagement team and FAPQ

6.31 In any matter where the engagement team disagrees with advice provided by FAPQ and is unable to resolve this through further discussion with the FAPQ team member(s) dealing with the query, the Engagement Director should discuss the matter with the Director, Audit Quality and seek to reach a consensus position.

6.32 If the Engagement Director and the Director, Audit Quality are unable to reach a consensus position or the Engagement Director disagrees with a decision by the Director, Audit Quality not to provide approval in a matter covered by ***Table 6B*** above, an audit panel should be convened to resolve the matter.

6.33 If there remains a substantive difference of opinion following the conclusion of such an audit panel, the matter should be referred to the C&AG, who will make the final decision.

Other differences of opinion

6.34 In accordance with paragraph 37 of ISA (UK) 220 (Revised July 2021), if differences of opinion arise within the engagement team, or between the engagement team and the Engagement Quality Reviewer or individuals performing activities within the NAO's system of quality management, including those who provide consultation (except FAPQ, for which a specific policy is set out in the preceding section), the engagement team should follow the NAO's policies and procedures for dealing with and resolving such differences of opinion, which are set out in this section. As required by paragraph 31(e) of ISQM (UK) 1, the NAO has established a quality objective that differences of opinion are brought to the attention of the NAO and resolved.

6.35 If a substantive difference of opinion arises within the engagement team, the Engagement Director should seek to resolve this through discussion between relevant members of the engagement team. If the difference of opinion cannot be resolved through such discussion, the Engagement Director should use their professional judgement to determine appropriate action, which may involve one or more of the following:

- discussing with the C&AG and/or Executive Director of Financial Audit and/or Deputy Head of Financial Audit;
- consultation with FAPQ and/or other teams; and/or
- the Engagement Director's documenting their ultimate decision and the reasons for this in a note for the audit file, noting that different views have been expressed and considered.

6.36 In the circumstances where a difference of opinion cannot be resolved through consultation with FAPQ or an Audit Panel, the matter should be referred to the C&AG to determine the outcome.

6.37 ***Consultation required*** If a substantive difference of opinion arises between the engagement team and the Engagement Quality Reviewer or individuals performing activities within the NAO's system of quality management other than FAPQ, the engagement team should consult FAPQ, who may (at the discretion of the Director, Audit Quality) convene an Audit Panel to resolve the disagreement.

6.38 Paragraph 38 of ISA (UK) 220 (Revised July 2021) requires that the Engagement Director, as engagement partner:

- takes responsibility for differences of opinion being addressed and resolved in accordance with the firm's policies or procedures;
- determines that conclusions reached are documented and implemented; and
- does not date the auditor's report until any differences of opinion are resolved.

Chapter 7: Engagement Quality Review

Relevant standards and guidance

7.1 ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* deals with the firm's responsibility to establish policies or procedures addressing engagements that are required to be subject to Engagement Quality Reviews.

7.2 Paragraphs 1-23 to 1-25 of Practice Note 10 (Revised 2022) *Audit of financial statements* and regularity of public sector bodies in the United Kingdom provide guidance on applying the requirements of ISQM (UK) 1 relating to Engagement Quality Review in the public sector.

7.3 ISQM (UK) 2 (Updated March 2023) *Engagement quality reviews* deals with the appointment and eligibility of the Engagement Quality Reviewer and the Engagement Quality Reviewer's responsibilities relating to the performance and documentation of an Engagement Quality Review. The objective of the NAO under ISQM (UK) 2 (Updated March 2023) is, through appointing an eligible Engagement Quality Reviewer, to perform an objective evaluation of the significant judgements made by the engagement team and the conclusions reached thereon.

7.4 ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* sets out responsibilities of the Engagement Director, in the role of Engagement Partner, for audit engagements for which an Engagement Quality Reviewer is required.

The role of an Engagement Quality Review

7.5 As set out in paragraph 7 of ISQM (UK) 2 (Updated March 2023), the public interest is served by the consistent performance of quality engagements. Quality engagements are achieved through planning and performing engagements and reporting on them in accordance with professional standards and applicable legal and regulatory requirements. Achieving the objectives of those standards and complying with the requirements of applicable law or regulation involves exercising professional judgment and, when applicable to the type of engagement, exercising professional scepticism. As set out in paragraph 8 of ISQM (UK) 2 (Updated March 2023), an EQR is an objective evaluation of the significant judgments made by the engagement team and the conclusions reached thereon. The EQR's evaluation of significant judgments is performed in the context of professional standards and applicable legal and regulatory requirements. However, an EQR is not intended to be an evaluation of whether the entire engagement complies with professional standards and applicable legal and regulatory requirements, or with the NAO's policies or procedures.

7.6 As set out in paragraph 9 of ISQM (UK) 2 (Updated March 2023), the EQR is not a member of the engagement team. The performance of an EQR does not change the responsibilities of the Engagement Director, in the role of Engagement Partner, for managing and achieving quality on the engagement, or for the direction and supervision of the members of the engagement team and the review of their work. The EQR is not required to obtain evidence to support the opinion or conclusion on the engagement, but the engagement team may obtain further evidence in responding to matters raised during the EQR.

Determining whether an engagement should be subject to Engagement Quality Review

7.7 The Director, Audit Quality, will determine whether an Engagement Quality Reviewer (EQR) should be appointed for individual engagements, following consultation with the Portfolio Directors. This determination will take into account the circumstances of the engagement, including:

- the requirements of paragraph 34(f) of ISQM (UK) 1 as per the following paragraph;
- whether the entity is a Public Interest Entity (PIE) or whether any relevant laws or regulations require an Engagement Quality Review; or
- when it is determined that an engagement quality control revies is an appropriate response to address a risk to quality. Considerations should include:
    - the nature of the engagement, including the extent to which the entity's financial statements are of high Parliamentary or public interest; or
    - the identification of unusually complex circumstances or technical risks and/ or judgements in an engagement or class of engagements; or
    - whether it is likely that there may be a significant modification to the audit opinion;
    - where senior engagement staff are new to their role;
    - whether the engagement is a Category A audit; and
    - whether an EQR would be an appropriate response to any of the quality risks recorded within Quality Risk Registers (noting that existing mitigations against the risk can be taken into account in making this determination) – this will be considered as part of the risk assessment process within the system of quality management (see Chapter 4: Quality monitoring), which may identify EQR for a defined list of audit engagements as a quality response.

7.8 In accordance with paragraph 34(f) of ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements*, an Engagement Quality Reviewer should be appointed for:

- audits of financial statements of listed entities;
- audits or other engagements for which an Engagement Quality Review is required by law or regulation;
- audits or other engagements for which the NAO determines that an Engagement Quality Review is an appropriate response to address one or more quality risk(s);
- audits of financial statements of Public Interest Entities;
- public reporting engagements carried out in accordance with the Standards of Investment Reporting; and
- engagements for which an Engagement Quality Review is required by the FRC's Providing Assurance on Client Assets to the Financial Conduct Authority standard (Revised November 2019).

7.9 The audit file should evidence our considerations as to whether an audit needs an EQR, especially for category A1 audits.

7.10 The Engagement Director (and the Portfolio Director, if this is a different individual) should remain alert for changes in circumstances that indicate that an Engagement Quality Review may be appropriate, even though at the start of the engagement such a review was not required. Where this is the case, the Engagement Director should consult with the Director, Audit Quality as to whether an EQR should be appointed and document the result of this consultation. The Director, Audit Quality, will appoint individuals or teams to the EQR role where determined appropriate.

7.11 The EQR procedures also apply to contracted-out audits meeting the criteria for a quality control review. The decision to appoint an EQR is independent of the review processes in place at the partner firm, although this could affect the risk profile of the engagement, and the scope of the EQR's remit extends across the whole engagement. The NAO Engagement Director is not independent of the assignment so cannot act as an EQR and this review process would not mitigate the need for a different person to perform the role of NAO EQR.

7.12 EQRs focus on the key areas of professional judgement for those audits where there is a significant risk to the C&AG and the NAO. They help to minimise the audit risk by ensuring that audit judgements are subject to review before certification.

Appointment and eligibility of EQRs

7.13 In accordance with paragraph 17 of ISQM (UK) 2 (Updated March 2023), the Director, Audit Quality, as an individual with the competence, capabilities and appropriate authority within the NAO to fulfil the responsibility, has responsibility for the appointment of EQRs and therefore shall determine who will perform the EQR function for engagements where it is determined that an EQR is needed. The decision will take into consideration an individual's objectivity and independence from the body being audited, their specific skill set and their experience at the Director grade. The decision will also take into consideration the individual's competence, capabilities and time to fulfil the responsibility.

7.14 An EQR is an NAO Director, suitably qualified independent and objective person, or a team made up of such individuals, with sufficient and appropriate experience, time and authority to evaluate objectively the significant judgements the engagement team has made, that appropriate consultation has taken place in respect of difficult or contentious matters and that conclusions reached support the recommended audit report/certificate.

7.15 In accordance with paragraph 18 of ISQM (UK) 2 (Updated March 2023), the EQR should not be a member of the engagement team, and should:

- have the competence and capabilities, including sufficient time, and the appropriate authority to perform the EQR;
- comply with relevant ethical requirements, including in relation to threats to objectivity and independence of the EQR; and
- comply with provisions of law and regulation, if any, that are relevant to the eligibility of the EQR.

7.16 In accordance with paragraph 18-1 of ISQM (UK) 2 (Updated March 2023), for audits of financial statements of public interest entities, the EQR should be eligible for appointment as a statutory auditor and not be involved in the performance of the audit to which the EQR relates.

7.17 For single reviewers, the EQR should be a CCAB-qualified director with at least three years' experience as an Engagement Director. Where a specialist audit licence is required for the Engagement Director, the EQR should also hold that licence. EQRs for audits of a specialist nature or requiring particular expertise (such as in complex IT systems) will need to have appropriate skills in that area. An EQR must have received specific EQR training. Where a reviewer is appointed from outside the NAO, the equivalent level of experience and expertise will be required. A team of reviewers will be assembled to fulfil the EQR role when the Director, Audit Quality determines that an array of specialist skills or complex issues necessitates more than one reviewer.

7.18 By exception, the Director, Audit Quality may appoint an EQR who only has two years' experience as an Engagement Director in circumstances where the individual appointed to the role has a specialist licence or particular expertise relevant to the engagement subject to the EQR.

7.19 In order to be independent and objective, the EQR should not have any responsibilities for the audited entity or any entities in the same group and should not have been a member of the engagement team in the preceding five years. This policy is consistent with paragraph 19 of ISQM (UK) 2, which requires a cooling-off period of two years, or a longer period if required by relevant ethical requirements, before the engagement partner can assume the role of EQR. The maximum duration an NAO Director can act as an EQR for any particular assignment is seven years and will not normally exceed five years. For audits of public interest entities, the EQR should not be in post for longer than five years. Furthermore, the Engagement Director should not be in the line management chain of the EQR. FAPQ will document a central assessment of the capacity, capability and independence of EQRs as part of a central EQR analysis.

7.20 Where the EQR's eligibility to perform the EQR is impaired (which may be, for example, due to changes in the circumstances of the engagement, including new conflicts of interest, and/or changes in the other responsibilities of the EQR; and may be identified by the EQR themselves, members of the engagement team or FAPQ), the appropriate actions to be taken by the NAO, including the process for identifying and appointing a replacement in such circumstances, are as follows:

- The Director, Audit Quality, should consider whether the EQR continues to have the appropriate competence and capabilities, along with sufficient time, to perform the EQR.
- If the Director, Audit Quality considers that this is not the case, they should consider whether the engagement continues to require an EQR (if it does not, they should inform the EQR and the Engagement Director that the EQR appointment is terminated).
- If it does, the Director, Audit Quality should identify a replacement EQR who is eligible for appointment and communicate this appointment to the replacement EQR, the previous EQR and the Engagement Director.
- The Director, Audit Quality should provide the Engagement Director with a note of their decision to appoint a replacement EQR, or to terminate the EQR appointment, and the circumstances behind this, which should be retained on the audit file.
- Upon appointment, the replacement EQR should review any work performed on the EQR so far and confirm that it is appropriate, amend the scope of the EQR and re-perform as they see fit in line with their professional judgement. They should discuss the key issues on the engagement with the Engagement Director and Key Audit Partner(s) (discussion with the C&AG is not required, but the EQR may consult the C&AG if they consider this would contribute to the effectiveness of their review or assist in resolving a disagreement) and document this discussion in the EQR Response Group.

7.21 In accordance with paragraph 23 of ISQM (UK) 2 (Updated March 2023), where the EQR becomes aware of circumstances that impair the EQR's eligibility to perform the EQR, the EQR should notify the Engagement Director and the Director, Audit Quality, and:

- if the EQR has not commenced, decline the appointment to perform the EQR; or
- if the EQR has commenced, discontinue the performance of the EQR.

Threats to the objectivity of the EQR

7.22 ***Consultation required*** In accordance with paragraph 24(c) of ISQM (UK) 2 (Updated March 2023), where the nature and extent of engagement team discussions with the EQR about a significant judgement give rise to a threat to the objectivity of the EQR, the engagement team and the EQR should take appropriate actions based on the circumstances, taking into account the requirements set out in Chapter 8: Ethical considerations. Such actions will include consultation with the Ethics Function. This requirement extends to any threats to the objectivity of EQR Assistants.

Performance and documentation requirements

7.23 A formal EQR consists of an objective evaluation of the significant judgements made by the engagement team as well as specific consideration over whether appropriate consultation has taken place on difficult or contentious matters, especially those matters with differing opinions The EQR shall also review the financial statements and auditor's report. This does not preclude a Director from requesting a Director consultation on one specific issue (though this would not constitute an Engagement Quality Review).

7.24 The EQR should perform an objective evaluation of the significant judgements made by the engagement team and the conclusions reached in formulating the proposed C&AG's audit certificate and ensure that the audit file documentation reflects this. When the EQR covers a group audit, it is

expected that, to the extent necessary (in the EQR's professional judgement) to evaluate the significant judgements made by the Group Engagement Team, the EQR will review work performed by component auditors for the purpose of the group audit. In accordance with paragraph 24(a) of ISQM (UK) 2 (Updated March 2023), the EQR should perform procedures at appropriate points in time during the engagement to provide an appropriate basis for this evaluation.

7.25 To preserve objectivity in undertaking this challenge function, the EQR's responsibilities do not include consultation on technical issues. These should principally be through FAPQ. Where the EQR considers that the engagement team should consult on a technical issue, this should be discussed with the Engagement Director.

7.26 The scope of the Engagement Quality Review should be documented (this should include a reconsideration of the scope of the EQR after the EQR has, in accordance with paragraph 25 of ISQM (UK) 2 (Updated March 2023), read and obtained an understanding of information communicated by the engagement team regarding the nature and circumstances of the engagement and the entity) along with conclusions on all the matters required to be considered in the review and any other relevant matters the EQR director wishes to note and report to the Engagement Director. The Engagement Director may not sign the certification journal (or the audit certificate, where signature is delegated) until all matters raised by the EQR have been satisfactorily resolved.

7.27 In accordance with paragraph 24-1 of ISQM (UK) 2 (Updated March 2023), the EQR should:

- consider the NAO's compliance with the relevant ethical requirements in relation to the engagement;
- form an independent opinion as to the appropriateness and adequacy of the safeguards applied; and
- consider the adequacy of the documentation of the Engagement Director's consideration of the relevant ethical requirements and evaluation of any threats to compliance with those requirements.

7.28 In accordance with paragraph 25 of ISQM (UK) 2 (Updated March 2023), in performing the EQR, the EQR should:

- read, and obtain an understanding of, information communicated by:
    - the engagement team regarding the nature and circumstances of the engagement and the entity), including, in the NAO context:
        - the Engagement Details tab in Apex;
        - the Set Up Workflow Step;
        - the Engagement Risk Assessment Audit Form;
        - the Overall Audit Strategy;
        - the 'Understanding the Entity' templates listed in ***Table 15D***;
        - the Enquiries of Key Audited Entity Contacts Workflow Step Item;
        - the Audit Planning Report; and
        - the Engagement Team Discussion on Risk and Fraud; and
    - the NAO related to the firm's monitoring and remediation process, in particular identified deficiencies that may relate to, or affect, the areas involving significant judgements made by the engagement team (in the NAO context, this would involve a review of the Sharepoint pages relating to the system of quality management, which will highlight key quality risks and actions for audit engagements);
- discuss with the Engagement Director and, if applicable, other members of the engagement team, significant matters and significant judgements made in planning, performing and reporting on the engagement;
- based on the information obtained in the preceding bullet points, review selected engagement documentation relating to the significant judgements made by the engagement team and evaluate:
    - the basis for making those significant judgements, including, when applicable to the type of engagement, the exercise of professional scepticism by the engagement team;

  - whether the engagement documentation supports the conclusions reached; and
  - whether the conclusions reached are appropriate;
- for audits of financial statements, evaluate the basis for the Engagement Director's determination that relevant ethical requirements relating to independence have been fulfilled;
- evaluate whether appropriate consultation has taken place on difficult or contentious matters or matters involving differences of opinion and the conclusions arising from those consultations;
- for audits of financial statements, evaluate the basis for the Engagement Director's determination that the Engagement Director's involvement has been sufficient and appropriate throughout the audit engagement such that the Engagement Director has the basis for determining that the significant judgements made and the conclusions reached are appropriate given the nature and circumstances of the engagement; and
- review:
  - for audits of financial statements, the financial statements and the auditor's report thereon, including, if applicable, the description of the key audit matters;
  - for review engagements, the financial statements or financial information and the engagement report thereon; or
  - for other assurance and related services engagements, the engagement report, and when applicable, the subject matter information.

7.29 ***Consultation required*** In accordance with paragraph 26 of ISQM (UK) 2 (Updated March 2023), the EQR should notify the Engagement Director if the EQR has concerns that the significant judgements made by the engagement team, or the conclusions reached thereon, are not appropriate. If such concerns are not resolved to the EQR's satisfaction, the EQR should notify the Director, Audit Quality, that the EQR cannot be completed.

7.30 In accordance with paragraph 27 of ISQM (UK) 2 (Updated March 2023), the EQR should determine whether the requirements in ISQM (UK) 2 (Updated March 2023) with respect to the performance of the EQR have been fulfilled, and whether the EQR is complete. If so, the EQR should notify the Engagement Director that the EQR is complete. This notification should be made using the Tasks functionality within Apex.

7.31 ***Consultation required*** The EQR should complete a Declaration of Independence to confirm they are sufficiently independent from the engagement team and the body being audited. If the Engagement Director has any doubts about the independence of the EQR, they should contact the Director, Audit Risk and Compliance.

7.32 The EQR should document, for the audit engagement reviewed, that:

- the procedures required by the NAO's policies on Engagement Quality Review have been performed;
- the Engagement Quality Review has been completed on or before the date of the C&AG's audit certificate; and
- the EQR is not aware of any unresolved matters that would cause the EQR to believe that the significant judgements the engagement team made and the conclusions it reached were not appropriate.

7.33 The EQR Audit Response Group, as well as the planning and concluding procedures in Apex, should be used to document that the EQR has been performed. Such documentation should be completed in a timely manner. These should be supplemented, as appropriate, with other documentation or sign-offs within the file to demonstrate the EQR challenge on key judgements and their engagement throughout the audit cycle (for example, by including minutes of meetings and e-mails of correspondence with the engagement team). In accordance with paragraph 28 of ISQM (UK) 2 (Updated March 2023), the EQR should take responsibility for the documentation of the EQR. In accordance with paragraph 29 of ISQM (UK) 2 (Updated March 2023), the documentation of the

EQR should be included with the engagement documentation. In exercising these responsibilities, the EQR should ensure that they have reviewed any EQR documentation prepared by EQR Assistants and EQR team members.

7.34 In accordance with paragraph 30 of ISQM (UK) 2 (Updated March 2023), the EQR should determine that the documentation of the EQR is sufficient to enable an experienced practitioner, having no previous connection with the engagement, to understand the nature, timing and extent of the procedures performed by the EQR and, when applicable, individuals who assisted the reviewer (EQR Assistants), and the conclusions reached in performing the review. The EQR should also determine that the documentation of the EQR includes:

- the names of the EQR and any EQR Assistants;
- an identification of the engagement documentation reviewed;
- the basis for the EQR's determination in accordance with paragraph 27 of ISQM (UK) 2 (Updated March 2023) (whether the requirements in ISQM (UK) 2 (Updated March 2023) with respect to the performance of the EQR have been fulfilled, and whether the EQR is complete);
- the notifications required in accordance with paragraphs 26 (any concerns that the significant judgements made by the engagement team, or the conclusions reached thereon, are not appropriate) and 27 of ISQM (UK) 2 (Updated March 2023); and
- the date of completion of the EQR.

7.35 Other matters the EQR will usually consider in evaluating the significant judgments made by the engagement team include:

- significant risks, including fraud risks, and the engagement team's response thereto;
- judgements made, particularly with respect to materiality and significant risks;
- the significance and disposition of corrected and uncorrected misstatements identified during the audit;
- compliance with relevant ethical requirements; and
- the matters to be communicated to management and those charged with governance and, where applicable, other parties.

7.36 In accordance with paragraph 21(a) of ISQM (UK) 2 (Updated March 2023), the EQR should take overall responsibility for the performance of the EQR. The EQR determines the extent of the review, which can depend on the complexity of the engagement, the risks associated with the audit and the experience of the Engagement Director and engagement team. For example, a review which is required as a result of a single issue which has arisen in an audit will have a narrower focus than a review that is required as a result of high inherent audit risk.

7.37 As set out in paragraph 16 of ISQM (UK) 2 (Updated March 2023), the proper application of the requirements of ISQM (UK) 2 (Updated March 2023) is expected to provide a sufficient basis for the achievement of the objective of the standard. However, if the NAO or the EQR determines that the application of the relevant requirements does not provide a sufficient basis for the achievement of the objective of the standard, the NAO or the EQR, as applicable, should take further actions to achieve the objective: for example, the EQR may decide to undertake additional procedures over and above the requirements of ISQM (UK) 2 (Updated March 2023) in order to achieve the objectives of the EQR.

EQR Assistants – role

7.38 As described in paragraph A19 of ISQM (UK) 2 (Updated March 2023), in certain circumstances, it may be appropriate for the EQR to be assisted by an individual or team of individuals with the relevant expertise. For example, highly specialised knowledge, skills or expertise may be useful for understanding certain transactions undertaken by the entity to help the EQR

evaluate the significant judgments made by the engagement team related to those transactions. Such individuals are referred to as EQR Assistants.

7.39 In accordance with paragraph 21(b) of ISQM (UK) 2 (Updated March 2023), the EQR is responsible for determining the nature, timing and extent of the direction and supervision of the individuals assisting in the EQR, and the review of their work.

7.40 Following the appointment of an EQR Assistant, the appointed EQR may delegate any EQR task to the Assistant except for the following

- any discussions with the engagement partner and Key Audit Partner(s);
- setting the scope of the EQR; and
- forming a conclusion on the significant judgements made during the engagement.

EQR Assistants – eligibility

7.41 The Director, Audit Quality, may appoint one or more EQR Assistants to an engagement who are eligible for such an appointment. An assessment of the capabilities, capacity (including time) and independence of the EQR Assistant will be documented centrally and approved by the Director, Audit Quality prior to appointment.

7.42 In accordance with paragraph 20 of ISQM (UK) 2 (Updated March 2023), individuals who assist the EQR should not be members of the engagement team; should have the competence and capabilities, including sufficient time, to perform the duties assigned to them; and should comply with relevant ethical requirements, including in relation to threats to their objectivity and independence and, if applicable, the provisions of law and regulation.

7.43 In order to be independent and objective, an EQR Assistant should not have any responsibilities for the audited entity or any entities in the same group and should not have been a member of the engagement team in the preceding five years. The maximum duration an EQR Assistant may act for any particular assignment is seven years and will not normally exceed five years. For audits of public interest entities, an EQR Assistant should not be in post for longer than five years. Furthermore, the Engagement Director should not be in the line management chain of the EQR Assistant. This policy mirrors the equivalent requirements for EQRs as set out earlier in this Chapter.

7.44 An EQR Assistant should complete a Declaration of Independence to confirm they are sufficiently independent from the engagement team and the body being audited.

Responsibilities of the Engagement Director in relation to the EQR

7.45 In accordance with paragraph 36 of ISA (UK) 220 (Revised July 2021), for audit engagements for which an EQR is required, the Engagement Director should:

- determine that an EQR has been appointed;
- cooperate with the EQR and inform other members of the engagement team of their responsibility to do so;
- discuss significant matters and significant judgements arising during the audit engagement, including those identified during the EQR, with the EQR; and
- not submit the audit certificate or report for C&AG signature, or sign the audit report where signature is delegated, until the completion of the EQR.

7.46 In accordance with paragraph 24(b) of ISQM (UK) 2 (Updated March 2023), the Engagement Director is precluded from dating the audit certificate or report until notification has

been received from the EQR in accordance with paragraph 27 of ISQM (UK) 2 (Updated March 2023) that the EQR is complete.

Section 4: Ethics

Chapter 8: Ethical considerations

Relevant standards and guidance

8.1 The NAO complies with the FRC Revised Ethical Standard 2024 (the Ethical Standard) and International Standards on Auditing (UK) (ISAs (UK)) in respect of all financial audit engagements. These standards form an integral part of the NAO Code of Conduct. The Revised Ethical Standard 2024 becomes effective on 15 December 2024. It will be applied to all in house audits reviewing 2024-25 financial statements and any audits where planning commences post the issuance of this Manual (October 2024). Audits and non-audit services which are in progress as at 1 September 2024 may continue under the provisions of the Revised Ethical Standard 2019. For contracted-out audits, performed following the processes in Section 10: Contracted-out work, the NAO will apply the iteration of the Revised Ethical Standard applied by the contractor firm. Further guidance on this will be published by FAPQ and FA Operations, including which firms may be applying a version of the standard which deviates from the Revised Ethical Standard 2024.

8.2 For financial audit engagements of public interest entities, the NAO complies with the Revised Ethical Standard 2024 as applied to public interest entities and ISAs (UK). The Revised Ethical Standard 2024 introduces a number of additional requirements for audits of public interest entities, which are explained in Chapter 45: Public Interest Entities.

8.3 For financial audit engagements of listed entities, the NAO complies with the Revised Ethical Standard 2024 as applied to listed entities and ISAs (UK). This introduces a number of additional requirements for audits of listed entities, references to which may be found in paragraph 1.46 of the Revised Ethical Standard 2024.

8.4 For financial audit engagements which are not audits of public interest entities and not audits of listed entities, the NAO complies with the Revised Ethical Standard 2024 and ISAs (UK) to the extent that this is required under the pronounced scope of the Revised Ethical Standard 2024. This sets out that the Standard applies to:

- audits of financial statements undertaken in compliance with International Standards on Auditing (UK); and
- other “public interest assurance engagements” undertaken in compliance with performance standards issued by the FRC, including:
    - Reporting accountants acting in connection with an investment circular (the Standards for Investment Reporting – ‘SIRs’);
    - Reviews of interim financial information by the independent auditor of the entity (International Standard on Review Engagements (UK) 2410);
    - Engagements to provide assurance on client assets to the Financial Conduct Authority (the CASS Standard); and
    - Other assurance engagements specified by the FRC as "public interest assurance engagements" performed in accordance with International Standard on Assurance Engagements (UK) (ISAE (UK)) 3000.

Engagements such as Agreed Upon Procedures do not require the application of the Revised Ethical Standard 2024, though the NAO will apply its principles to ensure the products delivered are

independent and objective. The policies within this Manual which are relevant to compliance with the Ethical Standard have been drafted with the general objective of aligning closely to the requirements of the Revised Ethical Standard 2024 as applied to listed entities, in so far as such alignment is appropriate to the NAO's circumstances and the nature of its audited entities.

8.5 It is not NAO policy to apply the additional requirements listed in paragraph 1.46 of the Revised Ethical Standard 2024 to engagements which are not audits of public interest entities and not audits of listed entities, except in so far as they inform the drafting of the general requirements set out in the FAM. Therefore, the requirements in paragraph 1.47 of the Ethical Standard (to establish policies and procedures which set out the circumstances in which those additional requirements are applied to other engagements and to communicate the application of such requirements to those charged with governance) do not apply to such engagements.

8.6 Paragraphs 1-229 to 1-235 of Practice Note 10 (Revised 2022) provide guidance on applying the Ethical Standard in the public sector.

8.7 Paragraphs 14 and A16-A19 of ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independent auditor and the conduct of an audit of accordance with International Standards on Auditing (UK)* require that the auditor comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements.

8.8 Paragraphs 16 to 21 and the related application guidance of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* set out the Engagement Partner's (for NAO audits, the Engagement Director's) responsibilities with respect to relevant ethical requirements.

8.9 Paragraphs 29, A62 to A64 and A66 of ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* set out the responsibilities of the firm for establishing quality objectives that address the fulfilment of responsibilities in accordance with relevant ethical requirements, including those related to independence.

8.10 ***Table 25D*** in Chapter 25: Group audit procedures discusses requirements relating to relevant ethical requirements applicable to group audits.

8.11 'Relevant ethical requirements', as defined in those ISAs (UK) and ISQM (UK) 1 include:

- the provisions of the International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards)* (IESBA Code) related to audits of financial statements; and
- for UK auditors, the Revised Ethical Standard 2024 referred to above.

Definitions

8.12 The following definitions set out in the Revised Ethical Standard 2024 have also been applied within the guidance in this Chapter:

8.13 The Revised Ethical Standard 2024 defines a covered person as a person in a position to influence the conduct or outcome of the engagement. In the context of the NAO, this is considered to include the following individuals in respect of all of our engagements, except where safeguards have been put in place to ensure that they are not covered persons on individual engagements:

- all members of the engagement team;
- the EQR;
- the Hot Review Manager and Director;

- any internal experts who perform work on behalf of the engagement team or assist the engagement team (e.g. MESH);
- any external experts who perform work on behalf of engagement team or assist the engagement team (this would include all members of staff at the external expert who have been engaged in the assignment);
- the C&AG;
- the Private Secretary to the C&AG;
- Executive Directors;
- the Director, Audit Quality;
- Senior Audit Managers in Financial Audit Practice and Quality;
- the Director, Audit Risk and Compliance;
- members of the Audit Technology Services (ATS) team;
- certain members of the Audit Transformation Programme (ATP) team who have responsibilities relating to Apex development;
- other regular attendees at Financial Audit Management Team meetings;
- the performance coaches of the Engagement Director, Engagement Manager and Engagement Team-Leader as well as the performance coaches of these individuals; and
- for contracted out audits, all covered persons within the contractor audit firm.

8.14 The Revised Ethical Standard 2024 has been interpreted in the context of the NAO. The Revised Ethical Standard 2024 wording includes “Partners within the firm”, which has been omitted in favour of “covered persons relevant to the engagement”. NAO Directors do not have the same level of oversight and control as in a private sector firm and thus, are unable to influence the conduct and outcome of an audit through holding a relationship or connection with an audited entity outside of their portfolio. Covered persons includes the Engagement Director for an audited entity who act independently of and are not influenced by other Engagement Directors.

8.15 Connected parties are defined by the Revised Ethical Standard 2024 as including:

- An entity that has direct or indirect control over the audited entity if the audited entity is material quantitively or qualitatively to that entity.
- An entity with a direct financial interest in the audited entity if that entity has significant influence over the audited entity and the interest in the audited entity is material quantitively or qualitatively to that entity.
- An entity that is controlled directly or indirectly by the audited entity.
- An entity over which the audited entity or and entity controlled by the audited entity has a direct financial interest that gives it significant influence and that interest is material quantitively or qualitatively to the audited entity and entities controlled by the audited entity.
- An entity that is under common control of the audited entity if both entities are material quantitively and qualitatively to the ultimate controlling entity of both parties
- Key management personnel and those charged with governance at the audited entity, its parent entity and any subsidiary entities.
- Those who may be in a position to influence the activities or the entity, its key management personnel, those charged with governance or management and those charged with governance at the parent entity or subsidiary entities.

8.16 Factors that may be relevant to determining whether an entity or an interest in an entity is material to another entity include:

- the extent and nature of the relationships between the audited entity and the other entity and the impact these relationships have on either entity or the NAO; and
- the extent and nature of the relationship(s) between the NAO and the other entity and the impact this has on independence.

8.17 The FRC's *Glossary of Terms – Ethics and Auditing* (Updated December 2019) defines "persons who are closely associated" as including:

- A spouse or partner considered to be equivalent to spouse in accordance with national law.
- A dependent child in accordance with national law.
- A relative who (at any point in the period from the start of the financial period in respect of which the engagement is being conducted to the certification date) has lived in the same household as the person with whom they are closely associated for at least one year.
- A firm whose managerial responsibilities are discharged by, or which is directly or indirectly controlled by, the firm/person with whom they are associated, or by a spouse, dependent child or close relative of such a person in which the firm or any such person has a beneficial or other substantially equivalent economic interest.
- A trust whose managerial responsibilities are discharged by, or which is directly or indirectly controlled by, or which is set up for the benefit of, or whose economic interests are substantially equivalent to, the firm/person with whom they are associated or any the spouse child or close relative of such a person.

Background information and application guidance

8.18 Professional standards and guidelines are essential for the credibility, quality and professionalism of public-sector auditing. In our audit work the NAO applies the highest levels of ethical and professional standards and uses the ethical and professional standards applicable to auditing bodies.

8.19 In considering whether the Revised Ethical Standard 2024 has been complied with, it will be necessary to apply the "Third Party Test". This test involves an evaluation of whether the overarching principals and requirements of the Revised Ethical Standard 2024 have been met with reference to the perspective of an objective, reasonable and informed third party.

8.20 The NAO as an organisation and its staff undertake routine transactions with HM Revenue and Customs (HMRC), in order to meet statutory taxation requirements, and with the Scheme Administrator for the Civil Service pension arrangements (MyCSP), which acts on behalf of the Scheme Manager (the Cabinet Office). The NAO considers that no specific safeguards are required because:

- transactions with both the Scheme Administrator for the Civil Service pension arrangements and HMRC that are entered into by the NAO and its staff are undertaken on an arm's length basis; and
- any benefit received by individual NAO staff as the result of being a member of the Civil Service pension arrangements will not materialise for years into the future.

8.21 The judgement that no specific safeguards are required, as set out in the preceding paragraph, also applies in respect of:

- transactions between:
    - closely connected family members of NAO staff and
    - the Scheme Administrator for the Civil Service pension arrangements or HMRC;
- transactions between:
    - staff of a firm undertaking a contracted-out audit on behalf of the NAO and
    - the Scheme Administrator for the Civil Service pension arrangements or HMRC; and
- transactions between:
    - the NAO, NAO staff, their closely connected family members or staff of a firm undertaking a contracted-out audit on behalf of the NAO and
    - entities involved in managing or administering other pension schemes audited by the NAO; and
- transactions involving other NAO audited bodies which are conceptually similar and where similar principles and circumstances apply: i.e., the transactions between an audited entity and the NAO

and/or NAO staff and/or closely connected family members and/or staff of a contractor audit firm are routine in nature and undertaken on an arm's length basis, in the audited entity's capacity as a government-funded entity delivering services to the general public or services which are available to a wide range of corporate entities or businesses on similar terms.

8.22 The NAO would be required to consider further safeguards if the NAO or any member of staff were in dispute with the Scheme Administrator and/or Scheme Manager of the Civil Service pension arrangements, or with HM Revenue and Customs or another audited entity where similar principles apply as described above.

8.23 The NAO should not provide an engagement to any entity or person where that entity or person is in a position to influence the affairs of the NAO or the performance of any engagement of the NAO. An exception is made with respect to the audit of the Financial Reporting Council (FRC). To mitigate the risk, the Engagement Director responsible for the FRC audit is excluded from responsibility for any Public Interest Entity audits and is not responsible for any engagement with the FRC in their role as our regulator. The conflict is noted and reported to Those Charged with Governance of the FRC.

Preliminary and on-going engagement activities

8.24 The engagement team should consider compliance with the Revised Ethical Standard 2024 at the start of any audit engagement. This includes audits which are undertaken on a statutory basis and ongoing engagements. This is to ensure that the engagement team has the necessary independence and ability to perform the engagement. This includes assessment and documentation of whether the NAO meets the ethical outcomes of the overarching principles and supporting ethical provisions, and complies with the requirements, of the Revised Ethical Standard 2024 and whether there are threats to its integrity, objectivity or independence and the safeguards applied to mitigate those threats and why they mitigate the threats.

8.25 FA CompassThe Engagement Director should ensure, prior to the acceptance of an engagement that the audit fee for the previous engagement has been recovered from the entity or that suitable processes have been agreed for the recovery of the audit fee.

8.26 The NAO has established policies and procedures that ensure that the organisation acts with integrity, objectivity and independence. The engagement team should document this consideration on the Engagement Risk Assessment Audit Form.

Ethical principles

8.27 The Revised Ethical Standard 2024 establishes overarching principles on integrity, objectivity and independence which underpin the requirements of the Standard and should be taken account of when making judgements on ethical matters. These principles have been interpreted in the context of the NAO as follows.

Integrity and Objectivity

8.28 The C&AG, the NAO and all staff shall behave with integrity and objectivity in all professional and business activities and relationships.

Independence

8.29 In relation to each engagement, the NAO, and each covered person, shall ensure (in the case of a covered person, insofar as they are able to do so) that the NAO and each covered person

is free from conditions and relationships which would make it probable that an objective, reasonable and informed third party would conclude the independence of the C&AG, the NAO or any covered person is compromised. The definition of covered persons in the NAO context is given in the 'Definitions' section earlier in this Chapter.

Ethical requirements

8.30 The requirements which support the overarching principles of the Revised Ethical Standard 2024 are set out in Part B of the Revised Ethical Standard 2024. All audit financial audit engagements undertaken by the NAO must comply with these requirements as applicable to listed entities. There are six broad sections which these requirements fall under:

8.31 The NAO is required to comply with the standards and report all breaches to the Competent Authority on a biannual basis, or by exception when the Competent Authority would expect notification. Where notifications of conflicts assessed as a breach are communicated directly to the Ethics Function, the Ethics Function will communicate these to the relevant Engagement Director and consult with the Engagement Director, appropriate Executive Directors and the C&AG regarding actions and appropriate safeguards.

8.32 ***Consultation required*** Where the engagement team identifies potential breaches, the engagement team should consult the Ethics Function. The Ethics Function will liaise with the Engagement Director, appropriate Executive Directors and the C&AG to consider any actions and safeguards. For breaches identified by teams or by the Ethics Function, the Ethics Function will facilitate reporting to the Financial Reporting Council. A Root Cause Analysis should be carried out on the breach as an identified deficiency in the system of quality management in accordance with paragraph 41(a) of ISQM (UK) 1 and the associated application guidance (further guidance on Root Cause Analysis may be found in Chapter 4: Quality monitoring). Any breaches must also be disclosed in the audit certificate or report. The disclosure in the audit certificate or report should be agreed as part of the consultation with FAPQ.

8.33 After consultation with the Ethics Function has concluded, the Engagement Director should ensure that details of any breaches of the Revised Ethical Standard 2024 and of any safeguards applied and actions taken to address any threats to independence are reported to those charged with governance.

Section 1: General Requirements and Guidance

8.34 The work of the NAO is underpinned by rigorous quality assurance arrangements. The C&AG is the designated Ethics Partner for the NAO. The NAO's responses to quality risks within the system of quality management are built into our work through the Office's policies on recruitment, training and continuing professional development, the Code of Conduct, and through operational guidance specific to the execution of our work, detailed within this Manual. The latter covers matters such as methodology and process and the level and nature of review of the work completed. It is designed to ensure that the Office's work complies with professional standards, including the Revised Ethical Standard 2024. The C&AG is ultimately responsible for ensuring the adequacy of these policies and procedures and ensuring sufficient support and guidance is provided to staff. Part of this framework includes hot and cold review of engagements to ensure appropriate consideration of threats to the integrity, objectivity and independence of the firm, its partners and staff.

8.35 The Revised Ethical Standard 2024 requires all NAO staff and covered persons who become aware of any condition or relationship which could impair the independence of the NAO or any covered person to report the matter to the Engagement Director (if known) or (failing that) to the firm's Ethics Partner/Function, or otherwise to the senior management of the firm or those with direct

responsibility for the management of the firm's audit and other public interest assurance business, at the earliest opportunity. For individual's own conflicts, this responsibility to report is met via the Declarations of Independence and Covered Person requirements on individual audits, and completion of the Code of Conduct declarations. When staff become aware of a conflict another individual should declare that has been withheld or have concerns on the appropriateness of the response to an ethical matter, staff may contact the Ethics Function or use the NAO's Whistleblowing policy as appropriate.

8.36 ***Consultation required*** The Director, Audit Risk and Compliance leads the NAO's Ethics Function, supporting the C&AG in his role as ethics partner. Any key judgements concerning ethical matters must be referred to the Ethics Function for consideration. The Director, Audit Risk and Compliance will consult the C&AG on more judgemental and high-risk assessments or those which involve conflicts held by Executive Directors, or with an Executive Director in the absence of the C&AG.

8.37 The Ethics Function maintains a confidential log of conflicts of interest and other ethical issues which arise and safeguards which have been put in place to mitigate any risks arising from these issues. This log is shared with the FRC upon request and updated regularly.

8.38 ***Consultation required*** Where the Ethics Function identifies a new conflict of interest or ethical issue affecting a particular engagement, they will inform the relevant Engagement Director of the issue and safeguards which are required to mitigate against any threat to independence and objectivity. The Engagement Director should consider the information provided and document on the audit file their agreement with any judgements and safeguards communicated. Where they disagree, they should discuss this with the Ethics Function.

8.39 The Engagement Director shall identify and assess the circumstances which could adversely affect the objectivity and integrity of the NAO as a whole or covered persons in the performance of the engagement, including any that could impair independence and shall apply procedures or safeguards which will either:

- Eliminate the threat to independence; or
- Reduce the threat to a level at which independence is not compromised.

8.40 ***Consultation required*** The Engagement Director should consult with the Ethics Function where they are unable to introduce suitable safeguards to reduce the threat to independence arising from an ethical issue to a suitable level.

8.41 Where the Engagement Director, following consultation with the Director, Audit Quality, concludes that there are no appropriate safeguards to reduce the threats to objectivity, integrity and independence arising from the ethical issue to an acceptable level, then the C&AG should withdraw from the engagement where possible.

8.42 Disclosure will be considered in both the auditor's report and in communications with those charged with governance, in addition to safeguards being implemented to reduce the threat, where it is not possible to withdraw from the engagement.

8.43 The Engagement Director must consider the following regarding threats to independence, integrity and objectivity for the audited entity and its connected parties:

- the context of their individual and cumulative effects; and
- current relationships with the entity and its connected parties and circumstances and relationships which existed prior to and in prospect following the engagement.

8.44 The Engagement Director should ensure their consideration of the NAO's objectivity and independence is appropriately documented and updated on a timely basis and also reviewed and confirmed prior to certification. Paragraph 1.71 of the Revised Ethical Standard 2024 provides guidance on what matters should be documented.

8.45 The engagement team should document in the audit file on a timely basis conclusions on compliance with independence requirements via their declarations of independence within Apex and include details of any relevant consultation that supports the conclusion and any issues identified with respect to compliance with the Ethical Standard and matters that impact upon the NAO's objectivity and independence.

8.46 The Engagement Director must consider threats to independence in relation to each covered person for the engagement. A central register of interests in respect of the Executive Team, Private Office, the Director, Audit Quality, the Director of IT Audit, and Senior Audit Managers and key members of the Financial Audit Practice and Quality, MESH Modelling, Property Centre of Expertise, Pensions Centre of Expertise, Financial Instruments Centre of Expertise, Fraud and Error, Digital Financial Audit and data analytics teams is maintained and updated on regularly to assist with this requirement.

8.47 The Ethics Function will communicate whether there are any conflicts on the central register of interests which are relevant to audited entities in the portfolio of each portfolio director on an annual basis, usually in October in line with the planning cycle. This will include a nil return where applicable. Portfolio directors should cascade this communication to the relevant engagement teams within their portfolio. The Ethics Function will contact portfolio directors with details of any new threats to independence which may arise from their monthly reviews of the register in between the annual circularisation exercise.

8.48 There is a separate procedure within the 'FA Declaration of team members' independence and skills' Audit Response Group in the audit file to ensure that this consideration has been completed in respect of all covered persons for the engagement. Team members are required to declare any potential conflicts between themselves and the audited entity and any connected parties (for example if they were connected to the management expert used to support a balance in the financial statements).

8.49 The engagement team should clearly document all threats to objectivity, integrity and independence which are relevant to an engagement on the audit file (within the Engagement Risk Assessment Audit Form) together with any safeguards which may have been implemented to eliminate the threat or reduce these threats to a level at which independence is not compromised. Any communications from FAPQ or Private Office relating to these threats to independence should also be documented within the audit file. For personal and sensitive matters that impact upon independence, integrity or objectivity, a file note should be included that notes that safeguards and refers to the Ethics Function for detail of the nature and context of the threat.

8.50 ***Consultation required*** Where an audited entity or third party have raised concerns surrounding the objectivity, integrity and independence of the C&AG, the NAO and any covered persons these matters must be referred to the Director, Audit Risk and Compliance.

8.51 Where the EQR forms part of the safeguard to mitigate a threat to independence, the EQR should clearly document the actions which they have taken as part of their role in acting as a safeguard against the identified threat.

8.52 If, during the period covered by an engagement, an entity relevant to the engagement is acquired by, merges with, or acquires another entity, the NAO and each relevant Engagement

Director should identify and evaluate any current or recent interests or relationships, including any non-audit or additional services provided to that entity, which, taking into account available safeguards, could compromise the integrity, objectivity or independence of the NAO or covered persons and the ability to continue with the engagement after the effective date of the merger or acquisition. Paragraph 1.31 of the Revised Ethical Standard 2024 sets out the timeframe and provisions specific to Public Interest Entities in relation to this.

Ethical threats – descriptions

8.53 The principal types of threats to the auditor's objectivity and independence are (Section 1, Revised Ethical Standard 2024):

Self-interest threat

8.54 A self-interest threat arises when the NAO, staff or any covered person for an engagement has financial or other interests which might cause the NAO or the covered person to be, or perceived to be, reluctant to take actions in connection with the engagement that would be adverse to the interests of the NAO or any individual in a position to influence the conduct or outcome of the audit.

Self-review threat

8.55 Self-review threats are discussed in 'Section 5: Non-audit/additional services' of this Chapter.

8.56 A self-review threat may also arise if an engagement team or a member of the engagement team provides detailed guidance on how to treat a transaction or apply an accounting standard.

Management threat

8.57 Supporting Provision A2.1 of the Revised Ethical Standard 2024 prohibits the NAO and employees of the NAO from taking decisions on behalf of the management of the audited entity. Paragraph 5.18 of the Revised Ethical Standard 2024 specifically prohibits the provision of any non-audit services involving taking decisions on behalf of management. A management threat can also arise when the NAO or a covered person undertakes an engagement to provide non-audit services in relation to which management are required to make judgments and take decisions based on that work. In such work, the NAO or the covered person may become closely aligned with the views and interests of management and the auditor's objectivity and independence may be impaired, or may be perceived to be, impaired. The Revised Ethical Standard 2024 determines that in such circumstances, the threat to independence and objectivity arising from playing such a role is so great that it cannot be safeguarded.

8.58 The NAO should not accept any engagement which includes the provision of services where it is probable that an objective, reasonable and informed third party would conclude that the NAO or a covered person was playing a part in management decision-taking.

8.59 It is not possible to specify all types of decision that are the responsibility of management, but they typically involve leading and directing the entity, including making significant judgments and taking decisions regarding the acquisition, deployment and control of human, financial, physical and intangible resources. Examples of judgements and decisions that should not be made by the NAO or a covered person include:

- setting policies and strategic direction;
- directing and taking responsibility for the actions of the entity's employees;
- authorising transactions;

- deciding which recommendations of the NAO or other third parties should be implemented, recognising that a greater threat exists where management are considering recommendations made by the NAO, where there is no alternative course of action;
- taking responsibility for the preparation and fair presentation of financial statements in accordance with the applicable financial reporting framework;
- taking responsibility for the preparation and presentation of subject matter information in the case of another public interest assurance engagement; and
- taking responsibility for designing, implementing and maintaining internal control.

8.60 NAO staff must not provide advice on the purchase or sale of specific investments, including recommendations on the use of cash, other investments or insurance policies. Advice includes commentary in written reports, e-mails or verbal communication.

Advocacy threat

8.61 An advocacy threat arises when the NAO undertakes work that involves acting as an advocate for an audited entity and supporting a position taken by management in an adversarial or promotional context. In order to act in an advocacy role, the NAO has to adopt a position closely aligned to that of management. This creates both actual and perceived threats to the integrity, objectivity and independence of the NAO and covered persons.

Familiarity (or trust) threat

8.62 A familiarity (or trust) threat arises when the NAO or a covered person is predisposed to accept or is insufficiently questioning of the audited entity's point of view (for example, where close personal relationships are developed with the audited entity's personnel through long association with the audited entity).

Intimidation threat

8.63 An intimidation threat arises when the conduct of the NAO or a covered person is influenced by fear or threats (for example, where the engagement team encounters an aggressive and dominating individual).

8.64 These categories may not be entirely distinct and certain circumstances may give rise to more than one type of threat.

Section 2: Financial, business, employment and personal relationships

8.65 This section outlines the requirements and guidance on the specific circumstances arising out of financial, business, employment and personal relationships with audited entities which may threaten the auditor's objectivity or independence. It provides examples of safeguards which can eliminate or reduce the threat to an acceptable level and requires that where this is not possible, the relationship is not entered into or the engagement is withdrawn from.

8.66 In this section, a 'person closely associated' has the meaning defined in the FRC's *Glossary of Terms – Ethics and Auditing* (Updated December 2019). This definition is also described in the Definitions section later in this Chapter.

Current NAO staff and employment at an audited entity

8.67 The NAO should not employ a person to undertake audit work if that person is also employed by the audited entity or by any affiliate of such an entity.

8.68 ***Consultation required*** Where audit staff are considering applying for a role with any NAO audited entity they:

- have worked on within the last two years;
- are currently performing work on; or
- expect to be allocated to in the current audit cycle,

that staff member must inform their line manager, their Group People Development Director, the Chief People Officer, and the Director, Audit Risk and Compliance or (for staff in the Value for Money Service Line) the Director, Value for Money Practice and Quality at the earliest point, and this should be prior to applying for the position. The individual should be removed from the engagement team and the above persons updated on the progress of their application, including whether it results in acceptance of a job offer.

8.69 ***Consultation required*** Staff in grades at and above Audit Manager/Band 1, and colleagues responsible for managing projects and engagements, are required to notify immediately their line manager, their Group People Director, the Chief People Officer, and the Director, Audit Risk and Compliance or (for staff in the Value for Money Service Line) the Director, Value for Money Practice and Quality of any potential employment with an entity audited by the NAO.

8.70 ***Consultation required*** All other grades/roles are required to notify the persons stated above where future employment with an audited entity is probable.

8.71 Any disclosure will be treated in confidence.

8.72 Where a member of staff leaves the NAO to take up employment with an audited entity where they have been a covered person for an engagement relevant to that entity in the current audit cycle, all work which they have performed on that relevant engagement must be re-reviewed by the Engagement Director. Where the member of staff has worked on the audit within the last year (or two years in the case of an Engagement Director), the Engagement Director should determine and document whether it is appropriate to review the work performed on the previous year's audit.

8.73 Where the Engagement Director leaves to take up employment at an audited entity and they have been a covered person for an engagement related to that entity, the entirety of the audit file will need to be re-reviewed and approved by the incoming Engagement Director or Executive Director as appropriate.

8.74 Where an Engagement Director or Executive Director leaves the NAO, they are not permitted to take up any of the following positions at entities where they have been members of the engagement team for a period of two years following the date upon which they ceased to be a member of that entity's engagement team:

- A key management position at the entity, where they can influence the strategic or operational decision making of the entity.
- Audit committee member.
- Director of the entity (or equivalent).
- Member of the entity's management board (or equivalent).

These restrictions do not extend to Executive Directors' role as a covered person by virtue of being a member of the Executive Team, unless they have actively participated in the audit, such as by being a member of an audit panel or undertaking file review.

8.75 ***Consultation required*** The engagement team will be required to document their consideration of whether the individuals within any of the positions noted above are former employees of the NAO as part of their preliminary engagement procedures. The threats to integrity, objectivity and independence are most pronounced when the individual was a senior member of

NAO staff (i.e., Director or above), or a member of the audit team in the previous two audit cycles, or worked on any audit in the past two audit cycles with the Engagement Director as either a co-Director or as an Engagement Quality Reviewer. Where this is the case and consideration by the Ethics Function has not already occurred, the engagement team should consult with the Ethics Function, who will advise on whether any further safeguards may be required. Consultation is not required for staff below Director level who have been promoted to more senior levels in the audited entity, or other ex-NAO staff members who left the NAO over two years ago, unless the Engagement Director considers there to be a threat and is in doubt as to the action they should take. The audit file should document the audit team's assessment supporting the decision not to consult.

8.76 Where such a position as highlighted above is entered into by a former Engagement Director, the new Engagement Director shall ensure that appropriate safeguards are put in place to mitigate any threats to independence. This may include rotating engagement personnel to remove any individuals with a personal connection to the former Engagement Director from the engagement, or resignation from the engagement where this is possible.

8.77 ***Consultation required*** Where an Executive Director or former Executive Director wishes to take up a position at an audited entity within 2 years of their final day of employment at the NAO, they should make the Director, Audit Risk and Compliance aware of this at the earliest opportunity. An assessment of any threats to independence will be undertaken and relevant safeguards implemented prior to the Executive Director or former Executive Director concerned accepting the appointment. This may include resignation from the engagement where this is possible and consideration, such as around the team composition, where this is not possible.

8.78 Where FAPQ are made aware that former senior NAO staff have taken up a position at an audited entity, they will inform the relevant portfolio director.

8.79 ***Consultation required*** If the C&AG leaves the NAO to take up a senior position at an NAO audited entity, the Engagement Director should confirm with the Ethics Function before any further audit work is undertaken that no connections remain between the NAO and the former C&AG. This requires that:

- all financial interests be fully settled (including retirement benefits) unless these are made in accordance with pre-determined arrangements that cannot be influenced by any remaining connections between the former C&AG and the NAO; and
- the former C&AG does not participate or appear to participate in the NAO's business or professional activities by way of employment, consultancy or other contractual arrangement, or in any other way.

8.80 Where a former director or person who was in a position to significantly influence the audited entity, the preparation of its financial statements or other subject matter information or subject matter of such an engagement joins the NAO, they should not be placed in a position where they act as covered person on the engagement for that entity or its affiliates for a minimum period of two years.

Financial interests[2] and business interests

8.81 In relation to an audited entity, the parent body of an audited entity, any subsidiary of an audited entity or any other entity otherwise related to such an audited entity, in circumstances that may cause, or may be perceived by an objective, reasonable and informed third party as causing, a

[2] The Revised Ethical Standard 2024 provides in paragraph 2.1 and 2.2 definitions of financial instruments and financial interests that are covered by this section.

self-interest threat, the NAO, Executive Team[3] and covered persons relevant to an engagement, together with any persons who are closely associated to them, may not:

- Hold a direct financial interest.
- Hold an indirect financial interest (other than interest held through a diversified collective investment scheme) that is material to the NAO, the individual concerned or the audited entity.
- Make loans or deposits or accept loans or guarantees unless these transactions, loans or guarantees are made with banks or similar institutions in the ordinary course of business, on ordinary credit terms and are not material to either party.
- Hold or enter into business relationships. Business relationships with management are also excluded. Where such a relationship is entered into the relevant individual should cease involvement in the engagement. However, this does not include business relationships involving the purchase of goods and services in the ordinary course of business and on an arms-length basis and which are not material to either party, or where the value of the transaction would be inconsequential to either party in the view of an objective, reasonable and informed third party.
- Enter into employment relationships or be employed by the types of entities listed above. Where a person has such an employment relationship, they shall be prevented from acting as a covered person on the relevant engagement.
- Take up any positions as directors or officers of within the types of entities listed above. Similarly, such persons should not take up positions on sub-committees of the Board of such entities or be in a position to hold either directly or indirectly more than 20% of the voting rights in such an entity.

8.82 ***Consultation required*** Covered persons must inform the Engagement Director where they become aware that either they or a person closely associated with them have acquired a financial interest in an audited entity, the parent body of an audited entity or a subsidiary of an audited entity. The Engagement Director must consult with the Ethics Function where the financial interest has been acquired by the Engagement Director, a person closely associated with them or a 'close family member' or if and the Engagement Director is in doubt as to the action they should take in relation to declarations by members of their team.

8.83 All NAO Directors, Executive Directors and persons closely associated with them may not hold a direct or indirect financial interest in an audited entity, the parent body of an audited entity or any subsidiaries of an audited entity that is material to the NAO, the individual concerned or the audited entity.

8.84 All NAO Directors, Executive Directors and persons closely associated with them may not make loans or deposits or accept loans or guarantees with audited entities, their parent bodies and any subsidiary bodies of audited entities unless these transactions, loans or guarantees are made with banks or similar institutions in the ordinary course of business and on ordinary credit terms.

8.85 ***Consultation required*** Where arrears exist on any loans made by an audited entity, its parent body or the audited entity's subsidiaries to a covered person or a person closely associated with them, the covered person must alert the Engagement Director, HR and the Director, Audit Risk and Compliance of this fact promptly.

8.86 ***Consultation required*** Where a covered person becomes aware that either they or a closely associated person have entered into a business relationship with an audited entity, the parent body or an audited entity or a subsidiary of an audited entity, they should inform the Engagement Director. Where a business relationship has been entered into by the Engagement

[3] The Revised Ethical Standard 2024 has been interpreted in the context of the NAO. The Ethical Standard wording includes "Partners within the firm", which has been omitted in favour of "covered persons relevant to the engagement". NAO Directors do not have the same level of oversight and control as in a private sector firm and thus, are unable to influence the conduct and outcome of an audit through holding a relationship or connection with an audited entity outside of their portfolio. Covered persons includes the Engagement Director for an audited entity who act independently of and are not influenced by other Engagement Directors.

Director, a person closely associated with them or one of their close family members, or the Engagement Director is in doubt as to the action they should take regarding a declaration by members of their team, they must consult with the Ethics Function.

8.87 The expectation is that where business relationships which do not meet the criteria set out in paragraph 2.26 of the Revised Ethical Standard 2024 exist between either the NAO, a covered person or a person closely associated with them and an audited entity, the parent body of an audited entity, any subsidiary of an audited entity or any other entity otherwise related to such an audited in circumstances that may cause, or may be perceived by an objective, reasonable and informed third party as causing, a self-interest threat or members of management, that the relevant business relationship would be terminated at the earliest possible opportunity. Where this is not possible, then the relevant covered person should be removed from their role as a covered person on the engagement. If the relationship is held by the NAO, the NAO would withdraw from the engagement where possible, and otherwise put in place relevant safeguards and communications of these to Those Charged with Governance.

8.88 Where the NAO enters into a business relationship with an audited entity or a connected party, an ethical assessment will be made by the Ethics Function, the outcome of which will be communicated to the Engagement Director.

Secondments

8.89 ***Consultation required*** Some NAO staff are seconded to central government bodies. HR obtain advice from the FAPQ team on ethical issues relating to secondment opportunities to audited entities, including safeguards to be put in place and will not proceed with secondments for which adequate safeguards cannot be implemented that reduce actual and perceived threats to independence to a tolerable level. Responsibility for implementing these safeguards rests with HR, the Engagement Director and the wider engagement team. Any secondments to audited bodies must be approved by the relevant Executive Director for the Group.

8.90 ***Consultation required*** Some staff from audited bodies may be seconded to the NAO. HR obtain advice from the FAPQ team on ethical issues relating to inwards secondments including safeguards to be put in place. Secondments will not be put in place where adequate safeguards cannot be implemented that reduce actual and perceived threats to independence to a tolerable level. Responsibility for implementing these safeguards rests with HR, the Engagement Director and the wider engagement team. Any inward secondments from audited bodies and their connected bodies must be approved by the relevant Executive Director for the Group.

8.91 Secondments to audited bodies, their affiliates, parent bodies and subsidiaries of audited bodies may only be approved where they are less than twelve months in duration and do not involve NAO staff being involved in the preparation of the financial statements of audited bodies, their affiliates, their parent bodies and subsidiaries of audited bodies or being in a position to influence the decision making of the entity. The role should not involve the provision of prohibited non-audit services per the Revised Ethical Standard 2024 or be to the most senior roles in the Civil Service.

8.92 Audited entities, their affiliates, their parent bodies and subsidiaries of audited bodies at which NAO secondees are based must acknowledge responsibility for managing and supervising the activities of the secondee whilst on secondment. They must also confirm that the secondee will not be in a position to exercise discretionary authority to commit the entity to a particular position or accounting treatment and also that management will not solely rely on the secondee's work for decision making.

8.93 Upon return of the secondee to the NAO, appropriate safeguards will be implemented to reduce any residual risk to objectivity, integrity or independence to an acceptable level. Such safeguards will ensure that the returning secondee will not be given any role relating to the entity at which they were seconded for a period of at least 2 years. Safeguards determined by the Ethics Function will be communicated to the relevant Engagement Director.

8.94 Similarly, any secondments into the NAO from audited bodies will only be permitted for a short time frame. Any such secondees will not be permitted to undertake work on engagements relevant to the audited body which they have been seconded from and its connected bodies.

Family, friends and past NAO staff employed by audited entities

8.95 ***Consultation required*** Where a covered person becomes aware that a person closely associated with them (as defined in the FRC's) becomes employed in a position at an audited entity where they can influence the accounting records or financial statements or other subject matter information or subject matter of such an engagement, then they should inform the relevant Engagement Director. It would be usual in such circumstances for the relevant covered person to be removed from their role as a covered person. Where the covered person concerned is the Engagement Director, they must consult with the Ethics Function as to the appropriate course of action to mitigate the threat to independence.

8.96 Where the NAO or any member of staff (in particular, any a covered person relevant to the engagement) or person closely associated or close with them is appointed to a position as a director or officer of:

- an audited entity;
- a sub-committee of the board;
- an entity which holds directly or indirectly more than 20% of the voting rights in the entity relevant to an engagement; or
- an entity in which the entity relevant to such an engagement holds directly or indirectly more than 20% of the voting rights,

then the covered person concerned should inform the relevant Engagement Director, who will put in place appropriate safeguards to mitigate the risks to independence.

8.97 In circumstances where a covered person becomes aware that they or persons closely associated to them have entered into a relationship with an audited entity, management of an audited entity, its parent body or the subsidiaries of an audited entity, which may create a threat to independence then they must inform the relevant Engagement Director promptly. The Engagement Director will then be responsible for putting in place appropriate safeguards to reduce the risk arising from the threat to an acceptable level.

8.98 The Engagement Director should ensure that they have obtained sufficient information from any external consultants or experts, including contractor auditors, who have been involved in the engagement concerning financial interests, business relationships, employment and personal relationships to be able to assess any potential threats to independence arising from these in the context of the engagement.

Section 3: Long association with the audit engagement and with entities relevant to engagements

8.99 The NAO shall monitor the length of time which directors and staff in senior positions serve as members of the engagement team, to manage the perceived threat to objectivity and independence which might result from long association. This section lists the safeguards that should be introduced including rotating audit partners and involving additional partners and internal quality reviews. It sets out limits to the periods of time for which an individual can act in a senior role on

audits: for example, that no-one should act as an Engagement Director on an individual audit for more than five years, except where approved in line with the requirements below.

8.100 For public interest entities and other listed entities, there are requirements for audit firm rotation which are set out in legislation. The NAO must ensure that it does not accept or continue an audit engagement that would breach those requirements.

8.101 Except where approved in line with the requirements below, Engagement Directors must be rotated at least every five years. This includes time spent participating in an engagement where an audit engagement has moved between firms. Where an individual has acted as Engagement Director for an audited entity for a period of five years, they should not subsequently participate in the audit engagement until a further period of five years has elapsed. This includes not undertaking a role as Engagement Quality Reviewer (EQR) during this period. If the role of Engagement Director is delegated the same rotation policy applies to the individual delegated the role and rotation continues to apply to the Portfolio Director. On completing their rotation, the Engagement Director should not continue to have significant or frequent interaction with senior management, or with those charged with governance of the entity they have previously audited.

8.102 Where an Engagement Quality Reviewer (EQR) becomes the Engagement Director, the combined period of service in these positions shall not exceed seven years. Any individual who has acted as an EQR and/or Engagement Director for an audited body for a full five years shall not participate in the audit engagement until a further five years has elapsed. This should include any time spent participating in an engagement where an audit engagement has moved between firms.

8.103 The Engagement Director is responsible for ensuring that any previous Engagement Director who has been rotated off the audit in order to comply with the requirements of this section is not in a position where they can exert significant influence over the engagement. This includes ensuring the outgoing Engagement Director does not continue to have significant or frequent interactions with management or those charged with governance.

8.104 In certain limited circumstances where there is a clear audit quality reason to do so, an individual may act as Engagement Director for an additional year. Where this reason remains valid after this first year, this may be extended for one more year but only after another application to do so. This means that the maximum term for an Engagement Director, in limited circumstances, would be f seven years, conditional on approval being granted for the extensions.

8.105 Approval for an extension to an individual's term as Engagement Director will not be given where the individual concerned has previously acted as the EQR on the engagement and the combined period of service in these positions would exceed seven years if approval for the extension was given.

8.106 ***Consultation required*** Any request for an individual to act as an Engagement Director for longer than a period of five continuous years must be approved by the Executive Director of Financial Audit based on a recommendation from the Director, Audit Operations following review and approval by the Director, Audit Risk and Compliance. Such requests may not be made for audits of public interest entities unless they meet the requirements for extension set out in Chapter 45: Public Interest Entities. Requests may only be made for listed entities when all of the following conditions apply:

- the decision is made by the audited entity's audit committee (although the NAO may propose an extension);
- the decision is made on the grounds of audit quality;
- the decision is made before any audit planning or other work on the engagement is undertaken; and

- the decision does not look to reinstate an Engagement Director who rotated off in the last five years, after five years in the role.

8.107 Any requests to extend the period of time for which an individual acts as Engagement Director must set out the case for extension, clearly explaining why the extension supports audit quality, together with any proposed safeguards to mitigate the additional threat from familiarity posed by the extension. Following approval of any such extension, the extension and any safeguards to mitigate the risk associated with long associated must be communicated to those charged with governance and approval documentation retained on the audit file.

8.108 An individual would not normally act as the Engagement Director or the EQR of a public interest entity for a period of longer than five years. Where an individual who was previously the EQR becomes the Engagement Director on the audit of a public interest entity, the combined length of time in both roles would not normally exceed five years.

8.109 The NAO seeks to avoid rotating the entirety of an engagement team below Engagement Director at the same point in time, particularly where such a rotation would also coincide with the end of the fifth year of the Engagement Director's tenure. In such circumstances, an extension to the Engagement Director's tenure will only be approved in the exceptional cases where it is not possible to avoid the rotation of other engagement team members.

8.110 The Engagement Director should ensure that other team members are not involved in the engagement for more than 7 years.

8.111 Where it has been determined that the Engagement Director may act for a further period (not exceeding two years), this fact, the reasons for it, and relevant safeguards applied should be disclosed to those charged with governance at the audited entity and approval documentation retained on the audit file.

8.112 In determining whether the periods for rotation have been met, where there are significant gaps in service (for instance, caused by a period of maternity or paternity leave, a sabbatical or long-term sickness absence and the role is taken on by another person) the NAO should exclude this period for the purposes of calculating applicable rotation periods. Any periods excluded should be long-term in nature and should not comprise multiple smaller blocks of time aggregated together. If the person in substance retains their role, then that period of absence should not be excluded for the purposes of calculating the rotation period.

Section 4: Fees, remuneration and evaluation policies, litigation, gifts and hospitality

8.113 Circumstances involving the charging of fees, and any resulting economic dependence, litigation, remuneration and gifts and hospitality may threaten the auditor's objectivity or independence.

Gifts

8.114 Gifts, favours and hospitality from an audited entity or any other entity related to that entity should not be accepted by the NAO, covered persons relevant to the audit or persons closely associated with them, unless the value is clearly insignificant and hospitality (including travel and accommodation offered by the audited entity) should not be accepted unless it is reasonable in terms of frequency, nature and cost. Audit teams should also not offer gifts, favours or hospitality to audited entities or entities related to them unless clearly insignificant and consider the threats posed by any gifts, favours or hospitality provided prior to formally accepting the audit. Further detail on these matters is contained within the Code of Conduct.

8.115 ***Consultation required*** The cumulative effect of multiple insignificant instances should be considered in assessing the threats to independence, objectivity and integrity. Where there is any doubt as to the acceptability of gifts, favours or hospitality offered by the entity, members of the engagement team should discuss the position with the Engagement Director. If there is any doubt as to the acceptability of gifts, favours or hospitality offered to the Engagement Director, or if the Engagement Director has any residual doubt about the acceptability of gifts, favours or hospitality to other individuals, the Engagement Director should report the facts to the Ethics Function, for further consideration regarding any action to be taken.

Fees

8.116 The level of fees charged to audited entities for audit engagements should be assessed on an individual engagement basis with regard to the guidance provided in the NAO's Finance Manual. Fees for the provision of engagements, non-audit and audit-related services to an entity relevant to an engagement, its UK parent undertaking and any worldwide controlled undertaking shall not be contingent fees.

8.117 Contingent fees are fees calculated on a predetermined basis relating to the outcome or result of a transaction, or other event, or the result of the work performed. Additional or supplementary fees paid over and above an agreed engagement fee, which do not cover the cost of additional work, but reward an outcome which was not agreed at the time of the engagement letter are also contingent fees. Fees are not contingent if a court, competent authority, or other public authority has established them.

8.118 ***Consultation required*** If fees for professional services, including any audit fees, are overdue and the amount is non-trivial (i.e. more than 10% of the annual audit fee), the Engagement Director must consult with the Director, Audit Risk and Compliance, who will consider the circumstances (for example: dispute, financial distress etc.) and what safeguards may be applied.

8.119 The Revised Ethical Standard 2024 includes a provision which requires auditors to consider whether an objective, reasonable and informed third party would conclude that it is probable that the independence of the auditor would be compromised as a result of the fee charged for the audit. In the context of the NAO, where the basis of the audit fee is calculated as full cost recovery, the only context where this may be applicable is to audits with a significant fee deficit or significant over-recovery of fees.

8.120 ***Consultation required*** The basis on which the NAO is funded, via Supply, and the fact that Director remuneration is not directly linked to fee recovery significantly mitigates against this risk. However, where fee deficit or over-recovery of fees is between 10% and 50% of the audit fee, the mitigating factors (such as the fact the NAO is Supply funded, the lack of link of Directors' remuneration to audit outcomes and the circumstances which led to the under-/over-recovery) should be formally documented within the audit file. Where fee deficit or over-recovery is over 50% of the audit fee, the engagement team should consult with the Ethics Function to consider whether further safeguards are required and whether reporting is required to those charged with governance.

8.121 ***Consultation required*** Where the fees for any additional or non-audit services performed by the NAO that are provided to an audited entity and its group exceed the statutory audit fee charged to the audited entity for the year, the Engagement Director should consider the threats that this poses to integrity, objectivity and independence. In such circumstances, the Engagement Director should ensure that appropriate safeguards are put in place to mitigate any threat to an appropriate level and determine whether communication is required to those charged with governance (especially where large fees are recurring). Such safeguards may include ceasing to

provide the relevant additional or non-audit service. The engagement team should also consult with the Ethics Function.

8.122 ***Consultation required*** Where the audit fees from an individual audited entity and its subsidiary bodies or a collection of entities with the same beneficial owner or controlling party (which is not a corporate holding entity) exceed 5% of the NAO's total audit fee income on a regular basis, the Engagement Director must consult with the Ethics Function. As a guide, this threshold is likely to be at risk of being exceeded where those fees total £1,000,000 or higher. Where it is possible for the C&AG to withdraw from the engagement, this will be considered. Where it is not possible to withdraw from the engagement, alternative safeguards to mitigate the risk as far as is feasible will be introduced. The Ethics Function will consider whether the appointment of an EQR is appropriate or required under the Revised Ethical Standard 2024. Communication should be made to Those Charged with Governance outlining the considerations of the threats and safeguards concluded upon.

8.123 ***Consultation required*** Where a cash audit fee in excess of £1,500,000 is proposed, approval of the fee charged must be obtained from the Director, Audit Risk and Compliance.

8.124 A full assessment of compliance with Section 4 of the Ethical Standard should be retained on the audit file for any engagements to provide additional or non-audit services where the fee charged for the additional services exceeds either the fee charged for the audit or £10,000.

8.125 ***Consultation required*** Where the audit fee charged is likely to be less than 50% of projected audit costs, the engagement team should consult with the Ethics Function.

Litigation

8.126 ***Consultation required*** Where there is outstanding litigation or legal matters between the NAO and an audited entity, the Engagement Director must undertake an assessment of whether this poses a threat to integrity, objectivity and independence. In such circumstances, the Engagement Director should consult with the Ethics Function where there is uncertainty.

Section 5: Non-audit/additional services

8.127 The provision of non-audit services to the audited entity may threaten the auditor's independence. For audited entities, other additional work that:

- does not relate to financial information and/or financial controls; or
- is not integrated with the work performed in the audit, or is not performed largely by the existing audit team; or
- is not on the same principal terms and conditions as the audit,

will be regarded as an "other non-audit service" for the purpose of the Revised Ethical Standard 2024.

8.128 The Ethical Standard defines 'non-audit services' as any engagement in which an audit firm provides professional services to an audited entity, its affiliates or another entity in respect of the audited entity, other than the audit of financial statements. Non-audit services funded or scoped by an audited entity but where the non-audit service is not conducted on that entity, and non-audit services to an entity where the subject matter is connected to another of the NAO's audited entities, should be considered in scope of the requirements set out below and considerations relating to the impact upon the integrity, independence and objectivity of the engagement team.

8.129 In the case of a public interest entity or other listed entity, the Engagement Director will need to establish that the audited entity has communicated a policy (as required under the UK Corporate Governance Code) on the use of the NAO or the NAO's contractor audit firms where applicable to supply non-audit or additional services to its affiliates. It is recommended that this is documented within the Set Up Checklist in Apex.

8.130 In the public sector, the statutory scope of an audit can extend beyond expressing an independent opinion on an entity's financial statements to include reporting on an entity's arrangements to ensure the proper conduct of its financial affairs, manage its performance or use of its resources, meaning that all statutory work performed by the NAO on behalf of the C&AG is excluded from the definition of non-audit services.

8.131 Threats to the NAO's objectivity and independence can arise from work that is performed (including VfM studies), even where such work is performed within the C&AG's statutory remit. However, Value for Money and wider assurance reports (including 'economy, efficiency and effectiveness' examinations under Part 2 of the National Audit Act 1983) do not meet the definition of non-audit services[4], because the services are not provided to, commissioned or scoped or paid for by the entity being examined, but rather are performed for and funded by Parliament.

8.132 Before discussing or facilitating any non-audit or additional service that might be provided by the NAO, the Engagement Director should consider the threats that such a service would have on the engagement and whether it is probable that an objective, reasonable and informed third party would conclude that the integrity, objectivity or independence of the NAO or covered persons are compromised. The Engagement Director should consider whether the outcome of that service has a material impact on the financial statements or other subject matter information of another NAO audit.

8.133 The Engagement Director should ensure that the reasoning for a decision to provide non-audit services to an audited entity (in particular as part of a separate engagement), is appropriately documented prior to the engagement letter for the service being issued to the entity. Guidance on matters to consider is outlined in paragraphs 5.13 and 5.14 of the Revised Ethical Standard 2024. The Engagement Director is required to consider the threats and safeguards available when initially considering providing the non-audit/additional service and to review these each year and/or if the scope or objectives of these services changes significantly.

8.134 Matters to be documented include all key elements of the process and any significant judgments concerning:

- threats identified, other than those which are clearly insignificant, and the process used in identifying them;
- safeguards adopted and the reasons why they are considered to be effective;
- the need for and nature of review by an EQR or other independent director of both the non-audit/additional services and the audit, including communications to the EQR by the Ethics Function of the circumstances concluded as potentially giving rise to self-review threat (confirmation to the Ethics Function that any concerns raised by the EQR have been satisfactorily resolved before signature of the opinion is captured via standard EQR process);
- overall assessment of threats and safeguards, including whether there is 'informed management' when a potential management threat is identified; and
- communication with those charged with governance.

8.135 ***Consultation required*** In situations where a management threat is identified in connection with the provision of non-audit services or advice or support provided to the audited entity, this

[4] The Glossary of Terms – Ethics and Auditing (Updated December 2019) defines non-audit services as "Any engagement in which an audit firm provides professional services to an audited entity, its affiliates or another entity where the subject matter of the engagement includes the audited entity and/or its significant affiliates other than the audit of financial statements of the audited entity."

documentation should include the Portfolio Director's assessment of whether there is informed management. The Portfolio Director must consult with the Ethics Function in all such instances. The NAO should not accept a non-audit or additional service engagement that would require a covered person to play any part in the management decision-taking of the entity. Such engagements are prohibited.

8.136 The NAO provides limited assurance services such as grant certification work to some audited entities in addition to statutory audit work. Although these services are all assurance work, they should be considered under the framework for non-audit services set out in the Ethical Standard.

8.137 Although it is rare for the NAO to be formally engaged to provide significant non-audit services, there may be similar self-review, advocacy and management threats when assistance is provided to an audited entity that goes beyond auditing their financial statements.

8.138 A self-review threat exists when the results of a non-audit/additional service, or the subject matter of such service, whether performed by the NAO, the engagement team or others within the firm, are addressed in the engagement or reflected in the amounts included or disclosed in the financial statements or other subject matter information of the engagement (for example: where the engagement team are involved in determining the accounting entries for a transaction or the preparation of the financial statements).

8.139 A threat to objectivity and independence arises because, in the course of the audit, the engagement team may need to re-evaluate the work from the non-audit service. By virtue of providing the non-audit service, the NAO is associated with aspects of the preparation of the financial statements and may (or appear to) be unable to take an impartial view of relevant aspects of those financial statements.

8.140 Where a non-audit/additional service provided by the NAO requires the NAO, staff or covered persons relevant to the engagement to act as an advocate for an entity in relation to matters which are material to the financial statements or other subject matter information, or to the subject matter of an engagement, it is unlikely that any safeguards can eliminate or reduce the advocacy threat to a level where independence would not be compromised.

8.141 As part of the engagement acceptance process discussed in Chapter 9: Engagement acceptance (statutory and non-statutory), before accepting an engagement to provide a non-audit service to an audited entity or providing assistance beyond auditing the financial statements, the Portfolio Director should:

- consider whether it is probable that a reasonable and informed third party would regard the objectives of the proposed engagement as being inconsistent with the objectives of the audit of the financial statements;
- identify and assess the significance of any related threats to the auditor's objectivity, including any perceived loss of independence; and
- identify and assess the effectiveness of the available safeguards to eliminate the threats or reduce them to an acceptable level.

8.142 All engagements (audit and non-audit) are subject to approval by the C&AG.

8.143 In assessing the significance of a self-review threat arising from a non-audit service, the Engagement Director should consider the extent to which the non-audit or additional service will:

- involve a significant degree of subjective judgment; and
- have a material effect on the preparation and presentation of the financial statements or other subject matter information or subject matter of the engagement.

8.144 ***Consultation required*** Where any threat to the NAO's objectivity and independence is identified, the Portfolio Director assesses the significance of that threat and considers whether there are safeguards that could be applied and which would be effective to eliminate the threat or reduce it to an acceptable level. If such safeguards can be identified and are applied, the non-audit service may be provided. In these circumstances, the Engagement Director should consult with the Director, Audit Risk and Compliance.

8.145 Where the Engagement Director or Director, Audit Risk and Compliance concludes that no appropriate safeguards are available to eliminate or reduce to an acceptable level the threats to the NAO's objectivity, including any perceived loss of independence, related to a proposed engagement for a non-audit service for an audited entity, the NAO should either:

- not undertake the non-audit service engagement; or
- not accept or withdraw from the audit engagement.

8.146 ***Consultation required*** In the circumstance outlined in the previous paragraph, where the threat of non-audit services cannot be reduced to an acceptable level, the Engagement Director should consult with the Director, Audit Risk and Compliance. For many audited entities, the NAO is the statutory auditor and so it would not be possible to withdraw from the audit engagement. In these circumstances, it would not be possible to undertake the non-audit service. The Portfolio Director must consult with Director, Audit Risk and Compliance in these circumstances.

8.147 Where a significant degree of judgment relating to the financial statements is involved in a non-audit service or additional service engagement, the engagement team may be inhibited from questioning that judgment in the course of the audit. Whether a significant degree of subjective judgment is involved will depend upon whether the non-audit service or additional service involves the application of well-established principles and procedures, and whether reliable information is available. If such circumstances do not exist because the non-audit service or additional service is based on concepts, methodologies or assumptions that require judgment and are not established by the audited entity or by authoritative guidance, the NAO's objectivity and the appearance of its independence may be adversely affected. Where the provision of a proposed non-audit service or additional service would also have a material effect on the financial statements, it is unlikely that any safeguard can eliminate or reduce to an acceptable level the self-review threat.

8.148 All engagement team members should ensure that they are familiar with the requirements for maintaining our independence and any restrictions placed on the scope of our work or safeguards are appropriately followed.

8.149 In performing their work, each member of the team should consider whether the scope of the services being provided is moving beyond simply undertaking an audit and discuss with the Engagement Manager or Engagement Director any concerns that they have. All team members may discuss any concerns that they have with the Ethics Function.

8.150 The Engagement Manager and Engagement Director should consider carefully whether the engagement team are providing assistance to our audited entities that goes beyond the audit role, and if so, what the threats that arise from this are and how to mitigate this risk. This may involve not providing the assistance or putting in place appropriate safeguards.

8.151 ***Consultation required*** Where the Engagement Manager and Engagement Director have determined it would be inappropriate in the circumstances to provide assistance to an audited entity, or where safeguards have been put in place, the Engagement Director must inform the Ethics Function.

8.152 Where an NAO team is proposing to perform an additional engagement or service on behalf of an audited entity, they should ensure that the relevant Portfolio Director has been informed.

8.153 All decisions and judgements surrounding the provision of non-audit services to audited entities should be saved into the relevant audit file for the audited entity.

8.154 Communications are required with Those Charged with Governance where non audit/additional services are provided by the NAO or a contractor audit firm. The communications should outline the nature of the services to be provided, assessment of threats and safeguards, and confirm compliance with the Revised Ethical Standard 2024. Non-audit services should be clearly distinguished in communications from audit related services. Communications should be retained on the audit file.

Accounting services

8.155 "Accounting services" are defined in Section 5 of the Revised Ethical Standard 2024 as "*provision of services that involve the maintenance of accounting records or the preparation of financial statements or other subject matter information or subject matter that are then subject to audit or an other public interest assurance engagement. Advice on the implementation of current and proposed accounting standards is not included in the term accounting services.*."

8.156 The C&AG is responsible for laying the financial statements of a number of our audited entities within the House of Commons under statute. In practice, the NAO has agreed that this duty will be discharged in most cases directly by the Department or the sponsoring Department of the applicable audited entity. However, there remain a few audited entities where the NAO continues to publish and lay annual reports on behalf of audited entities. The NAO does not consider that this activity constitutes Accounting Services under the FRC Ethical Standard as the audited entity remains responsible for the maintenance of its own accounting records and the preparation of the printers proof draft financial statements. The C&AG's responsibilities extends solely to that noted in statute for publication and laying, which does not constitute an accounting service. As this is statutory responsibility of the C&AG, no fees are charged to the audited entity for undertaking this service.

8.157 The C&AG is also responsible for setting an Accounts Direction for a small number of audited entities under statute. This function effectively involves setting the financial reporting framework for the audited entity. The NAO does not consider that this function constitutes accounting services for the purposes of Section 5 of the Revised Ethical Standard 2024 as management remain responsible for the preparation of their own financial statements and the selection of accounting policies under which those financial statements are prepared. As this is a statutory responsibility of the C&AG, no fees are charged to the audited entity or others for undertaking this service.

8.158 The NAO will not provide accounting services to any of its audited entities.

8.159 Although the NAO will not maintain accounting records or prepare an entity's financial statements, the engagement team may be providing commentary to audited entity management which is analogous to accounting services in identifying and posting necessary adjustments in the preparation of the financial statements.

8.160 It is a matter of professional judgement whether there is a threat to objectivity and independence from commentary and recommendations that is given to audited entities. It is usual to provide management with proposed corrections or recommendations on matters that have come to the engagement team's attention during the course of the audit. Such matters might typically include:

- comments on weaknesses in the accounting records and suggestions for addressing them;
- errors identified in the accounting records and in the financial statements and suggestions for correcting them; and
- commentary on the accounting policies in use and on the application of current and proposed accounting standards.

8.161 Commentary and recommendations are a by-product of the audit process and will usually not give rise to a threat to the NAO's objectivity and independence. However, more extensive support on errors or accounting policies might represent a threat.

8.162 If the engagement team is providing extensive support to the audited entity analogous to accounting services, this will create threats to the auditor's objectivity and independence, principally self-review and management threats, the significance of which depends on the nature and extent of the services in question and upon the level of public interest in the audited entity.

8.163 When providing support analogous to accounting services to an audited entity, unless the NAO is working with informed management, there is a risk that the engagement team undertakes a management role.

8.164 To conclude that there is informed management, the engagement team needs to:

- be satisfied that the member of management who will receive the results of the non-audit service has authority to decide whether the NAO's recommendations should be implemented, take responsibility for the preparation and fair presentation of the financial statements, and take responsibility for designing, implementing and maintaining internal control;
- conclude that the member of management has the capability to make independent management judgments and decisions on the basis of the information provided; and
- communicate the results of the work to the audited entity and, where judgments or decisions are to be made provide the support of an objective analysis of the issues to consider and give the audited entity the opportunity to decide between reasonable alternatives.

8.165 The NAO should not provide support to entities where this would involve the NAO undertaking part of the role of management. Engagement teams may only provide support if such support:

- does not involve initiating transactions or taking management decisions; and
- is of a routine, mechanical nature requiring little or no technical judgement; and
- appropriate safeguards are applied to reduce the self-review threat to an acceptable level.

8.166 The maintenance of the accounting records and the preparation of the financial statements are the responsibility of the entity's management. The NAO should not initiate any transactions or take any decisions or make any judgments, which are properly the responsibility of the management. These include:

- authorising or approving transactions;
- preparing originating data (including valuation assumptions); or
- determining or changing journal entries, or the classifications for accounts or transactions, or other accounting records without management approval.

Other non-audit services

8.167 Section 5 of the Revised Ethical Standard 2024 recognises a number of non-audit services which may be provided by audit firms, which may give rise to threats to independence, including:

- information technology services;
- valuation services;
- actuarial valuation services;

- tax services;
- litigation support services;
- legal services;
- recruitment and remuneration services;
- corporate finance services;
- transaction related services;
- restructuring services; and
- services related to the audited entity's internal audit function.

The NAO does not provide any of these services to audited bodies.

8.168 ***Consultation required*** Where contractor audit firms are providing, or propose to provide, these services to audited bodies, the engagement team should consult with the Ethics Function.

8.169 The Revised Ethical Standard 2024 dictates that the NAO (or contractor audit firms in the case of contracted out audits) should not provide internal audit services to entities relevant to the engagement, or to significant affiliates of such entities, where the NAO or contractor audit firm is undertaking an audit engagement. Internal audit services include direct provision and supplementing the entity's internal audit function in specific areas.

Audit-related services

8.170 Audit-related services are those audited services carried out by members of the engagement team where the work involved is closely related to the audit work and is performed on the same principal terms and conditions as the audit. In these cases, the threats to auditor independence are clearly insignificant and, as a consequence, safeguards need not be applied. Audit-related services are:

- reporting required by law or regulation to be provided by the auditor;
- reviews of interim financial information;
- reporting on regulatory returns;
- reporting to a regulator on audited entity assets;
- reporting on government grant;
- reporting on internal financial controls when required by law; or
- extended audit work that is authorised by those charged with governance performed on financial information and/or financial controls, where this work is integrated with the audit work and is performed on the same principal terms and conditions.

8.171 The Engagement Director should ensure that only those non-audit services listed above are described as audit-related services in communications with those charged with governance of the audited entity. Audit-related services require approval by those charged with governance.

Section 6: Provisions available for the audit of small entities

8.172 The NAO does not apply the provisions available for the audit of small entities section of the Revised Ethical Standard 2024 to any of its financial audit engagements.

Section 7: Communication surrounding ethical considerations

8.173 The Engagement Director should ensure that those charged with governance of the audited entity are appropriately informed on a timely basis of:

- all significant facts and matters that bear upon the auditor's objectivity and independence (including in relation to any services or support other than statutory audit), including outlining the principal threats and the safeguards put in place;

- any inconsistencies between the Revised Ethical Standard 2024 and the entity's policy on the supply of non-audit services, and any apparent breach of that policy; and
- ***Consultation required*** in the case of a Public Interest Entity audit, any instances where the person consulting and the Ethics Function disagree on the appropriate action in response to an ethical matter and it is ultimately concluded that the Ethics Function's advice should not be followed. Such matters must also be communicated to the NAO's independent non-executives and to the Financial Reporting Council.

8.174 ***Consultation required*** Any issues should be communicated in writing at the earliest opportunity via the Audit Planning Report, Audit Completion Report or letter following consultation with the Ethics Function.

8.175 The Engagement Director should ensure that the Audit Committee is provided with:

- a written disclosure of relationships that bear on the NAO's objectivity and independence and safeguards that are in place to reduce the threat to auditor independence from these threats;
- details of non-audit/additional services provided to the audited entity and the fees charged in relation thereto;
- written confirmation that the NAO and each covered person is independent;
- details of any inconsistencies between the Ethical Standard and the entity's policy for the supply of non-audit services by the NAO and any apparent breach of that policy; and
- an opportunity to discuss auditor independence issues.

Section 8: Reporting on the financial statements

8.176 In accordance with paragraph 28(c) of ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements*, the auditor's report should confirm that the engagement team has remained independent of the audited entity and has complied with the requirements of the Ethical Standard as applicable to listed entities. For the audit of Public Interest Entities, the auditor's report should state that the engagement team has complied within the requirements of the Ethical Standard as applicable to Public Interest Entities. This disclosure should be included in the Basis for opinion[s] section of the report.

8.177 ***Consultation required*** Where a breach in the requirements of the Ethical Standard has occurred, this should be disclosed within the Basis for opinion[s] section of the auditor's report together with details of any safeguards or other actions which have been taken to mitigate the impact of the breach. Any auditor's reports containing such disclosures must be approved by the Director, Audit Risk and Compliance. The Ethics Function will liaise with FA Compass to report any breaches of the Ethical Standard to the Financial Reporting Council.

Section 9: Providing feedback to audited entities

8.178 Engagement teams may often be asked to provide feedback to audited entity on matters relating to the audit engagement. In doing so, teams should not provide feedback which forms part of the audited entity's formal appraisal feedback that feeds into their performance management system.

8.179 However, where the feedback which is sought is more general and in support of continuous improvement, particularly surrounding how the accounts preparation and audit process could be improved, this may be provided as part of our normal client engagement activities. Where engagement teams are unsure about the nature of feedback being requested, they may consult with the Ethics Function.

Section 5: New engagements and standing information

Chapter 9: Engagement acceptance (statutory and non-statutory)

Relevant standards and guidance

9.1 ISA (UK) 210 (Revised June 2016) (Updated May 2022) *Agreeing the terms of audit engagements* deals with the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance. This includes establishing that certain preconditions for an audit, responsibility for which rests with management and, where appropriate, those charged with governance, are present.

9.2 Paragraphs 1-28 to 1-37 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 210 (Revised June 2016) (Updated May 2022) in the public sector.

9.3 Paragraphs 22 to 24 and the related application guidance of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* set out responsibilities of the Engagement Director, in the role of Engagement Partner, regarding the acceptance and continuance of client relationships and audit engagements.I

9.4 Paragraph 1-5 of Practice Note 10 (Revised 2022), which is based on paragraphs A18-A23 of ISQM (UK) 1, sets out considerations regarding the acceptance and continuance of client relationships and specific engagements where the option of withdrawing from the engagement is not available.

Background

9.5 This Chapter sets out the procedures that should be performed when beginning a new engagement, either with a new client or an existing client, in the situations where the C&AG either is, or is not, required by statute (law or regulation) to undertake the engagement.

Engagement risk management

9.6 The NAO gains appointment to most audited bodies by statute which normally defines the overall scope of the work performed. However, the NAO is often asked to work for bodies and on engagements beyond our current statutory appointment framework. Such work can include audits of audited entities under the Companies Act, project audits, grant certification, due diligence work, specified procedures work and work where the NAO issues any form of other auditor's report or opinion. These assignments bring a different level of risk to our business and are often more unstructured and specialist than our statutory appointment work and may require skills which the NAO does not possess in-house. Many of the audited entities are also new to the NAO and in areas where the NAO may have little knowledge or experience. Failure to assess and consider these

business risks before accepting discretionary audited entities and discretionary engagements could place the NAO's reputation at risk.

9.7 The engagement risk management procedures for financial statement audit and other financial assurance engagements are aimed at understanding and mitigating the assignment and engagement risk for all appointments. These procedures should be followed in all cases. Directors should use their judgement to consider whether to recommend acceptance of an engagement.

9.8 Agreeing the terms of the engagement at the start of the financial statement audit or other financial assurance engagement ensures that there is no misunderstanding with the audited entity as to the terms of the engagement.

9.9 The general requirements for taking on a new audit discussed in this Chapter apply equally to companies.

9.10 The engagement risk management policies and procedures described below apply to all financial statement audit and other assurance engagements.

9.11 Other assurance engagements include all work where the NAO expresses a formal opinion or view to an audited body or third party. The definition includes grant certification work, specified procedures audits and work where the NAO issues any form of auditor/assurance report or opinion about the outcome of the evaluation or measurement of a subject matter (e.g. efficiency savings) against appropriate criteria (e.g. centrally defined benchmarks for savings). Such work does not include our VFM studies. FAPQ may be consulted if directors are not clear whether an engagement falls within the definition of an audit or assurance engagement.

9.12 Key roles in the engagement risk management process are described in ***Table 9A*** below.

Table 9A: Key roles in the engagement risk management process

The Executive Team is the principal risk management committee of the NAO and will consider audited entity acceptance issues of wide-ranging corporate interest and set precedent for the acceptance of engagements.
The C&AG acts as the principal risk manager. He will approve the acceptance of audited entities. He will also be responsible for agreeing the acceptance of new audit and assurance engagements.
The Director, Audit Quality is responsible for supporting the C&AG in the discharge of their risk management role and in providing guidance to directors. They will advise the C&AG on all proposals for new audited entity and engagement acceptances. They will appoint 'Engagement Quality Reviewers' (EQR) for high-risk audits.
Engagement Directors generally discharge the responsibilities of an engagement partner, as defined in International Standards on Auditing (UK). However, where the portfolio director is different to the Engagement Director, it is the portfolio director that considers audited entity and engagement acceptance under our engagement risk management process and makes recommendations to the C&AG through the Director Financial Audit Practice and Quality. The Engagement Director's responsibilities include ensuring the competence of their engagement teams and the quality of the audit and assurance work undertaken.
The Engagement Quality Reviewer (EQR) is independent from an individual engagement, and helps manage engagement audit risk through providing an objective evaluation of the significant judgements made by the engagement team and the conclusions reached in formulating the opinion.
Portfolio Executive Directors are independent from an individual engagement and help manage significant political or reputational risks associated with engagements. They will also be responsible for advising the C&AG on conclusions to key engagement issues (i.e., those that impact his opinion) through the Audit Panel.

Communication with the predecessor auditor

9.13 Where the prospective audited entity is currently audited by another auditor, the Engagement Director should communicate with the predecessor auditor. Teams should use a pro-forma letter to authorise the NAO to contact the outgoing auditors which should be signed by the prospective audited entity and sent to the outgoing auditors to determine if there are any reasons that would cause the assignment to be rejected.

9.14 ***Consultation required*** The Engagement Director should inquire whether there are any circumstances which might suggest that the audited entity or engagement should not be accepted. This should include inquiring with the predecessor auditor as to whether they are aware of any instances of non-compliance with laws and regulations by the audited entity, which the C&AG should be aware prior to accepting the engagement (in accordance with paragraph A55 of ISA (UK) 220 (Revised July 2021)). For agreement (non-statutory) audits, where an outgoing auditor provides reasons why a new assignment should not be accepted, the decision on whether to recommend acceptance of the engagement to the C&AG should be made by the relevant Executive Director on advice from the Director, Audit Quality.

Audited entity acceptance and re-acceptance

9.15 When the NAO takes on a new discretionary audited entity, the NAO needs to consider the risks to it of taking on that audited entity. Examples of the matters the NAO might consider are shown in ***Table 9B***. Over time, the risks associated with an audited entity may change and this assessment should be revisited on at least an annual basis.

Table 9B: Key issues for audited entity acceptance and re-acceptance

The integrity and character of management, those charged with governance, and, where relevant, owners
The financial strength of the audited entity
Whether we are familiar with the sector and have access to suitable skills
Whether the audited entity is one we see contributing to our corporate objectives
The reputation of the audited entity, and its effect on our reputation
The risk to our independence or perceived independence;
Whether engagement with this audited entity might enhance the risk of reputational damage or litigation from the audited entity or third parties

9.16 Forming judgements in this area is challenging, and the processes undertaken will include:

- meeting with senior management of the potential audited entity;
- researching the background to senior management and the organisation;
- consulting colleagues in the NAO on any previous contact the NAO may have had with the entity;
- consulting with and reviewing the work of the predecessor auditors; and
- understanding the regulatory environment in which the entity operates and any potential exposure to regulatory risk arising from the engagement.

9.17 Background research and discussions with predecessor auditors will enable the NAO to consider the risks associated with the audited entity and make an informed decision at an appropriate level within the NAO, on whether the NAO wishes to accept the audited entity. It will also help the NAO prioritise the use of our audit resources. The engagement team should document fully their consideration of audited entity acceptance risk when the NAO accepts a new audited entity.

Engagement acceptance

9.18 There are a number of circumstances in which a new financial statement audit engagement may arise:

- a new body is created and the C&AG is appointed the auditor of that body by statute;

- as a result of changes to legislation, the C&AG is appointed the auditor of an existing body, replacing previous audit arrangements;
- the NAO is appointed at the request of an entity or its sponsoring body; or
- the NAO tenders for and wins a new non-statutory audit appointment on a competitive basis. In practice this option is typically only used for international audits.

9.19 In addition, the NAO is being asked to undertake an increasing number of audit and assurance engagements which are not limited to the audit of financial statements.

9.20 When the NAO takes on a new engagement or submit a tender to perform non-statutory work, the NAO needs to understand whether the engagement exposes it to an acceptable level of risk. Examples of the matters the NAO might consider in accepting new work, or annual consideration of reacceptance of audited entities, are shown in ***Table 9C***.

Table 9C: Key issues for engagement acceptance and re-acceptance

For all engagements the engagement team should consider:
Whether the NAO has the skills and experience to carry out the work.
The availability of key resources at the required time.
The complexity of the engagement.
The regulatory environment of the entity.

For discretionary engagements the engagement team should also consider:
Whether the NAO and the engagement team can comply with ethical requirements.
Whether the scope of the work increases the risk to our reputation.
The level of non-standard elements in the engagement.
The effect of the engagement on our independence or perceived independence.
Whether the engagement contributes to our corporate objectives.
Whether the engagement is a corporate priority.
The NAO's exposure to regulatory risk.

9.21 ***Consultation required*** Engagement acceptance considers whether the NAO should accept a specific piece of work for an audited entity. In relation to statutory engagements, the procedures enable the NAO to identify factors which would prevent the acceptance of an engagement were there not a statutory obligation to perform the work, and to take steps in accordance with Practice Note 10 (Revised 2022). The Engagement Director should consider all new engagement requests and make recommendations to the C&AG through the Director, Audit Quality. Such requests should also be copied to the Executive Director responsible for the Financial Audit Service Line, as well as the Executive Director responsible for the relevant Group. The C&AG will approve the acceptance of an engagement for the first time, following consideration of the risks of accepting that engagement. The engagement acceptance process incorporates considerations relating to audited entity acceptance and should be undertaken for all audit and assurance engagements, including statutory engagements.

9.22 Many of the audits which the C&AG undertakes are audits by statutory appointment and in these circumstances, the NAO cannot withdraw or decline the appointment. However, there are many other avenues open to the NAO: for example, the C&AG can report to Parliament on matters that might otherwise have caused them to withdraw from the engagement.

9.23 The engagement acceptance process enables the NAO to consider whether the risk of the engagement outweighs the benefits to the NAO of accepting the engagement, and the corporate priority the NAO may wish to give this work. The engagement team should fully document their consideration of the risk of a new engagement when accepting that engagement. As engagement

risk changes throughout the lifecycle of an engagement, the engagement acceptance assessment should be revisited at regular intervals. In particular, this should be re-assessed ahead of the final audit visit and prior to certification as part of the continuous risk assessment process.

9.24 In considering engagement acceptance, the engagement team should consider whether the scope of the proposed engagement means that it will be undertaken under appropriate auditing framework. Chapter 10: Determining the form of opinion provides guidance on the different types of engagement that can be undertaken.

9.25 The engagement team should complete a Data Protection Impact Assessment (DPIA) triage before accepting any engagements.

9.26 Engagement acceptance must be completed prior to the commencement of any audit procedures.

9.27 If the preconditions for an audit are not present, the Engagement Director shall discuss the matter with management to determine actions which could be taken to ensure that such preconditions are present.

9.28 If management or those charged with governance impose a limitation on the scope of the NAO's work in the terms of a proposed audit engagement such that the Engagement Director believes the limitation will result in the auditor disclaiming an opinion on the financial statements, and the NAO is required to perform the audit, then the engagement team should consider reporting to Parliament.

9.29 The Engagement Director considers the integrity and competency of the audited entity's board members and senior managers. The matters which are to be considered are outlined in the Engagement Risk Management Audit Form. This consideration is used to inform the audit risk assessment and the resulting audit approach.

9.30 In undertaking engagement acceptance procedures, the Engagement Director should explicitly consider the resource implications of accepting the engagement and whether the NAO has the appropriate skills and expertise necessary to undertake the engagement. This should include a consideration of whether the appointment of an internal or external expert a field other than accounting or auditing would be necessary to obtain sufficient appropriate evidence, with reference to the requirements of ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert*.

9.31 At the outset of the audit, the Engagement Director should consider whether the NAO is able to obtain appropriate staffing for the engagement, either within the NAO or by using audit partners, using the Engagement Risk Assessment Audit Form. In establishing the overall audit strategy, the Engagement Director should determine the particular staffing required for this year's engagement. The Engagement Director should discuss the resourcing and staffing implications of a prospective new engagement with the Director, Audit Operations, as appropriate.

9.32 This aims to ensure that the team (at all levels, and whether in-house or staff from an audit firm) meets the ethical and professional requirements stipulated by both the NAO and the profession. The process involves a consideration of any particular skills and competencies required, for example, with regard to specialist transactions such as derivatives or expenditure on grants and subsidies with complex rules. The composition of the team is assessed to ensure that the team is of sufficient size, experience and expertise to conduct the assignment. This is considered in the context of the audited organisation and their ability to produce a good quality, timely draft of the accounts, and the history of errors identified in the audit, the effectiveness of their systems and controls and

the reporting timetable. The consideration of skills and competencies required for the engagement should be undertaken without reference to level of fees to be charged for the engagement.

9.33 ***Consultation required*** In accordance with paragraph 24 of ISA (UK) 220 (Revised July 2021), if the Engagement Director obtains information that would have caused the C&AG to decline the audit engagement had that information been available earlier and had the option of declining the engagement been available, the Engagement Director must consult promptly with the Director, Audit Quality, and where necessary, the C&AG.

Engagement re-acceptance

9.34 The Engagement Director should go through the same process of consideration of audited entity and engagement risk as part of reaccepting existing audited entities and engagements as they would for accepting a new audited entity or engagement.

9.35 The Engagement Risk Assessment Audit Form is used to document the Engagement Directors' consideration of engagement risk. This should be completed annually for every audit. The assessment will aid awareness of the additional risks that may need to be addressed when planning and carrying out the audit and help ensure that appropriate resources are applied to the audit.

9.36 The assessment of engagement acceptance informs the assessment of whether an Engagement Quality Review or Executive Director involvement is required. The decision to reaccept an audit engagement should be completed at an early stage, before the Engagement Director establishes the overall audit strategy.

9.37 For all engagements the NAO recognises that our assessment of risk may change during the course of an appointment, and the NAO will need to revisit these risks at appropriate and at regular intervals by reviewing the engagement acceptance procedures for the appointment. For any existing engagement, the review will inform the NAO's need to resign from the assignment, if possible, or report to the PAC that the NAO would have resigned if it were possible.

9.38 The Engagement Director reviews the assessment of engagement acceptance at the completion stage of the audit assignment in light of the conduct and findings of the audit. This also allows for early consideration of any future mitigating actions required to tackle any apparent deficiencies (such as those relating to the skills mix of the engagement team) and the need to appoint an Engagement Quality Reviewer for the following year's audit.

Agreeing the terms of an audit engagement

9.39 The requirements in ISA (UK) 210 (Revised June 2016) (Updated May 2022) to agree the terms of the audit engagement with management and, where appropriate, those charged with governance are met by signing either:

- for audits where the C&AG is required by statute (law or regulation) to undertake the engagement (statutory audits), a letter of understanding; or
- for audits where the C&AG is not required by statute (law or regulation) to undertake the engagement (non-statutory audits), a letter of engagement.

9.40 A letter of understanding articulates the terms of the engagement which are prescribed by statute, to ensure all parties understand these.

9.41 Where the C&AG undertakes the audit by statutory appointment, some of the ISA requirements are satisfied by legislation and an engagement letter setting out the detailed terms of the engagement is not required. Instead, the NAO agrees a letter of understanding with the

Accounting Officer, setting out the respective responsibilities of the audited entity and NAO and the basis on which the audit is carried out. This ensures that the management of the audited body have a clear understanding of the scope of the engagement.

9.42 A letter of engagement records the parties' agreement to the terms of the engagement where the C&AG is undertaking the audit by agreement. The issue of an engagement letter establishes a contractual relationship between the entity and the NAO. The terms of the letter must therefore be clear as to the rights, responsibilities and duties of all parties. If engagement teams consider that legal advice might be required in any particular case, they should consult the Legal and Policy team who manage the office's contract for legal advice.

9.43 In either case, the letter will be based on standard templates issued by FAPQ. For non-standard engagements, FAPQ may be consulted on the contents of the letter before an engagement letter is issued.

9.44 The letter of understanding or engagement should specifically cover the following issues in addition to the general requirements of ISA (UK) 210 (Revised June 2016) (Updated May 2022):

- the scope of the assignment and the appropriate auditing standards and/or specified procedures to be applied. Where relevant, this should normally also include a clear statement that the assignment does not represent a full audit of the financial statements of the audited body; and
- details of the nature and contents of the certificate or report to be issued under the assignment. A pro-forma should be appended to the engagement letter; and any necessary caveats or disclaimers as to the use that can be made of reports or certificates issued under the assignment.

9.45 The letter should be sent to the audited entity when the NAO first undertakes an engagement or assignment and must be signed by both parties to the agreement. The Engagement Director will normally sign on behalf of the C&AG. The addressee of the letter should sign and return the letter to the NAO to indicate acceptance of the terms of the engagement. A scan of the signed copy should be included in the Apex audit file.

9.46 The letter should be shared with those charged with governance on an annual basis to allow them to review it and consider whether any changes may be necessary. The engagement team should also consider on an annual basis, as part of the planning process, whether the letter of understanding or letter of engagement (as appropriate) needs to be re-issued. Factors that may indicate that a new letter should be issued include:

- the appointment of a new Accounting Officer;
- any indication that the entity misunderstands the objective and scope of the audit;
- a change in the scope of our audit (e.g. the audited entity is now required to prepare group accounts where previously it did not);
- a significant change in nature or size of the audited entity;
- changes in legislation affecting the audited entity or the C&AG; or
- the introduction of new accounting or auditing guidance.

9.47 If the NAO does not issue a new letter of understanding/engagement letter, the engagement team should document the reasons why this is considered unnecessary in the Apex audit file.

9.48 Accepting inappropriate audited entities or engagements could damage the NAO and C&AG's reputation and standing. Similarly, accepting an engagement and then failing to respond to risks identified in audited entity or engagement acceptance could lead to incorrect audit opinions.

9.49 ***Consultation required*** Engagement Directors should consult FAPQ at an early stage when proposing to agree non-standard terms of engagement (including where management seeks

the inclusion of a non-standard term or clause in a letter of understanding or letter of engagement) or where there are judgements as to whether the preconditions for an audit are met.

9.50 Decisions about audited entity and engagement acceptance and reacceptance cannot be delegated by the Engagement Director. Engagement Directors and Engagement Managers should either perform or be closely involved in the work done to provide evidence to support a decision on whether to accept or reaccept audited entities and engagements.

9.51 ***Consultation required*** The engagement team should consult FAPQ where management seeks to amend the terms of the engagement during the course of the engagement.

Determining the financial reporting framework

9.52 The NAO's audited entities are typically established under a particular legislative framework which, together with relevant accounting provisions, prescribes the form and content of the financial statements – this framework may include:

- the specific legislation that has established the audited entity and determines its activities;
- Accounts Directions;
- the Government Financial Reporting Manual and Managing Public Money;
- standards that constitute IFRS and/or UK GAAP;
- other HM Treasury guidance on the application of accounting standards, the Companies Acts and the disclosure of information;
- the Charities SORP; and
- the Pensions SORP.

9.53 Given its propensity to change each year, teams should consider whether there have been changes in the applicable legislative and regulatory framework. The entity's framework of authorities and (relevant) legislative framework should be clearly documented prior to the performance of any risk assessment procedures or audit work.

9.54 Paragraphs A8 to A9 of ISA (UK) 210 (Revised June 2016) (Updated May 2022) set out circumstances where the financial reporting framework can be presumed to be appropriate. These include entities using International Financial Reporting Standards (IFRSs) promulgated by the International Accounting Standards Board or International Public Sector Accounting Standards (IPSASs) promulgated by the International Public Sector Accounting Standards Board. For UK public sector bodies, the FReM can be presumed to be appropriate. can be presumed to be appropriate.

9.55 However, if the accounts direction includes specific requirements that supersede the FReM, the engagement team is required to consider whether together they represent an acceptable accounting framework. If the engagement team does not consider that the accounting framework adopted would give a true and fair view, they will need to discuss this with the audited entity and, if necessary, HM Treasury at the earliest possible opportunity.

9.56 The financial reporting framework for a particular engagement may be a special purpose framework, rather than requiring a full set of financial statements. These types of engagement are discussed in Chapter 10: Determining the form of opinion.

Declining to re-accept an engagement or otherwise ceasing to hold office as auditor

9.57 ***Consultation required*** In circumstances where the engagement team proposes not to re-accept an engagement or the NAO otherwise ceases to hold office as statutory auditor of an audited entity, they should consult FAPQ, who will ensure the NAO complies with its requirements under paragraph 34-1(e) of ISQM (UK) 1 *Quality management for firms that perform audits or reviews of*

financial statements, or other assurance or related services engagements to provide the successor statutory auditor with access to all relevant information concerning the entity, including information concerning the most recent audit.

9.58 The procedures for sharing information with successor auditors that are set out in Chapter 42: Companies should be applied to all NAO audit engagements, including non-company audits.

Chapter 10: Determining the form of opinion

Relevant standards and guidance

10.1 ISA (UK) 210 (Revised June 2016) (Updated May 2022) *Agreeing the terms of audit engagements* deals with the auditor's responsibilities in agreeing the terms of the audit engagement with management and, where appropriate, those charged with governance.

10.2 ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* deals with the auditor's responsibility to form an opinion on the financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

10.3 Paragraphs 1-203 to 1-216 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) in the public sector.

10.4 ISA (UK) 701 (Revised November 2019) (Updated May 2022) *Communicating key audit matters in the independent auditor's report* deals with the auditor's responsibility to communicate key audit matters in the auditor's report. It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication. It also deals with the auditor's responsibility to communicate other audit planning and scoping matters in the auditor's report. These requirements are commonly referred to as extended auditor reporting and apply only to certain types of entity.

10.5 Paragraphs 1-217 to 1-218 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 701 (Revised November 2019) (Updated May 2022) in the public sector.

10.6 Paragraphs 2-83 to 2-91 of Practice Note 10 (Revised 2022) deal with the form of a regularity opinion and other reporting on regularity.

Background

10.7 This Chapter covers considerations involved in determining the form of opinion, including any regularity opinion, at the outset of the engagement. Matters relevant to reporting the actual findings of the audit, such as modified opinions, are covered in Section 13: Concluding and reporting.

Proforma certificates and reports

10.8 ***Consultation required*** FAPQ provides proforma audit certificates and reports for different types of engagement, which are updated each year. Engagement teams should use the relevant proforma template. If none of the proforma templates are relevant to the circumstances of a particular entity, or significant changes or customisations to the templates are required, or law or regulation prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of ISAs (UK) (as envisaged by paragraph 21 of ISA (UK) 210 (Revised June 2016) (Updated May 2022)), the engagement team should consult FAPQ.

Extended auditor reporting

10.9 The NAO's policy is that audits of the following entities must prepare extended auditor reports:

- Listed Companies
- Public Interest Entities
- Entities that are required, and those that chose voluntarily, to report on how they have applied the UK Corporate Governance Code
- Ministerial Government Departments
- Other entities as determined by the C&AG

10.10 ***Consultation required*** All extended auditor reports must be submitted to FAPQ for review, but only require a DAQ minute where the report is modified. Unmodified extended auditor reports do not require a DAQ minute but must still be submitted to FAPQ for review.

10.11 Pro-forma Extended Auditor Reports have been provided for engagement teams to draft their Extended Auditor Reports. These pro-formas are available for both Departments and Companies.

10.12 It is important that the form and content of Extended Auditor Reports are presented in a uniform fashion, as this promotes the reader's understanding of the report, and highlights unusual circumstances when they occur. The Extended Auditor Report will therefore include the following elements:

- Title
- Addressee
- Introductory paragraph identifying the statements to be audited
- Opinion on the financial statements
- Opinion in respect of an additional financial reporting framework
- Opinion on regularity (where applicable)
- Basis for opinions
- Conclusions related to Going Concern
- Overview of audit approach including:
    - Key Audit Matters
- Application of materiality
    - Materiality
    - Performance materiality
    - Other materiality considerations
    - Error reporting threshold
- Audit scope
- Other Information
- Opinion on Other Matters
- Matters on which I report by exception
- Responsibilities of the Accounting Officer
- Auditor's Responsibilities for the Audit of the Financial Statements
    - Extent to which the audit was considered capable of detecting irregularities, including fraud.
    - Procedures to detect fraud
    - Procedures in response to identified risks
- Corporate governance statement [where audited entities report on how they have applied the UK Corporate Governance Code] (as required by paragraph 22-3 of ISA (UK) 720 (Revised November 2019) (Updated May 2022))
- Report (when applicable)
- Auditor's signature
- Auditor's address and
- Date of the report

10.13 Chapter 54: Overall conclusions and preparing the certificate or report provides further details on the content of NAO Extended Auditor Reports, as determined by the findings of the audit and the key audit matters identified.

Determining when a regularity opinion is required

10.14 For new engagements, the consideration of whether a regularity opinion is required should be made as part of the engagement acceptance process.

10.15 There are a variety of factors which determine whether a regularity opinion should be provided on the financial statements. These include: the requirement to include a regularity opinion by statute, the requirement to include a regularity opinion by convention and a request to provide a regularity opinion either by the entity itself or by its sponsoring body.

10.16 For a number of bodies audited by the NAO, the requirement to provide a regularity opinion is established in statute. For example, the C&AG is required to provide a regularity opinion on the financial statements of Government Departments and their Executive Agencies by virtue of the Government Resources and Accounts Act 2000.

10.17 Engagement teams should review the legislation under which the C&AG has been appointed as auditor to determine whether this requires a regularity opinion to be provided. Where the legislation is not clear on the requirement for a regularity opinion, the Legal and Policy team may be consulted for further advice.

10.18 The concept of regularity reflects Parliament's concern that public money is used only for those purposes approved by Parliament. The preparation of financial statements by bodies carrying out a public function is an important means by which they are accountable for the use of public funds made available to them by Parliament.

10.19 Where an entity is exercising a function for which they are not directly accountable to Parliament for the use of funds made available to them, a regularity opinion may not be required. This is particularly relevant to entities audited under the Companies Act. Chapter 42: Companies provides further guidance on establishing whether a regularity opinion may be provided in these circumstances.

10.20 ***Consultation required*** For some entities, a regularity opinion may be requested either by the entity through management or those charged with governance, or by the entity's sponsoring Department in support of their own regularity opinion. In such circumstances, the Engagement Director should assess such requests, based principally on the extent to which the audited entity is funded by government grant or performs a public function. The Engagement Director's consideration should include a consideration of whether there is an appropriate framework of authorities in place against which to audit. A recommendation must then be made to FAPQ, and the final judgement recorded on the audit file.

10.21 ***Consultation required*** Where a regularity opinion is recommended or required on an existing engagement where such an opinion has not previously been provided, the Engagement Director must submit a briefing to FAPQ setting out why a regularity opinion is required. Such a recommendation will then be approved by the Director, Audit Quality prior to submission to the C&AG for approval.

10.22 ***Consultation required*** In circumstances where the Engagement Director determines that a regularity opinion is no longer required for an existing engagement, the Engagement Director must

submit a briefing to FAPQ setting out the circumstances. Any such recommendation must be approved by the Director, FAPQ with the final judgement recorded on the audit file.

Types of assurance engagement

10.23 Although not all adopted in the UK by the Financial Reporting Council, the International Auditing and Assurance Standards Board (IAASB) have issued the International Framework for Assurance Engagements as well as International Standards on Review Engagements (ISREs) and International Standards on Assurance Engagements (ISAEs), which should be referred to as best practice (rather than mandatory guidance) for other assurance engagements.

10.24 ***Figure 10A*** shows the different standards that can be applied to different assurance engagements, based on the scope of the engagement:

Figure 10A: Relevant standards for an assurance engagement

Standards	International Framework for Assurance Engagements							
	ISRE 2400 (Revised) *Engagements to review historical financial statements*	International Standards on Auditing (ISAs) and International Standards on Auditing (UK) (ISAs (UK))	ISA (UK) 800 (Revised)/ ISA (UK) 805 (Revised)	ISAE 3000 (Revised) *Assurance engagements other than audits or reviews of historical financial information*				ISRS 4400 (Revised) *Agreed-upon procedures engagements*
Guidance				ISAE 3400 *The examination of prospective financial information*	ISAE 3402 *Assurance reports on controls at a service organisation*	ISAE 3410 *Assurance engagements on greenhouse gas statements*	ICAEW AAF Technical Release 01/10	
Scope	Financial statements		Financial statements under special purpose frameworks	Prospective financial information (such as budgets)	Other: includes controls review	Statements quantifying greenhouse gas emissions	Grant certification	Other: includes controls review
		Recognised reporting framework / Other						
Opinion	Limited assurance	True and fair / Properly presents		Limited assurance	Reasonable assurance	Reasonable or limited assurance	Report of factual findings	

Frameworks other than full financial statements audits

10.25 Some engagements may be carried out under special purpose frameworks, which are covered by ISA (UK) 800 (Revised) *Special considerations – audits of financial statements prepared in accordance with special purpose frameworks* and ISA (UK) 805 (Revised) *Special considerations – audits of single financial statements and specific elements, accounts or items of a financial statement.*

10.26 Other engagements may be carried out on the basis of agreed-upon procedures, which are governed by International Standard on Related Services 4400 (Revised) (ISRS 4400) *Agreed-upon procedures engagements.*

10.27 In some cases, the NAO may be asked to undertake a specific engagement in order to support the assurance needs of a user of public sector financial information or other subject matter, such as another UK public audit body or audit firm, or entities having dealings with government-related entities (referred to collectively hereafter as 'subject matter users'). ***Table 10B*** summarises the possible frameworks that may be appropriate to support this type of work.

Table 10B: Available frameworks for undertaking work to support other UK public audit bodies or audit firms

Framework	Comments
Agreed-upon procedures International Standard on Related Services 4400 (ISRS 4400) *Agreed-upon procedures engagements*	The most common framework used for these engagements is an agreed-upon procedures engagement under ISRS 4400. This framework sets out an agreed set of procedures which the NAO engagement team will report upon on a factual basis without providing an opinion on any underlying subject matter. This framework carries the lowest risk for the NAO, as it is a factual based engagement where no conclusion is provided. It is then for the relevant subject matter user to draw a conclusion based upon the work undertaken. However, an agreed-upon procedures engagement can rapidly become complex where there is subjectivity in the interpretation of the result of the procedures. ***Consultation required*** All reports issued under an ISRS 4400 engagement should be submitted for FAPQ for review.
Special purpose frameworks and single/specific elements, accounts or items of a financial statement ISA (UK) 800 *Special considerations – audits of financial statements prepared in accordance with special purpose frameworks* and ISA (UK) 805 *Special considerations – audits of single financial statements and specific elements, accounts or items of a financial statement*	This framework is reliant upon the audited entity preparing subject matter to meet the needs of the assurance required by the relevant subject matter user. This framework requires significant engagement with both the audited entity and the relevant public audit agency to ensure that the subject matter of the engagement sufficiently meets their needs. The performance of an engagement under ISA (UK) 800/ISA (UK) 805 requires the auditor to undertake an ISA-compliant audit (to the extent possible) on the subject matter. This is likely to be the most resource intensive option.
Group audit ISA (UK) 600 (Revised September 2022) *Special considerations – audits of group financial statements (including the work of component auditors)*	Under this option, the relevant subject matter user will identify a component under ISA (UK) 600 (Revised September 2022) and issue group audit instructions setting out the procedures for the NAO team to perform as they would for a component auditor. Within this option, the relevant subject matter user would take responsibility for identifying components and setting the scope of the work. However, there is risk here that they might either set a scope which is not appropriate or that the NAO is asked to provide an opinion on subject matter which they may choose to disagree with at a later stage.
Other assurance engagements	This framework covers assurance engagements other than audits or reviews of historical financial information.

International Standard on Assurance Engagements 3000 (ISAE 3000) *Assurance engagements other than audits or reviews of historical financial information*	The objective is to obtain either reasonable assurance or limited assurance about whether the subject matter information is free from material misstatement and to express a conclusion regarding the outcome of the measurement or evaluation of the underlying subject matter through a written report that conveys either a reasonable assurance or a limited assurance conclusion and describes the basis for the conclusion. ***Consultation required*** All reports issued under an ISAE 3000 engagement should be submitted for FAPQ for review.
Prospective financial information International Standard on Assurance Engagements (UK) 3400 (ISAE 3400) *The examination of prospective financial information*	This framework covers engagements to examine and report on prospective financial information (financial information based on assumptions about events that may occur in the future and possible actions by an entity), including examination procedures for best-estimate and hypothetical assumptions. It does not cover prospective financial information that is expressed in general or narrative terms, such as management commentary in the Annual Report. The objective is to obtain sufficient appropriate evidence as to whether the prospective financial information is based on reasonable assumptions; properly prepared on the basis of the assumptions; properly presented and all material assumptions adequately disclosed; and prepared on a consistent basis with historical financial statements, using appropriate accounting principles.
Service auditor International Standard on Assurance Engagements 3402 (ISAE 3402) *Assurance reports on controls at a service organisation*	Where a UK government entity audited by the NAO is providing processing or other functions on behalf of another entity, the entity providing those functions would be a service organisation under ISA (UK) 402 (Updated May 2022) from the perspective of the other entity. In these circumstances, the relevant subject matter user may elect to engage the NAO to provide assurance over the operation of controls at the service organisation as the service auditor under ISA (UK) 402 (Updated May 2022). The options under ISAE 3402 would require the NAO to provide assurance over either the design and implementation (Type 1) or the operating effectiveness (Type 2) of controls operated by the UK government entity in these circumstances. This would also require the UK government entity to provide a clear description of the relevant controls. Whilst there are some obvious advantages to adopting such a framework, the NAO would need to be clear with the relevant UK public audit body that the scope of work under this framework is clearly limited to controls assurance and that should they require further substantive assurance, then there would need to be a separate engagement covering this under one of the other frameworks set out here.

10.28 ***Consultation required*** In cases where the NAO is asked to carry out a specific engagement designed to fulfil a particular purpose, other than the audit of a full set of entity financial statements, FAPQ should be consulted on the appropriate form of engagement.

Chapter 11: Determining the framework of authorities

Relevant standards and guidance

11.1 Paragraphs 2-5 and 2-16 to 2-24 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on determining the framework of authorities that are relevant to the regularity opinion.

The framework of authorities and the regularity opinion

11.2 As set out in paragraphs 2-4 to 2-5 of Practice Note 10 (Revised 2022), regularity is the concept that transactions that are reflected in the financial statements of an audited entity must be in accordance with the relevant framework of authorities. Frameworks of authorities are external frameworks, specific to the audited entity, with which the audited entity's transactions must conform. These frameworks are set by bodies able to issue and/or enforce the authorities for that entity. They might include, for example:

- authorising legislation;
- regulations issued under governing legislation;
- parliamentary authorities (including budgetary laws, for example budget estimates voted by the relevant Parliament/Assembly); and
- government or related authorities (for example Managing Public Money issued by HM Treasury).

11.3 Determining the framework of authorities for the entity is key to forming the regularity opinion, where one is given, and to establishing the scope of audit work required to provide the regularity opinion. The engagement acceptance process for each audit engagement where a regularity opinion is given should include explicit consideration and documentation of the framework of authorities for the entity. This should be revisited as part of the planning process in each subsequent period to ensure the documented framework of authorities is up-to-date and complete. The engagement team should undertake this exercise as part of establishing the overall audit strategy as set out in Chapter 15: Gathering entity initial information.

11.4 Paragraph 2-23 to 2-24 of Practice Note 10 (Revised 2022) set out considerations relating to the determination of which authorities are within the scope of the auditor's regularity opinion and therefore form part of the framework of authorities.

11.5 The framework of authorities is specific to the entity and will vary depending on the nature of the entity, its functions, accountability structures and legislative framework. ***Table 11A*** gives examples of frameworks of authorities common to a number of NAO audited entities.

Table 11A: Common frameworks of authorities for NAO audited entities

Entity	Authoring Legislation	Regulations under Governing Legislation	Parliamentary Authorities	Government Authorities
Departments	Government Resources and Accounts Act 2000 Legislation relevant to the Department	Specific Legislation/ Regulations relating to the operation of the Department and its functions	Supply Estimates	Managing Public Money Directions Issued by HM Treasury Cabinet Office Controls (unless exempt)

Executive Agencies	Government Resources and Accounts Act 2000 Legislation relevant to the Agency	Specific Legislation/ Regulations relating to the operation of the Agency and its functions	Obtained through Department's Supply Estimates Financial Memorandum/ Management Agreement set by parent Department	Managing Public Money Directions Issued by HM Treasury Cabinet Office Controls (unless exempt) Financial Memorandum/ Management Agreement set by parent Department
NDPBs	Specific legislation setting up the NDPB	Specific legislation/ Regulations relating to the operation of the NDPB and its functions	Obtained through Department's Supply Estimates Financial Memorandum/ Management Agreement set by parent Department	Financial Memorandum/ Management Agreement set by parent Department
Other entities	Specific to the entity			

11.6 The extent of the engagement team's work in obtaining an understanding of the framework of authorities will depend upon the complexity of laws and regulations and regulatory environment applicable to the entity. For example, some entities may operate in complex legislative and regulatory environments, where their activities are governed by an array of requirements, whereas some entities may be subject to limited restrictions.

11.7 As per paragraph 2-21 of Practice Note 10 (Revised 2022), laws and regulations that fall within the general framework include, for example, health and safety, employment and environmental protection regulations. Non-compliance with such frameworks would not affect the C&AG's opinion on the regularity of transactions but may be relevant to the engagement team's assessment of compliance with laws and regulations under ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements* and ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector*. Further guidance on these responsibilities may be found in Chapter 31: Consideration of laws and regulations and reporting to regulators.

11.8 In accordance with paragraph 2-29 of Practice Note 10 (Revised 2022), in establishing the framework of authorities, the engagement team's consideration should involve reviewing legislation and identifying the relevant provisions which authorise activities and reviewing the process for their transaction and interpretation in subsidiary regulations and guidance. In conducting this review, the engagement team should pay particular attention to statutory regulations which govern:

- the powers of relevant bodies to determine the relevant rules and procedures;
- the controls to be operated by the entity responsible for the administration of a scheme;
- the eligibility of beneficiaries to receive grants or other kinds of financial support under a scheme;
- the calculation of grants and any other payments; and
- the setting of fees and charges and other revenues.

11.9 The engagement team should in particular consider the extent to which these regulations and guidelines form part of the entity's framework of authorities.

11.10 The Engagement Director must ensure that the entity's framework authorities is clearly documented within the audit file. The Engagement Director must also ensure that all engagement team members fully understand the entity's framework of authorities and are aware of their responsibilities for identify breaches in their framework in support of the C&AG's opinion on regularity.

Specific elements of the framework of authorities for certain types of entity

11.11 Authorising legislation is the primary source of authority which governs the way in which an activity is performed. Authorising legislation includes Acts of Parliament, legislation establishing trading funds, the governing statutes for arm's length Bodies and European legislation (where the European legislation is retained by the UK). When expenditure is incurred or income raised under legislative authority the resulting payments and receipts must comply with all the relevant provisions of the legislation. If the payment or receipt is not in accordance with the legislation, the payment or receipt will be irregular. The legislation will vary from being very closely defined, to providing significant discretion to the Minister in administering the service. In some cases, the legislation will not be comprehensive and will be supported by regulations issued under governing legislation.

11.12 Many Acts of Parliament provide for their implementation by means of delegated legislation. Delegated legislation may take a number of forms including Statutory Instruments, rules, regulations and orders. Delegated legislation must be within the scope of the authorising legislation. It is frequently used to set the detailed regulations applying to services provided by government e.g. fees for statutory services and social security benefits. If a payment or receipt is made which is not in accordance with the delegated legislation, the payment or receipt will be irregular.

11.13 The breach of a framework agreement, financial memorandum or grant funding agreement between an entity and its sponsoring/funding body (for example, an Executive Agency and its sponsoring body) usually constitutes irregular activity, as the sponsoring body (usually a department or Secretary of State) has a statutory role in supervising the activities of the entity. A breach of requirements set down in governing/funding documents which do not derive from those set down in legislation, regulations or the framework of authorities does not constitute irregular activity, since it is not underpinned by any of the four elements of the framework of authorities relevant to regularity.

11.14 Acts of Parliament may permit the Minister to set the detailed rules of the service or scheme. In such instances any payments or receipts which are not made in accordance with the rules set by the Minister are considered to be irregular.

11.15 Parliamentary authority for income and expenditure is provided through the Supply process. However, there are three basic principles which must be adhered to by all departments:

- a sum provided for a particular service may not be used to provide another service;
- the expenditure of the department must not exceed the amount approved by Parliament in the Supply and Appropriation Acts; and
- the amounts provided are available for that financial year only and any unused funds must be surrendered to the Consolidated Fund at the end of the year.

11.16 If a department fails to adhere to these basic principles the resulting expenditure will normally be considered irregular.

11.17 The services which can be financed by a department are approved by Parliament via the Supply process. The 'ambit' of the vote describes the services on which a department may legally

spend its resources. Any expenditure undertaken by the department which is not covered by the ambit will be considered irregular.

11.18 In principle, HM reasury approval is required for all expenditure. HM Treasury often delegates to departments authority to enter into commitments and to incur expenditure. HM Treasury's delegated authority sets out the level of delegation, the programmes and objects of expenditure covered and the period over which it is extant. Treasury approval is always required for any spending proposals which are novel or contentious. More detailed guidance on novel and contentious payments is provided in Managing Public Money. Any expenditure which is incurred outside of HM Treasury's delegated authority and does not have specific Treasury approval is considered irregular.

11.19 HM Treasury has also issued a number of guidelines and guidance documents which departments are expected to comply with in incurring expenditure. For example, guidance on off-payroll arrangements and senior civil service pay. Where a body is required to prepare its financial statements in accordance with Directions issued by Treasury, then such guidance will form part of its framework of authorities.

11.20 HM Treasury has delegated to the Cabinet Office certain approval processes relating to expenditure areas that the Government wishes to control more tightly than departmental delegated authorities. Examples include provisions relating to civil service pay and spending controls. The controls and processes delegated to the Cabinet Office form part of the entity's framework of authorities, where the entity is required to comply with Managing Public Money as this delegation has been formalised through Managing Public Money.

11.21 A number of bodies which are required to comply with Managing Public Money have been given exemptions from compliance with the requirements of the controls set by Cabinet Office as set out in Annex 1.3 to their controls document.

11.22 Where Cabinet Office or other government departments have issued general best practice guidance for entities operating in the public sector (for example, Procurement Practice Notes), these would only form part of the framework of authorities to the entity where explicitly referenced in Managing Public Money or another document which forms part of the entity's framework of authorities (for example a framework agreement with a Sponsor Department).

11.23 Financial sanctions issued by HM Treasury resulting from breaches in spending controls are not considered irregular. HM Treasury consider these sanctions to be a budgetary disincentive and that these are not intended to represent a financial loss. This is on the basis that there is no overall loss to the Exchequer from the transactions. In most cases, the 'sanctions' take the form of a reduction in future budgets and therefore there is no irregular expenditure reflected in the accounts. However, in some cases, these are physical cash payments to the Consolidated Fund. In the latter case, since the initial funding is from the Consolidated Fund then again, there is no loss to the Exchequer.

11.24 It is the fact there is no loss to the Exchequer that distinguishes HM Treasury-issued sanctions from other fines imposed. Fines by external bodies where there is a loss to the Exchequer would be considered irregular. Fines by other government bodies would potentially be deemed irregular (such as to the Health and Safety Executive) since this involves a cash outflow to a body other than the Consolidated Fund.

11.25 The HM Treasury sanctions are also distinct from the underlying expenditure that gave rise to the sanction and may be deemed irregular. For instance, a salary payment without approval will likely be deemed irregular and result in a qualification of the regularity opinion.

11.26 HM Treasury sanctions themselves do not give rise to a qualification. The audited entity should be encouraged to set out the circumstances relating to the imposition of the sanction it the Governance Statement, and to disclose the nature and value in the financial statements (usually as a narrative to the losses and special payments note).

11.27 As discussed in Chapter 31: Consideration of laws and regulations and reporting to regulators, when designing and performing audit procedures and in evaluating and reporting the results thereof, the engagement team should recognise that non-compliance by the entity with laws and regulations may materially affect the financial statements. It should be noted that this is a separate concept from regularity and material non-compliance with laws and regulations may not necessarily affect the regularity opinion on the accounts. For example, a breach of a health and safety legislation may not result in income or expenditure being incurred which falls outside the scope of Parliament's intention.

11.28 Where a breach of laws and regulations is identified, whether or not that breach is also a breach of the framework of authorities, the engagement team should consider their obligations under ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements* and ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector*, in respect of reporting matters to the relevant authorities in the public interest and to regulators, where applicable.

11.29 Further guidance on the power to incur expenditure is contained in Managing Public Money. Further guidance in respect of regularity for audits of companies can be found in Chapter 42: Companies.

11.30 Any expenditure by a department which is in excess of its control totals as approved by Parliament will be considered irregular and must result in a qualification. Further guidance on the audit of the Statement of Parliamentary Supply can be found in Chapter 41: Parliamentary Supply.

Structure and funding of central government entities

11.31 In order to understand the concept of regularity it is necessary understand the structure and funding of central government entities and the different frameworks of authority which may apply.

11.32 Bodies within the central government sector are subject to both the authority of the Crown and the legislative and financial authority of Parliament. As a result, the relationship between the Crown and Parliament is a complex mix of:

- the powers available to Ministers (as agents of the Crown) under common law;
- the duties and obligations placed on Ministers by legislation; and
- Parliamentary procedures in the granting of monies to meet expenditure to be incurred by Ministers (the Supply Process).

11.33 Using the Crown Prerogative, Government Ministers may exercise any powers which the Crown has the authority to exercise. Under common law, the Crown is permitted to undertake any activity unless it is prevented from doing so by Statute. Explicit statutory authority is not generally necessary to enable Ministers to exercise functions. In principle therefore, Ministers can do anything which they are not prevented from doing by Statute. However, in most areas of government, the actions of Ministers and their departments are regulated by Parliament through legislation. The statutory regulation of Ministers' activities includes the regulation of their powers to incur expenditure or raise revenue in connection with those activities. Where legislation exists, Ministers and departments are bound by its terms. This serves to reduce the scope of ministerial discretion. There

have been instances where a judicial review has been required to determine the limits of Ministerial authority.

11.34 A statute which confers power on a Minister does not in itself provide authority for expenditure to be incurred. Authority for the expenditure is provided through the Supply Process. Thus, while Ministers and departments may undertake any activity unless prevented from doing so by statute, they may only incur expenditure on the activity if Parliament has agreed to provide funding for the activity. The Appropriation Act provides Parliamentary authority for expenditure. Further details on the Supply Process are provided in Chapter 41: Parliamentary Supply.

11.35 The Minister in charge of each government department and its sponsored bodies is answerable to Parliament for the activities of that department. Departments derive their authority from the Minister and may, in principle, perform any activity requested by the Minister.

11.36 The Accounting Officer (or their equivalent) is responsible for ensuring that the entity maintains proper accounting records and for preparing financial statements in accordance with the accounts direction. The accounting officer must also ensure that the entity maintains a sound system of internal control and that the public funds for which he/she is responsible are properly managed and efficiently and effectively used. Further guidance on the role of the Accounting Officer is provided in Managing Public Money.

11.37 If the Minister wishes the Accounting Officer to incur expenditure on transactions which the Accounting Officer considers to be irregular, or to provide poor value for money, the Accounting Officer should raise their objections in writing to the Minister and copy this to the C&AG. If, despite the Accounting Officer's advice, the Minister decides to continue with a course the Accounting Officer has advised against, the Accounting Officer should ask for a formal direction to proceed. A Ministerial Direction issued in this way does not itself regularise the related spend. The fact that a Ministerial Direction has needed to be issued based on an Accounting Officer's concerns is likely to be an indicator of increased risk that the related transactions may be irregular.

Section 6: Engagement teams

Chapter 12: Roles, delegations and licences

Relevant standards and guidance

12.1 Paragraphs 25 and A59-A78 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* include requirements relating to the assignment of engagement teams.

Segmentation of audit engagements

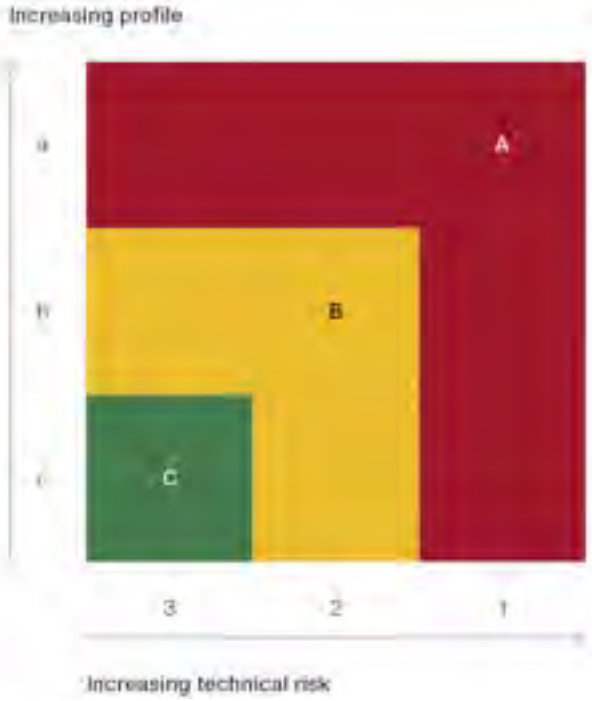
12.2 To support the Engagement Director's assessment of the appointed team's capability and competence to carry out the audit, Portfolio Directors will need to classify each of the audits in their portfolio depending on the complexity and risk associated with each assignment. In categorising audits, the approach set out in ***Table 12A*** below is taken to considering both the profile and technical risk within individual audits.

Table 12A: Definitions of profile and technical risk ratings

Profile Rating	Definition	Technical Rating	Definition
a	The organisation has a high public and/or Parliamentary profile. There is regular evidence of significant interest in their financial management and reporting.	1	The financial statements include significant areas which require specialist technical expertise and / or are likely to give rise to significant accounting and audit judgments (such as, but not limited to, the likely need for a modified opinion)
b	The organisation has a high profile within the sector in which it operates. There is occasional wider public or Parliamentary interest in their financial management and reporting.	2	The financial statements contain technical or judgmental areas, but of a common / routine nature.
c	The organisation has a low profile outside its immediate group or sponsoring department. Public or Parliamentary interest in the organisation's financial management and reporting is rare.	3	The financial statements are simple, with limited room for judgment and no requirement for specialist technical expertise.

12.3 This assessment of profile and technical risk is then mapped onto an ABC categorisation as set out in ***Figure 12B*** below.

Figure 12B: Mapping of profile and technical risk ratings to ABC segmentation of audits



12.4 This will provide an overall categorisation of audits as follows:

- Type A audits are audits with either a high profile or technical risk. There is evidence of significant Public and/or Parliamentary interest in their financial management and reporting, or significant areas of their financial statements which require specialist technical expertise to audit and / or are likely to give rise to significant accounting and audit judgments.
- Type B audits are those which are considered to be of medium profile or technical risk. There may be occasional Public or Parliamentary interest in their financial management and reporting. The financial statements may contain technical or judgmental areas, but of a common or routine nature.
- Type C audits are those with both a low public profile and technical risk. Public or Parliamentary interest in their financial management and reporting is rare. The financial statements are simple, with limited room for judgment and no requirement for specialist technical expertise.

12.5 The segmentation of each portfolio of audits is designed to guide engagement teams in the expected roles and responsibilities for individuals involved in audits dependent on the relative risk. Category A audits have more restrictions on role assignments.

12.6 The following restrictions apply to role assignments:

- *Engagement Director*
  - ***Consultation required*** Engagement Director roles for Category A audits may only be assigned to Senior Audit Managers with approval from the Director, Audit Quality (DAQ).
  - ***Consultation required*** Engagement Director roles for Category B and C audits assigned to Senior Audit Managers only require DAQ approval for individuals who have been in the Senior Audit Manager Grade for less than one year. Senior Audit Managers will not normally be assigned to Engagement Director roles until they have been in the grade for at least one year.
  - Engagement Director roles will not be assigned to staff at Audit Manager grade or below.
- *Engagement Manager*
  - ***Consultation required*** Engagement Manager roles for Category A audits assigned to Audit Managers require DAQ approval.
  - Engagement Manager roles for Category B and C audits assigned to Audit Managers do not require DAQ approval.

- Engagement Manager roles for Category A audits will not be assigned to Senior Auditors.
- ***Consultation required*** Engagement Manager roles for Category B and C audits assigned to Senior Auditors require DAQ approval.

- *Engagement Team-Leader*
  - Engagement Team-Leader roles for Category A audits assigned to Senior Auditors do not require DAQ approval. Senior Auditors will not normally be assigned to Engagement Team-Leader roles on Category A audits until they have been in grade for at least one year.
  - ***Consultation required*** Assignments of Engagement Team-Leader roles to individuals without a General Audit Licence require DAQ approval.

Table 12C: Category A audit role assignment restrictions and requirement for DAQ approvals

	Category A audits				
	Individual without a General Audit Licence	Senior Auditor	Audit Manager	Senior Audit Manager	Director
Engagement Director		Prohibited	Prohibited	Requires DAQ approval[5]	Expected
Engagement Manager		Prohibited	Requires DAQ approval	Expected	
Engagement Team-Leader	Requires DAQ approval	Expected	Expected		

Table 12D: Category B and C audit role assignment restrictions and requirement for DAQ approvals

	Category B and C audits				
	Individual without a General Audit Licence	Senior Auditor	Audit Manager	Senior Audit Manager	Director
Engagement Director		Prohibited	Prohibited	Expected (> 1 year in role) Requires DAQ approval (<1 year in role)	Expected
Engagement Manager		Requires DAQ approval	Expected	Expected	
Engagement Team-Leader	Requires DAQ approval	Expected	Expected		

12.7 Portfolio Directors retain overall responsibility for the audits within their portfolio, including ensuring that role assignments are made on an appropriate basis. In exercising this responsibility, they may decide to assign part of the role of Engagement Director to a Senior Audit Manager, following the permitted models in ***Table 12E*** below:

Table 12E: Options for models of assignment of Engagement Director roles to Senior Audit Managers

Role assignment model	Portfolio Director engagement

[5] We expect instances of the assignment of the Engagement Director role to a Senior Audit Manager on a Category A audit to be rare. In deciding whether or not to approve these cases, the Director, Audit Quality will take account of the requirements for specialist skills in the role (such as Responsible Individual status or pensions or charities experience).

All models	Responsible for assessing the risk and sensitivity of each audit engagement within the portfolio, and for ensuring that a suitable Director or Senior Audit Manager is assigned Engagement Director responsibility for that audit. Where Engagement Director responsibility has been delegated, responsible for revisiting this assessment throughout the audit.
Full assignment to Senior Audit Manager	The Portfolio Director should: • Attend the overall audit strategy meeting • Scan-read the financial statements with key sector knowledge in mind – looking at primary statements and key notes. • Read the Audit Completion Report. • Provide a short minute to be included on the Certification Journal confirming they have performed the above role and are content that the assignment of the Engagement Director role to a Senior Audit Manager remains appropriate.
Assignment of client engagement to Senior Audit Manager	Where the client is low profile, but with complex or high-risk audit issues. The Portfolio Director may decide to assign the client engagement to a Senior Audit Manager but retain responsibility for file review. The Portfolio director would retain all ISA (UK) 220 (Revised July 2021)/ISQM (UK) responsibilities, but attendance at audit committees et cetera would be handled by the Engagement Manager.
Assignment of file review to Senior Audit Manager	Where the audited entity's accounts are simple, but the relationship is significant/ high profile. The Portfolio Director would then retain all client liaison responsibilities, but in all other aspects, including the role of Engagement Partner under the ISAs (UK), would be assigned to a Senior Audit Manager in line with the "full" model.

12.8 The Director, Audit Quality is responsible for deciding whether to approve or decline to approve any role assignments arising which fall outside of the 'Expected' assignments shown in ***Table 12C*** and ***Table 12D*** above. In making these decisions, the Director, Audit Quality will take into account information submitted by those within the Financial Audit Service Line responsible for making resourcing decisions on audit engagements, including relevant Portfolio Directors; this information may include proposals to apply one of the role assignment models shown in ***Table 12E*** above. Individuals whose role assignment involves designation as a Key Audit Partner are included in a list of Key Audit Partners published by FAPQ on the Financial Audit Practice and Quality Sharepoint page.

12.9 In accordance with paragraph 26 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*, the Engagement Director should be satisfied that the engagement team, and any external experts (along with, for audits applying non-UK adapted ISAs, internal auditors who provide direct assistance) who are not part of the engagement team, collectively have the appropriate competence and capabilities to:

- perform the audit engagement in accordance with professional standards and applicable legal and regulatory requirements; and
- enable an auditor's report that is appropriate in the circumstances to be issued.

12.10 In accordance with paragraph A71 of ISA (UK) 220 (Revised July 2021), when considering the appropriate competence and capabilities expected of the engagement team as a whole, the Engagement Director may take into consideration such matters as the team's: considering the

appropriate competence and capabilities expected of the engagement team as a whole, the Engagement Director may take into consideration such matters as the team's:

- understanding of, and practical experience with, audit engagements of a similar nature and complexity through appropriate training and participation;
- understanding of professional standards and applicable legal and regulatory requirements (this would include an understanding of the applicable financial reporting framework and expertise in the auditing of regularity in the context of the activities that the entity undertakes);
- technical expertise, including expertise with relevant information technology and specialised areas of accounting or auditing;
- ability to exercise professional scepticism and apply professional judgement;
- understanding of the NAO's policies and procedures; and
- knowledge of the relevant industries in which the audited entity operates.

12.11 To help with this, qualified audit staff are 'licensed' to carry out audit assignments. These signify that a member of staff is considered capable of auditing those entities. The following licences exist:

- **General Audit licence**: All CCAB-qualified financial audit staff hold a licence for audits. This is subject to the satisfactory annual completion of CPD requirements, attendance at relevant mandatory courses (such as Audit Skills (Ask) training) and having sufficient and relevant financial audit experience. Non-CCAB-qualified audit staff may also be issued with a general audit licence.
- **Charities SORP licence**: Auditors qualify for this licence provided they have sufficient recent charities audit experience, and complete suitable and relevant CPD in charities SORP audit. This licence is required for audits of charitable GRAA companies.
- **Occupational Pension Scheme licence**: Auditors qualify for this licence provided they have sufficient recent occupational pension scheme audit experience, and complete suitable and relevant CPD in Pensions SORP audit.
- **Companies Act licence**: Auditors qualify for this licence provided that they have sufficient recent companies experience, and complete suitable and relevant CPD in companies audit. This licence is relevant both for companies audited under the GRAA and under the Companies Act. For audits of charitable GRAA companies, a Charities SORP licence should be applied for instead of a Companies Act licence. Staff signing off Companies Act audits must be appointed as a Responsible Individual by the ICAEW.
- **International Public Sector Accounting Standards licence**: Auditors qualify for this licence provided they have sufficient recent IPSAS experience and have completed suitable and relevant CPD in the IPSAS framework.
- **IT Financial Audit licence**: The licence is held by staff who are CISA-qualified and they have sufficient recent IT Audit experience and complete suitable and relevant CPD to support their practice.

12.12 All holders of specialist licences must also hold a General Audit licence.

12.13 ***Consultation required*** Holding a General Audit licence is normally a requirement for Engagement Team-Leaders, Engagement Managers and Engagement Directors undertaking all financial audit engagements. Where individuals without a General Audit licence are expected to perform these roles, approval must be obtained from the Director, Audit Quality.

12.14 For audits where specialist licences are relevant, holding the relevant licence is normally a requirement for Engagement Managers and Engagement Directors undertaking the assignment. The Engagement Manager should hold the relevant licence or be supervised by an Engagement Director with the licence.

12.15 If the Engagement Director does not hold the relevant licence, a second director with the licence can be appointed as a reference partner to mentor the Engagement Director as he/she trains

for the licence. This reference partner cannot also act as an EQR as he/she may be involved in helping reach key judgements and decisions and would therefore not be sufficiently independent to provide the objective evaluation required by ISA (UK) 220 (Revised July 2021). The presence of a reference partner mentoring the Engagement Director does not affect the decision to appoint an EQR where this would be appropriate.

Delegated signature

12.16 ***Consultation required*** The C&AG may decide to delegate the signature of an engagement for all engagements except for those where he is personally appointed by statute. All requests for delegated signature must be approved by the C&AG based on a recommendation from the Director, Audit Quality. Therefore, requests for delegation of signature must be submitted to FAPQ in the first instance. The Director, Audit Quality will then make a submission through Private Office as appropriate.

12.17 Staff signing off Companies Act audits must be appointed as a Responsible Individual by the ICAEW. Therefore, signature of Companies Act audits may only be delegated to Responsible Individuals.

Identification of the Key Audit Partner

12.18 In accordance with paragraph 34-1(c)(iv) of ISQM (UK) 1, as part of the engagement risk management procedures for both new and continuing audit engagements, the engagement team should document within the Engagement Risk Assessment Audit Form who is the Key Audit Partner for the engagement and confirm whether the Key Audit Partner is eligible for appointment as a statutory auditor. In the UK, eligibility for appointment as a statutory auditor is dealt with in Sections 1212 to 1225 of the Companies Act 2006.

12.19 For engagements where the C&AG is appointed auditor by statute, the C&AG is a Key Audit Partner. The C&AG is eligible for appointment as a statutory auditor under Part 42 of the Companies Act 2006. He is therefore able to be appointed auditor of a charity as per Section 144(2)(a) of the Charities Act 2011.

12.20 For audits performed under the Companies Act (this does not include GRAA Company audits), the Engagement Director must be appointed as a Responsible Individual by the ICAEW – Responsible Individuals are eligible for appointment as a statutory auditor to perform the audit on the C&AG's behalf in accordance with Section 1227 of the Companies Act. These directors sign the audit report "for and on behalf of the C&AG" as senior statutory auditor, the term applied by Section 504 of the Companies Act to the individual responsible for signing on the firm's behalf (analogous to engagement partners in private firms). The C&AG is then referred to as the statutory auditor, where a private sector auditor would insert the firm's name on the audit report.

12.21 For GRAA companies, the C&AG will sign the audit report personally as statutory auditor, for which appointment he is eligible under Section 1226 of the Companies Act.

12.22 For charity audits performed under the Charities Act 2011, the Key Audit Partner should be eligible for appointment under Chapter 3 of Part 8 of that Act.

12.23 In addition to the individual who signs the statutory audit report, the Engagement Director on an audit is also a Key Audit Partner, by virtue of the fact that they are primarily responsible for carrying out the audit on behalf of the C&AG. In the case of a group audit, the Engagement Directors of material components in the group will also be Key Audit Partners for the purpose of the group audit.

12.24 The NAO's formal designation of Key Audit Partners for each audit of financial statements engagement under paragraph 34-1(j) of ISQM (UK) 1 operates as follows:

- The C&AG is designated a Key Audit Partner for engagements where the C&AG is appointed as auditor by the provisions of this Manual.
- Key Audit Partners in the Director or Executive Director grades will be designated through the annual portfolio rotations process.
- Key Audit Partners in the Senior Audit Manager grade will be designated through their inclusion in a list of Key Audit Partners published by FAPQ on the Financial Audit Practice and Quality Sharepoint page. The list will be compiled and updated regularly using data from Financial Force and comprise those in the Senior Audit Manager grade who are assigned in the Engagement Director role for an active audit of financial statements project.
- Individual Group Engagement Teams will document the Engagement Directors of material components who are Key Audit Partners for the group audit within the Engagement Risk Assessment Audit Form in Apex. Where a material component of the group is not audited by the NAO, the engagement team should identify the person performing the role of Engagement Partner for that component, who will also be a Key Audit Partner for the purpose of the group audit.

12.25 ***Consultation required*** Where there is a need to change the designation of Key Audit Partner (regardless of grade) during an engagement which is not part of a centrally managed process, e.g. not part of Director promotions / rotations, the Engagement Director must notify FAPQ of the change. This requirement does not apply to Key Audit Partners external to the NAO.

Section 7: Audit workflow

Chapter 13: Process summary for NAO audits of financial statements

Relevant standards and guidance

13.1 ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.

The process for an audit of financial statements

13.2 The process is divided into the following phases:

- Setup: The auditor obtains approval to accept or continue with the engagement, sets up a Apex Audit Engagement and Financial Force project and determines whether roles on the audit are to be delegated.

- Planning: The auditor gathers information on the entity, makes an assessment of materiality and uses the Risk Assessment in Apex to assess the risks of material misstatement. The auditor identifies and documents relevant controls and then selects appropriate controls and substantive responses to the identified risks.

- Planning (Regularity): Where a regularity opinion is given, the auditor carries out an assessment of the risks of material irregular transactions, reviews controls over regularity and selects appropriate responses to these risks.

- Fieldwork: The auditor carries out the procedures selected at the planning stage as responses to the risks of material misstatement and, where relevant, risks of material irregular transactions. The auditor then evaluates the results of these procedures and comes to a conclusion on the level of assurance obtained.

- Completion: The auditor reports to those charged with governance, issues a certificate or report and finalises the audit file.

- Follow-up: The auditor gathers and responds to feedback on the audit.

13.3 ***Figure 13A*** shows the high-level process map for an audit of financial statements.

Figure 13A: High-level process summary

1. Setup	2. Planning		3. Fieldwork	4. Completion	5. Follow-up
	True and fair	Regularity			
Audit engagement approval	Gathering entity initial information	Initial risk assessment	Request, prepare and assess the evidence	Complete certification	Ensure continuous improvement of the audit
	Financial Reporting Sub-Activity scoping	Controls	Evaluate the evidence	Lock audit file	
	RoMM scoping	Responses to risks		Destroy audit file	
	Inherent risk assessment				
	Review controls				
	Responses to risks				

Chapter 14: Audit engagement approval

Relevant standards and guidance

14.1 ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards on Auditing (UK)* deals with the independent auditor's overall responsibilities when conducting an audit of financial statements in accordance with ISAs (UK), including the overall objectives of the independent auditor and the nature and scope of an audit designed to enable the independent auditor to meet those objectives.

14.2 ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. This includes the acceptance and continuance of client relationships and audit engagements.

14.3 ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* deals with the auditor's responsibility to prepare audit documentation for an audit of financial statements. This includes documentation of significant matters and related professional judgements which, at the planning stage (but also in the later stages of the audit), includes matters that give rise to significant risks (as defined in ISA (UK) 315 (Revised July 2020)).

14.4 ISA (UK) 300 (Revised June 2016) (Updated May 2022) *Planning an audit of financial statements* deals with the auditor's responsibility to plan an audit of financial statements.

14.5 ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.

14.6 Paragraphs 1-72 to 1-82 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 315 (Revised July 2020) in the public sector.

Assess/evaluate and obtain approval for proposed new engagement

14.7 ***Consultation required*** If the audit is a new engagement, the auditor follows the engagement acceptance process set out in Section 5: New engagements and standing information. This should include the following steps:

- Anti-money laundering checks
- Engagement Risk Assessment Audit Form
- Briefing pack for prospective Engagement Director
- Consultation with FAPQ
- C&AG briefing
- C&AG decision

Engagement continuance and re-acceptance procedures

14.8 If the audit is an existing engagement, the auditor follows the engagement continuance and re-acceptance procedures set out in Section 5: New engagements and standing information.

Set up audit file and Financial Force project

14.9 For a new engagement, or a new year of an existing engagement, the auditor sets up an Audit Engagement in Apex. The Apex file is prepared to comply with the requirement to prepare an audit file in ISA (UK) 230 (Revised June 2016) (Updated May 2022).

14.10 The auditor also ensures that a Financial Force project has been set up for each engagement.

The audit file

14.11 For the purpose of applying ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation,* the 'audit file' for NAO audits of financial statements is considered to consist of the Apex audit file or files (including the Audit Response Group Workflow Steps, embedded forms, Risk Assessment and Audit Responses) identified with the name of the audited entity or engagement, subject to the following section on audit documentation spread between multiple Apex Audit Engagements.

14.12 The audit file does not include documentation or data that should be held on AIMS or on Sharepoint.

14.13 ***Consultation required*** All financial audit engagements should be performed in Apex, unless otherwise agreed through consultation with FAPQ. FAPQ will maintain details of all audits which are undertaken outside the Apex environment.

Audit documentation spread between multiple Apex projects

14.14 ***Consultation required*** ISA (UK) 230 (Revised June 2016) (Updated May 2022) does not require the whole 'audit file' to be within one self-contained electronic file (it defines an audit file as "one or more folders or other storage media"), and some teams perform work across multiple Apex files covering the same audit engagement. For example, where common function work is performed on a service organisation or IT function that serves multiple NAO clients, the Apex files for those clients may link to a single common function audit file. Where the audit team intends to adopt for the first time an arrangement whereby audit documentation is spread between more than one Apex Audit Engagement, they should consult FAPQ.

14.15 Where this type of arrangement is adopted, the auditor should ensure that there is a prominent file note included in both audit files in Apex to explain where the cross-referenced documentation can be found and provide a link and project name reference to those. This is to make navigation through the files, either by internal or external reviewers, quick and easy to follow.

14.16 Where the audit file is spread between multiple inter-linked Apex projects, in order to comply with internal NAO policy on file closure, all the inter-linked projects must be closed within 20 working days of the first audit being certified. The auditor should consider whether this will be feasible if the certification dates for the different bodies are likely to be significantly different.

Role assignments

14.17 Role assignment decisions are made centrally in line with the process set out in Chapter 12: Roles, delegations and licences in order to obtain approval for such arrangements.

Initial steps for Apex file

14.18 The auditor should set up an Apex Audit Engagement following guidance available from the Audit Technology Support team. Mandatory Audit Response Groups relevant to the type of

engagement are imported into the file automatically when responses are generated following completion of the Risk Assessment within Apex.

14.19 The mandatory Audit Response Group templates relevant to each type of engagement in Apex are listed in ***Table 14A*** below.

Table 14A: List of mandatory Audit Response Group templates for each engagement type in Apex

Apex engagement type	Mandatory Audit Response Groups (automatically imported upon audit setup)
In-house Financial Audit	Accounts Preparation Annual Report Conclusions Continuous Risk Assessment Other Audit Matters
Contracted Out Financial Audit	Contracted Out Audits - Review of Accounts Contracted Out Audits - Review of firm's audit work

14.20 The auditor should complete the Engagement Risk Assessment Audit Form and other Workflow Step Items in the Set Up Workflow Step.

14.21 Where appropriate, the auditor prepares and issues a new Letter of Understanding or Letter of Engagement, or documents the reasons why this is unnecessary, referring to the guidance in Chapter 9: Engagement acceptance (statutory and non-statutory) (section entitled 'Agreeing the terms of an audit engagement').

14.22 The auditor considers whether an Engagement Quality Reviewer should be appointed for the engagement and documents this within the relevant Workflow Step Item, following the guidance in Chapter 7: Engagement Quality Review.

Set Up Workflow Step signoff

14.23 Once the above steps have been completed, the Engagement Team-Leader or team member completes the Set Up Workflow Step Items, and any associated Attached Files in the Apex file and submits these for review.

14.24 The Engagement Manager and then the Engagement Director perform a two-stage review of the Set Up Workflow Step Items in the Apex file. The Engagement Manager marks each checklist item as reviewed and the Engagement Director marks off the overall Workflow Step as reviewed. The engagement team should not progress the audit further until the Engagement Director has approved and reviewed the Setup workflow.

Chapter 15: Gathering entity initial information

Relevant standards and guidance

15.1 Paragraphs 16 to 33 and A12 to A48 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* include requirements to obtain information for use in identifying the risks of material misstatement due to fraud.

15.2 Paragraphs 1-38 to 1-51 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 240 (Revised May 2021) (Updated May 2022) in the public sector.

15.3 Paragraphs 13 to 15 and A11 to A14-2 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements* include requirements to obtain an understanding of matters relating to compliance with laws and regulations and make related inquiries.

15.4 Paragraphs 1-52 to 1-60 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 250A (Revised November 2019) (Updated May 2022) in the public sector.

15.5 ISA (UK) 300 (Revised June 2016) (Updated May 2022) *Planning an audit of financial statements* deals with the auditor's responsibility to plan an audit of financial statements.

15.6 ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.

15.7 Paragraphs 1-72 to 1-82 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 315 (Revised July 2020) in the public sector.

15.8 Paragraphs 9 to 18 and A1 to A40 of ISA (UK) 402 (Updated May 2022) *Audit considerations relating to an entity using a service organisation* include requirements to obtain an understanding of the services provided by a service organisation, including internal control.

15.9 Paragraphs 1-90 to 1-96 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 402 (Updated May 2022) in the public sector.

15.10 Paragraphs 13-15 and A19-A63 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures* include requirements relating to risk assessment procedures for accounting estimates and identifying and assessing the risks of material misstatement relevant to accounting estimates.

15.11 Paragraphs 1-108 to 1-115 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 540 (Revised December 2018) (Updated May 2022) in the public sector.

15.12 Paragraphs 11 to 24 and A8 to A45 of ISA (UK) 550 *Related parties* include requirements to obtain information relevant to identifying the risks of material misstatement associated with related party relationships and transactions.

15.13 Paragraphs 1-116 to 1-119 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 550 in the public sector.

15.14 Paragraphs 10-1 to 11-1 and A3 to A7-3 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern* include requirements to obtain an understanding of matters relating to going concern, including management's assessment.

15.15 Paragraphs 1-142 to 1-181 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 570 (Revised September 2019) (Updated May 2022) in the public sector.

Setting the overall audit strategy

15.16 Typically the Engagement Director and Engagement Manager and other engagement team members as appropriate will hold an initial planning meeting with the audited entity (to discuss key developments and issues), and then establish the overall audit strategy based upon the information obtained and their knowledge of the entity. Planning meetings are discussed in the 'Hold internal and external planning meetings' section below.

15.17 The engagement team may also perform preliminary analytical procedures before establishing the overall audit strategy. If preliminary analytical procedures are not performed at this stage of the audit, the engagement team should do so as part of the risk assessment procedures.

15.18 Our existing knowledge of the entity and the information obtained through meetings with the audited entity and preliminary analytical procedures will usually enable the engagement team led by the Engagement Director to perform an initial identification and assessment of the risks of material misstatement. The Risk Assessment within Apex facilitates this assessment.

15.19 In setting the overall audit strategy, the engagement team should have due regard to the key business risks faced by the entity and the prior year financial statements.

Hold internal and external planning meetings

15.20 Key engagement team members (such as the Engagement Manager and Lead) should participate in the planning meetings, but the Engagement Director cannot delegate establishing the overall audit strategy to other team members.

15.21 The audit team holds an initial strategy meeting.

15.22 The auditor holds a planning meeting with the audited entity, in which the ISA-required inquiries of the audited entity are made (any of these inquiries not made during the planning meeting should be made when completing the risk assessment procedures as part of developing the audit plan). These inquiries are discussed in more detail in the section below on 'Planning inquiries'. The outcome of these inquiries is recorded in the Gather Entity Information Workflow Step in the Apex file.

15.23 The audit team holds a Director-led internal planning meeting to discuss the overall audit strategy. This should include discussion (led by the Engagement Director and involving key engagement team members and specialists as appropriate) of the susceptibility of the entity's financial statements to material misstatement and irregular transactions and the application of the financial reporting framework to the audited entity's facts and circumstances. The outcome of this meeting is recorded in the Overall Audit Strategy Audit Form.

15.24 In advance of the Director-led internal planning meeting, the engagement team should review the following sections of the Risk Assessment in Apex (the results of this review will be discussed in the meeting as noted in the following paragraph):

- the scoping of Financial Statement Risk Areas and Financial Reporting Activities; and
- the completed Generic Inherent Risk Factors section.

15.25 The Director-led internal planning meeting should cover the following matters, which should be documented in the Overall Audit Strategy Audit Form:

- the characteristics of the engagement that define its scope (for example, an audit of financial statements performed under ISAs (UK) and Practice Note 10 (Revised 2022), under statute/by agreement, with/without a regularity opinion);
- the assessment of materiality, including classes of transactions, account balances or disclosures with lower levels of materiality;
- what specialist knowledge (if any) is required to complete the risk assessment and what resources and specialist knowledge (if any), including specific licences, are expected to be required to deliver the audit work;
- the timetable of the engagement, in light of the reporting objectives of the engagement and the communications required with those charged with governance;
- the framework of authorities for the entity and the key risks of non-compliance with the framework of authorities (including the identification of any significant risks in relation to the regularity opinion);
- any specific or general quality review findings which should be considered for the audit;
- the results of the preliminary engagement activities carried out as documented within the Engagement Risk Assessment Audit Form, covering the requirements of paragraph 6 of ISA (UK) 300 (Revised June 2016) (Updated May 2022);
- the results of the engagement team's review of the scoping of Financial Statement Risk Areas and Financial Reporting Activities performed within the Risk Assessment in Apex, including the key judgements and discussion points involved in this assessment;
- the results of the engagement team's review of the completed generic inherent risk factor section of the Risk Assessment in Apex, including the key judgements and discussion points involved in this assessment; and
- any other matters that are relevant to developing the overall audit strategy and/or significant in directing the engagement team's efforts, which may include a consideration of recent significant changes and developments that may affect the audit, such as on key programmes, and what effect this has on our overall risk assessment and the determination of materiality for the financial statements as a whole or for particular classes of transactions, account balances or disclosures;
- other risk assessment procedures that should be completed.

15.26 The discussion among the engagement team about the susceptibility of the entity's financial statements to material misstatement and irregularity:

- allows the engagement team members to exchange information about the business risks to which the entity is subject and about how and where the financial statements might be susceptible to material misstatement and irregularity due to fraud or error;
- provides a basis upon which all engagement team members contribute to the risk assessment through testing established approaches, and sharing information obtained throughout the audit or otherwise that may affect the assessment of risks of material misstatement or the audit procedures performed to address these risks.
- assists the engagement team members to gain a better understanding of the potential for material misstatement or material irregularity at the financial statement level or in the specific areas assigned to them, and to understand how the results of the audit procedures that they perform may affect other aspects of the audit including the decisions about the nature, timing, and extent of controls and substantive audit procedures; and
- provides an opportunity for more experienced engagement team members, including the Engagement Director, to share their insights based on their knowledge of the entity.

15.27 Chapter 30: Fraud responsibilities provides guidance and details of the categories and indicators of fraud that engagement teams should discuss, consider and assess as part of the engagement team discussion.

15.28 The Engagement Team Discussion on Risk and Fraud template may be used to document these requirements.

15.29 The engagement team should make clear on the Apex audit file how all engagement team members have been appropriately briefed about the audit risks and audit plan.

Other information obtained relevant to the engagement

15.30 The engagement team should consider whether they have obtained information as part of the audited entity acceptance/re-acceptance process that indicates the existence of risks of material misstatement or which is otherwise relevant to planning our audit. From acceptance/reacceptance the engagement team may have information from prior periods which impacts the risk assessment, such as indications of aggressive accounting, complex accounting estimates or a history of errors.

15.31 The Engagement Director should consider whether information obtained from other engagements performed for the entity is relevant to identifying risks of material misstatement. This will include information from the NAO's full range of work.

15.32 The Engagement Director and Engagement Manager should ensure that the risk assessment appropriately takes account of the NAO's wider understanding of the audited entity through the Office's wider work.

15.33 As part of establishing the overall audit strategy, the Engagement Director may conclude that the engagement team have sufficient understanding of one or more areas from prior periods to enable the extent of the risk assessment procedures to be reduced.

Planning inquiries

15.34 The ISAs require that a number of specific inquiries are made of management and those charged with governance to inform the engagement team's risk assessment processes.

15.35 Any inquiries which have not been addressed as part of establishing the overall audit strategy should be made as part of the risk assessment procedures. When making inquiries, where responses to inquiries of management or those charged with governance are inconsistent, investigate the inconsistencies.

15.36 Many inquiries will occur as part of the client planning meeting held by the Engagement Director and/or the Engagement Manager in advance of the audit, and therefore are included as part of establishing the overall audit strategy.

15.37 ***Table 15A*** below shows inquiries appropriate for the engagement Director or engagement Manager to ask of the most senior audited entity staff, such as the Accounting Officer and Finance Director, to inform their overall understanding of the entity.

Table 15A: Topics appropriate to discuss at a senior level (such as Engagement Director or Engagement Manager and Accounting Officer or finance director)

ISA-mandated inquiries	Other inquiries

Laws and regulations Whether the entity is in compliance with laws and regulations that may have a material effect on the financial statements (paragraph 15(a) of ISA (UK) 250A (Revised November 2019) (Updated May 2022)). Changes to laws or regulations that may be expected to have a fundamental effect on the operations of the entity (paragraph A11 of ISA (UK) 250A (Revised November 2019) (Updated May 2022)).	The attitudes, awareness, and actions of those charged with governance concerning the entity's internal control and its importance in the entity, including how those charged with governance oversee the effectiveness of internal control, and the detection or possibility of fraud
Going concern Management's knowledge of events or conditions beyond the period of management's assessment that may cast significant doubt on the entity's ability to continue as a going concern. (paragraph 10-4 of ISA (UK) 570 (Revised September 2019) (Updated May 2022)).	Any key judgements of which the audited entity is aware affecting the entity, including matters beyond the period of management's assessment which may impact on the ability of the entity to continue as a going concern.
Fraud Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments; their process for identifying and responding to the risks of fraud in the entity, including any specific risks of fraud that management has identified or that have been brought to its attention, or classes of transactions, account balances, or disclosures for which a risk of fraud is likely to exist; their communication, if any, to those charged with governance regarding its processes for identifying and responding to the risks of fraud in the entity; and their communication, if any, to employees regarding its views on business practices and ethical behaviour (paragraph 18 of ISA (UK) 240 (Revised May 2021) (Updated May 2022). Whether management has any knowledge of any actual, suspected or alleged fraud affecting the entity (paragraph 19 of ISA (UK) 240 (Revised May 2021) (Updated May 2022)).	The organisational structure and the extent to which the responsibility for ensuring regularity is devolved from the Accounting Officer/Chief Executive to, for example, the Principal Finance Officer or Finance Director, including any new business activities
Related parties The identity of the entity's related parties, including changes from the prior period; the nature of the relationships between the entity and these related parties; and whether the entity entered into any transactions with these related	

parties during the period and, if so, the type and purpose of the transactions (paragraph 13 of ISA (UK) 550 (Updated May 2022)).	

15.38 ***Table 15B*** below lists the planning inquiries required to be addressed to those charged with governance. These may be convenient to address while presenting the Audit Planning Report.

Table 15B: Inquiries required of those charged with governance

ISA mandated inquiries	Other inquiries
Fraud How those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the controls that management has established to mitigate these risks; whether they have knowledge of any actual, suspected or alleged fraud affecting the entity; and the risks of fraud in the entity, including those that are specific to the entity's business sector (paragraphs 21 to 22-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022)). These separate inquiries would not be required if all those charged with governance were also members of management, but this is unlikely to be the case for most public bodies.	**Regularity** Those charged with governance's knowledge of any actual, suspected or alleged irregularity affecting the entity (unless all of those charged with governance are involved in managing the entity). These inquiries are made in part to corroborate the responses to the inquiries of management.
Laws and regulations Whether the entity is in compliance with laws and regulations that may have a material effect on the financial statements (paragraph 15(a) of ISA (UK) 250A (Revised November 2019) (Updated May 2022)).	The allocation of responsibilities between those charged with governance and management
	The entity's objectives and strategies, and the related business risks that may result in material misstatements;
	Matters those charged with governance consider warrant particular attention during the audit, and any areas where they request additional procedures to be undertaken
	Significant communications with regulators
	Other matters those charged with governance consider may influence the audit of the financial statements.
	Possibility, knowledge of and process for identifying and responding to the risks of fraud
	Oversight of the effectiveness of internal control

	Operational performance
	The actions of those charged with governance in response to developments in accounting standards, corporate governance practices, Treasury and Cabinet Office guidance and related matters
	The responses of those charged with governance to previous communications with the auditor

15.39 ***Table 15C*** below summarises the inquiries and with whom they should be made. Those marked with an asterisk are mandated by ISAs (UK).

Table 15C: Appropriate persons to make inquiries of

Topic	Audited entity staff	Internal Audit
Fraud		
*The possibility of fraud and related controls:	Y	Y
*Assessment of the risk of material misstatement due to fraud, including the nature, extent and frequency of such assessments	Y	Y
*Process for identifying and responding to the risks of fraud, assessment of these arrangements and the outcome of these arrangements to date	Y	Y
*Communication, if any, to those charged with governance regarding management's processes for identifying and responding to the risks of fraud	Y	Y
*Communication, if any, to employees regarding management's views on business practices and ethical behaviour	Y	
*Whether there is any knowledge of any actual, suspected or alleged fraud affecting the entity, and what are their views about the risks of fraud	Y	Y
*Classes of transactions, account balances and disclosures most at risk of fraud and any fraud identified in these	Y	
*Any whistleblowing or complaints by potential whistleblowers and the response to these	Y	
*Inquire about specific internal audit procedures to detect fraud and how management has responded to any related findings		Y
*For service organisations, whether they have reported to the user entity any fraud or other irregularity (paragraph 19 of ISA (UK) 402 (Updated May 2022))	Y	Y
Laws and regulations		
The nature of the legal and regulatory framework and how the entity complies with that framework:	Y	

Changes in laws and regulations that directly determine the reported amounts and disclosures in the financial statements	Y	
Other laws and regulations that may be expected to have a fundamental effect on the operations of the entity	Y	
Policies and procedures regarding compliance with laws and regulations	Y	Y
Policies or procedures adopted for identifying, evaluating and accounting for litigation claims	Y	
Knowledge of non-compliance with laws and regulations or notice of any possible instances of such non-compliance	Y	
*For service organisations, whether they have reported any non-compliance with laws and regulations (paragraph 19 of ISA (UK) 402 (Updated May 2022))	Y	Y
Any examinations or inquiries performed by licensing, tax or other authorities/regulators	Y	
Significant communications with regulators	Y	Y
Any changes affecting corporate governance practices		Y
Financial reporting		
FReM changes affecting the current year accounts and actions taken in response to developments in accounting standards, corporate governance practices, etc.	Y	
General views on the entity's risk assessment process relating to financial reporting	Y	
Appropriateness of accounting policies adopted and any events or transactions that may cause new or amended accounting policies	Y	
Significant transactions outside the normal trading activities of the business	Y	
Events or changes in circumstances that would cause an impairment of non-current assets	Y	
Issues identified so far that may impact the preparation of the accounts	Y	
Assessment of the going concern basis for preparing the financial statements and the outcome of that assessment	Y	
Process to ensure the compliance and completeness of narrative on critical accounting policies and judgements	Y	
Information on the use of financial instruments, including derivatives	Y	
Information on the status of contingencies from the prior year	Y	
Any guarantee contracts	Y	
Any loss contingencies and/or un-asserted claims that may affect the financial statements	Y	
Accounting estimates		
*New or revised accounting estimates	Y	

*New types of conditions, events, regulatory changes, transactions or changes in the terms of transactions that that may give rise to new or revised accounting estimates	Y	
*Changes to accounting policies relating to accounting estimates	Y	
*Where the financial statements include amounts based on significant estimates, how the accounting estimates have been made, the nature of the data used, and the degree of estimation uncertainty inherent in the estimate	Y	
Use of experts in accounting for e.g. pensions / provisions / etc.	Y	
Consider whether there are the following in the accounts and also whether a fair value is used:		
• Provisions	Y	
• Depreciation	Y	
• Property, Plant and Equipment fair values	Y	
• Inventory valuations	Y	
• Internally developed assets e.g. software	Y	
• Pension liability	Y	
• Apportionments of lease payments between those for the asset and those for the service	Y	
• Interest rates implicit in leases	Y	
Related parties		
*The nature and extent of transactions with related parties (paragraph 13 of ISA (UK) 550)		
• Identity of related parties, including changes from the prior period	Y	
• Nature of the relationships with these related parties (including changes from the prior year)	Y	
• Significant transactions entered into with these related parties during the period (type and purpose)	Y	
*Controls in place to:		
• identify, account for, and disclose related party relationships and transactions;	Y	
• authorise and approve significant transactions and arrangements with related parties; and	Y	
• authorise and approve significant transactions and arrangements outside the normal course of business	Y	
Regularity		
The possibility of irregularity and related controls	Y	Y

Assessment of the risk (including significant risks) of material misstatement due to irregularity that management/internal audit has identified or that have been brought to its attention, or classes of transactions, account balances, or disclosures for which a risk of irregularity is likely to exist	Y	Y
Process for identifying and responding to the risks of irregularity	Y	Y
Communication, if any, to those charged with governance regarding management's processes for identifying and responding to the risks of irregularity	Y	Y
Knowledge of actual, suspected or alleged irregularity	Y	Y
The entity's organisational structure and the extent to which the responsibility for ensuring regularity is devolved from, for example, central government, the Accounting Officer or Chief Executive to, for example, the Principal Finance Officer or Finance Director	Y	Y
What practices and controls the entity has over grant regularity and residual risks	Y	Y
The Accounting Officer's or Chief Executive's methods of controlling those officers, departments or agents responsible for ensuring regularity	Y	Y
*Where service organisations are used by the entity, whether any irregularities have been reported to the user entity (paragraph 19 of ISA (UK) 402 (Updated May 2022))	Y	Y
Control and IT system changes		
Views on the entity's control environment and assessment of the process for reviewing the effectiveness of internal control	Y	
Changes to the IT system in period	Y	Y
Changes to controls the engagement team is relying on and other controls relevant to the audit	Y	Y
Accounts production processes and status of the prior year's reported internal control deficiencies	Y	
Risk and governance		
Communication to those charged with governance regarding business risks (including fraud)	Y	
The allocation of responsibilities between those charged with governance and management, including regularity	Y	Y
Oversight of the effectiveness of internal control	Y	Y
Procedures ensuring the compliance and completeness of Governance reports	Y	Y
Procedures ensuring the compliance and completeness of Sustainability reports	Y	Y

Significant risks and key judgements		
Consider for example: • Budgetary pressures (RDEL, CDEL, RAME, CAME) • Defined benefit pension schemes • Expected credit losses • Treatment of significant impairments, disposals and revaluations • New accounting system / team / new IT team / outsourced provider • Estimates requiring use of multiple economic scenarios	Y	
How does the audited entity ensure the compliance and completeness of narrative on critical accounting policies and judgements	Y	
Issues around use of service organisations or common functions, uncorrected misstatements from service organisations	Y	Y
Key disclosures		
What disclosures are likely to be included? Disclosures should only be included where material. If included and immaterial, review only for consistency with other information. Consider whether you might expect the audited entity to include the following: • Segmental disclosures • Fees and charges • Commitments • Remuneration report • Losses and special payments • Contingent liabilities • Parliamentary reporting (remote contingent liabilities) • IAS 19 (pension) disclosures • Staff costs note • Going concern / subsequent events	Y	
Audit-related topics		
Nature of work at each visit	Y	
Client liaison schedule and securing audited entity's (and our) commitment to deliver to it	Y	
The appropriate person(s) in the entity's governance structure with whom to communicate.	Y	
Responses to previous communications with auditors	Y	
Internal audit function		
Copy of the internal audit charter in order to obtain an understanding of the activities performed, oversight responsibilities and reporting process		Y
How the organisational status of the internal audit function, including the function's authority and accountability, supports the ability of the function to be free from bias, conflict of interest, or undue influence of others to override professional judgments		Y

Whether those charged with governance oversee employment decisions related to the internal audit function		Y
Whether the internal audit function is adequately and appropriately resources relative to the complexity of the audited entity and the nature of its operations		Y
Whether the internal auditors are members of relevant professional bodies or have certifications that oblige them to comply with the relevant professional standards, including continuing professional education requirements		Y
Whether there are adequate, documented internal audit procedures in place to ensure quality of reporting		Y

15.40 As well as inquiries of senior management and those involved in the financial reporting process, the engagement team may wish to obtain information or obtain the perspective of others within the entity. These inquiries may include the following:

- inquiries directed towards those charged with governance may help the engagement team understand the environment in which the financial statements are prepared;
- inquiries directed toward internal audit personnel may provide information about internal audit procedures performed during the year relating to the design and effectiveness of the entity's internal control and whether management has satisfactorily responded to findings from those procedures;
- inquiries of employees involved in initiating, processing or recording complex or unusual transactions may help the engagement team to evaluate the appropriateness of the selection and application of certain accounting policies;
- inquiries directed toward in-house legal counsel may provide information about such matters as litigation, compliance with laws and regulations, knowledge of fraud or suspected fraud affecting the entity, warranties, post-sales obligations, arrangements (such as joint ventures) with business partners and the meaning of contract terms; and
- inquiries directed towards marketing or sales personnel may provide information about changes in the entity's marketing strategies, sales trends, or contractual arrangements with its customers.

15.41 The engagement team may develop a better understanding of the entity and its environment through communication with the audit committee at a planning stage, including evaluating the effectiveness of the audit committee as part of the entity’s system of internal control.

15.42 Some areas can be discussed without the involvement of senior audited entity or senior NAO staff, but significant findings shall be communicated to all members of the engagement team. The inquiries made should reflect the engagement team’s knowledge of the entity, whether there have been any changes in circumstances in the year and any regularity considerations.

15.43 The engagement team may discuss with management and those charged with governance elements of the audit strategy and plan. However, the engagement team remains responsible for setting the audit strategy and plan.

15.44 A limitation on scope imposed by management (which may become apparent during planning and risk assessment discussions) would normally lead to an auditor declining to accept appointment. The C&AG is normally unable to decline appointment or to resign once appointed and should report this fact to those charged with governance and if appropriate, to Parliament. This point is discussed in paragraphs 1-5 and 1-6 of Practice Note 10 (Revised 2022) .

Planning inquiries – regularity

15.45 In making the required inquiries, the engagement team should also inquire as to the possibility of irregularity where relevant, in particular with respect to fraud or compliance with laws and regulations where those laws or regulations form part of the framework of authorities for that entity.

15.46 When discussing fraud and irregularity with internal audit, this may include inquiring about specific internal audit activities including the procedures performed, if any, by the internal auditors during the year to detect fraud or irregularity and whether management has satisfactorily responded to any findings resulting from those procedures.

Planning inquiries – professional scepticism

15.47 In accordance with paragraph 15 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements*, where responses to inquiries of management, those charged with governance or others within the entity are inconsistent the engagement team should investigate the reasons. The engagement team should also investigate where any responses to these inquiries appear implausible.

Understanding the reporting requirements

15.48 The Engagement Director should ensure that the team have considered and understand the nature of the entity and its financial reporting framework and requirements. These should be clearly documented in the audit file and understood by the engagement team.

15.49 The audit file should clearly document the nature of the entity subject to audit, its financial reporting framework and any other relevant reporting requirements for the engagement.

15.50 For group audits, an initial assessment of the nature of the group should be undertaken as part of developing the overall audit strategy (further guidance may be found in Chapter 25: Group audit procedures). This should include a consideration of the following:

- the boundary of the group;
- component materiality;
- significance of group components; and
- the approach to engagement with component auditors.

15.51 In understanding the financial reporting framework, any specific reporting requirements should be understood sufficiently to enable the design of audit procedures which will give assurance over the disclosures made.

15.52 Examples of reporting objectives of the audit and the nature and timing of planned communications include key dates for expected communications with management and those charged with governance (such as the Audit Completion Report) and whether these should be written or oral.

Risk assessment procedures

15.53 The Engagement Director and Engagement Manager should plan the nature, timing and extent of the risk assessment procedures required to confirm or update our understanding of the entity and the initial identification and assessment of the risks of material misstatement. The procedures required will consist of a mixture of:

- determining whether changes have occurred which would affect our understanding of the entity obtained from previous audits or other experience; and

- additional risk assessment procedures for the current period in one or more areas.

15.54 On the basis of the risk assessment procedures performed, the Engagement Director and Engagement Manager then assess the risks of material misstatement and risks of material irregular transactions and develop the audit plan, following the guidance in Chapter 17: Risk assessment and response planning and Chapter 18: Regularity risk assessment and response planning.

15.55 The overall audit strategy sets out the extent of planned reliance on information from previous audits and experience of the entity, and the procedures planned to determine it remains relevant.

15.56 The engagement team should consult all relevant resources and widely within the Group wherever possible to ensure the overall audit strategy reflects our collective knowledge and understanding of key issues relevant to the entity, such as through consulting our VFM colleagues. In particular, consideration should be given as to whether key issues identified represent significant risks of material misstatement or irregularity.

15.57 The Engagement Director and Engagement Manager should plan the nature, timing and extent of the risk assessment procedures required to confirm or update our understanding of the entity and the initial identification and assessment of the risks of material misstatement

15.58 The Appendix to ISA (UK) 300 (Revised June 2016) (Updated May 2022) includes examples of factors that may be considered in establishing the overall audit strategy.

15.59 Particularly significant factors in the context of planning an audit for the NAO's audit portfolio include:

- the entity's use of service organisations or common functions and how the engagement team can obtain evidence concerning the design or operation of controls performed by them;
- the expected use (and impact) of information obtained from other work performed on the entity, such as from VFM work; and
- changes in the legal environment affecting the entity.

15.60 Our existing knowledge of the entity is particularly relevant with respect to understanding the entity, its environment, and the entity's internal control. The nature of the NAO's audit portfolio and activities means that the engagement team will typically have significant knowledge from our previous experience with the entity, including from:

- our prior year audit and work papers; and
- information about the audited entity collated through our non-financial audit work.

15.61 In performing procedures to determine whether information the engagement team intends to use from prior periods remains relevant, the engagement team should:

- inquire of management and other relevant staff; and
- perform procedures such as examination of systems documentation or walkthroughs of relevant systems.

15.62 If risk assessment procedures are performed before the overall audit strategy has been signed off, the reasons for this should be clearly documented.

15.63 If controls or substantive procedures are performed before the audit plan has been approved, the reasons for this should be clearly documented.

Risk assessment procedures – regularity

15.64 Where a regularity opinion is provided, the planned risk assessment procedures should enable the engagement team to develop, or determine that they have, a sufficient understanding of the external framework of authorities affecting the entity and its activities to be able to identify events, transactions and practices that may significantly affect the regularity of transactions.

15.65 The entity's framework of authorities should be clearly set out and documented within the audit file. Further guidance on establishing the framework of authorities may be found in Chapter 11: Determining the framework of authorities. The Engagement Director should ensure that all team members are aware of the entity's framework of authorities.

Documentation

15.66 The results of our inquiries would typically be reflected in minutes of meetings. Often the minutes of a meeting will serve as evidence that ISA (UK) requirements have been met so there will be no need to document further beyond referencing key information within those minutes elsewhere on file and explaining whether the matters raised within those minutes impact on our risk assessment. Alternatively, template letters are available to send management and internal audit to facilitate effective documentation of these enquiries.

15.67 The overall audit strategy (for internal purposes) is held within the Apex audit file. The overall audit strategy is documented in multiple parts of the audit file, including the Workflow Steps for Set Up, Gather Entity Information and Risk Assessment & Response Plan. This will record the key decisions made in planning the audit and facilitate communication of significant matters to the engagement team.

Financial Audit Director Portfolio Review Meetings

15.68 As communicated to the Financial Audit Service Line by FAPQ, each Financial Audit Director will have a Director Portfolio Review Meeting to support strategy setting. FAPQ determines the level of consultation required for relevant audits following the guidance in Chapter 6: Technical support and consultation and communicates the process to the Financial Audit Service Line. The audit team documents the outcome of these consultation procedures in the Apex audit file.

Resource allocation and assessment

15.69 The auditor plans and allocates the resources required for the audit, including people to work on the team and the budgets required. In accordance with paragraphs 25 to 26 of ISA (UK) 220 (Revised July 2021), the Engagement Director is responsible for determining that:

- sufficient and appropriate resources to perform the engagement are assigned or made available to the engagement team in a timely manner, taking into account the nature and circumstances of the audit engagement, the NAO's policies or procedures, and any changes that may arise during the engagement; and
- members of the engagement team, and any auditor's external experts (along with, for audits applying non-UK adapted ISAs, internal auditors who provide direct assistance) who are not part of the engagement team, collectively have the appropriate competence and capabilities, including sufficient time, to perform the audit engagement.

15.70 ***Consultation required*** Alternatively, in accordance with paragraph 27 of ISA (UK) 220 (Revised July 2021), if the Engagement Director determines that resources assigned or made available are insufficient or inappropriate in the circumstances of the audit engagement, they should appropriate action, including communicating with appropriate individuals about the need to assign or make available additional or alternative resources to the engagement. For Human resources, the

appropriate individuals to consult will be Financial Audit Operations; for Technological and Intellectual resources, the appropriate consultation route is FAPQ.

15.71 Application guidance on undertaking this assessment is provided within paragraphs A59 to A79 of ISA (UK) 220 (Revised July 2021), and these requirements have been embedded within the Resource Assessment section of the Overall Audit Strategy Audit Form within Apex, which all engagement teams are required to complete as part of establishing their overall audit strategy.

15.72 In respect of the assessment of Technological resources, the following IT applications have been approved for use by the NAO and therefore individual engagement teams are not required to undertake additional quality assurance procedures upon these as part of their Resource Assessment:

- Apex;
- Pentana;
- the Journals App and GL-TB App developed by the NAO (noting that the engagement team will need to consier the quality assurance procedures used over bespoke applications developed within the NAO and used on audit engagements);
- IDEA;
- Financial Force;
- Huddle;
- Data snipper;
- Confirmation.com;
- Operis Analysis Kit (OAK); and
- Microsoft Office applications.

15.73 Intellectual resources available to NAO engagement teams which have been subject to central quality assurance procedures and for which no further quality assurance procedures are required at an individual engagement level, include:

- this Manual;
- auditing and accounting standards available on Croner-i;
- Practice Note 10 (Revised 2022);
- financial audit tools and templates and guidance available on Sharepoint or embedded within Apex;
- all methodological content housed within Apex;
- specialist guidance produced by central teams (such as Centres of Expertise);
- resources from the ICAEW Corporate Reporting and Audit and Assurance Faculties; and
- market data provided by Refinitiv (overseen by the Financial Instruments Centre of Expertise).

15.74 The Engagement Director and Engagement Manager shall determine the nature, timing and extent of resources necessary to perform the audit:

- the need to use appropriately experienced team members for riskier or more complex areas;
- the use of experts for complex matters (in particular for audits involving significant estimates; spreadsheet or models; and for the audits of companies; and charities) and whether these are to be obtained within the NAO and externally, for example drawing on the NAO's contractor audit firms.
- the resources to deploy for specific audit areas;
- the extent of review required when using the work of internal audit or auditors of components of a group; and
- the extent of interim audit work planned and the allocation of work between phases of the audit.

15.75 The engagement team should update Financial Force with budget information, milestones and resource allocations.

15.76 The Apex audit file, including the Resource Assessment section of the Overall Audit Strategy Audit Form, should consider the levels of resources required at the different stages of the audit, how such resources will be managed, directed and reviewed and how the overall and detailed review are expected to take place, including the assessment of the requirements for EQR review. This may include consideration of when and by whom the overall and detailed reviews should be performed, and an assessment of the requirements for EQR review.

15.77 Where there is an opportunity to obtain audit evidence more efficiently or effectively through computer-assisted audit techniques such as data analytics, this may impact upon the planned resource needs of the engagement and this should be reflected in the overall audit strategy.

15.78 Paragraphs 11 and A16 to A17 of ISA (UK) 300 (Revised June 2016) (Updated May 2022) establish requirements for the engagement team to plan the nature, timing and extent of direction and supervision of engagement team members and the review of their work.

15.79 The Engagement Director's consideration of resourcing at the initial planning meeting stage should also include a consideration of any specialist resources which may be required to complete the risk assessment.

Preliminary Analytical Procedures

15.80 Preliminary Analytical Procedures (PAPs) as risk assessment procedures help to identify aspects of the entity of which the engagement team was unaware and to corroborate their existing understanding through exploring relationships between information, both financial and non-financial which may have an audit impact. Unusual or unexpected relationships, trends or ratios that are identified through PAPs may assist in identifying risks of material misstatement or irregularity at the financial statement or assertion level, especially risks due to fraud.

15.81 The appropriate PAPs to perform will vary from entity to entity, depending upon the relationships between financial and non-financial data which would be expected for each entity.

15.82 The NAO's approach to PAPs involves, on both a consolidated and entity basis, at least:

- a review of the performance measures against which the entity is assessed and the impact that these may have on the reported results; and
- a comparison of e.g. the in-year financial statements, monthly management accounts, year-end forecasts (or projected figures) against the prior year's figures, including examination of expected and unexpected trends, including where relevant the Statement of Outturn against Parliamentary Supply and Estimate.

15.83 The appropriate PAPs to perform will vary from entity to entity, depending upon the relationships between financial and non-financial data which would be expected for each entity

15.84 The VFM team may have knowledge of current programmes, activities or policies the entity is implementing and what their associated cost, success or failure may mean for audit areas.

15.85 The entity may be embarking on a project of significant public and parliamentary interest. Other teams within or outside of the Group may have knowledge or experience of related audit risks associated with such ventures.

15.86 The strength of PAPs depends upon the granularity of the procedures performed. PAPs performed upon high level data (e.g. at the financial statement level) provide only a broad initial indication about the possibility of a material misstatement.

15.87 Where PAPs are performed at a high level, the results of other risk assessment procedures may assist in evaluating the results. Engagement teams should consider performing PAPs on disaggregated areas such as at the account, project code or perhaps for an on-going project impacting more than one account line.

15.88 If full interim or monthly financial information is not available (for example, where the management or in-year accounts do not include a Statement of Financial Position), it may be necessary to adopt a two-stage approach of performing limited analytical procedures at the planning stage based upon the information that is available, and then performing analytical procedures on an early draft of the financial statements to complete our risk assessment procedures.

15.89 In designing PAPs, the engagement team should consider the relationships between financial statement items (and non-financial data) which are relevant to public sector entities: for example,

- between financial information that would be expected to conform to a predictable pattern based on the entity's experience, such as staff costs; and
- where expenditure and income are expected to conform to a demand pattern that can be deduced from other related data, such as the number of people within a certain age range.

15.90 It will normally be appropriate to consider programme income and expenditure and administrative income and expenditure separately.

15.91 Programme expenditure and income relate to the actual function of the audited entity, and:

- may be closely related to non-financial information such as the number of bodies in receipt of grant or persons receiving hospital treatment;
- may not always be directly comparable to prior periods because of changes in eligibility rules and Government policy; and
- are usually comparable to published departmental / entity strategy and expenditure plans.

15.92 Administrative costs relate to the running of the audited entity and can be distinguished from programme expenditure because they are:

- usually closely related to comparable information for prior periods and are less likely to experience significant fluctuation owing to changes in Government policy and the entity's strategy;
- closely related to information such as number of locations, number of employees and size of buildings; and
- usually directly comparable to other entities with similar establishment sizes.

Key templates for gathering entity initial information

15.93 The engagement team should complete the following templates listed in ***Table 15D***, which are either created automatically or hosted within the Apex file:

Table 15D: Key templates for gathering entity initial information

Template	Purpose	Conclusion
'Understanding the entity and its environment'	Documenting the engagement team's understanding of the entity's organisational structure, ownership and governance; its business model and business risks; industry, regulatory and other external factors; the measures used to assess the entity's financial performance; the applicable financial reporting framework; the entity's accounting policies and the reasons for any changes thereto (as required by paragraph 19 of ISA (UK) 315 (Revised July 2020) and the related application guidance). Documenting the engagement team's understanding of the entity's related parties; the nature of their relationship with the entity; and any impact on the financial statements (as required by paragraph 13 of ISA (UK) 550 and the related application guidance). For further guidance, see the section later in this Chapter entitled 'Understanding the entity and its environment'.	Whether we have obtained sufficient understanding of the entity and its environment to be able to assess the impact of Inherent Risk Factors on the risks of material misstatement.
'Understanding the entity's system of internal control'	Documenting the engagement team's understanding of the nature of the components of the entity's system of internal control, including: • the control environment; • the risk assessment process; and • the process for monitoring the system of internal control. (as required by paragraphs 21, 22, 23 and 24 of ISA (UK) 315 (Revised July 2020) and the related application guidance). Documenting the engagement team's understanding of the entity, its environment and internal controls relevant to accounting estimates that apply at the entity level rather than to specific transactions and balances (as required by paragraph 13 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) and the related application guidance). Documenting the engagement team's understanding of the risks of fraud (as required by paragraph 17 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) and the related application guidance).	Our overall evaluation of the entity's control environment, risk assessment process or process for monitoring the system of internal control and whether any deficiencies have been identified in these components of the entity's system of internal control Whether there are significant deficiencies to report to those charged with governance in accordance with ISA (UK) 265 (Updated May 2022). Where deficiencies in the entity's overall control environment, risk assessment process or the process for monitoring the system of internal control are identified, Financial Statements-level risks of material misstatement to address risks arising from these deficiencies should be scoped in within the Risk Assessment in Apex. Whether we have gained sufficient understanding of the entity's system of internal control.

	Documenting the engagement team's understanding of the entity's general control environment for ensuring regularity (as required by paragraph 2-26 of Practice Note 10 (Revised 2022)).	Whether there are other findings from the risk assessment that could have implications for our audit work.
'Understanding the entity's information systems and communication'	Documenting the engagement team's understanding of the entity's information processing activities as required by paragraph 25 of ISA (UK) 315 (Revised July 2020).	Whether the entity's information systems and communication support the preparation of the entity's financial statements in accordance with the financial reporting framework.
'Rolled forward accounting and audit judgements'	Documenting the significant matters and related significant professional judgements that have arisen in prior years' audits and that remain relevant in the current audit period (as required by paragraph 8(c) of ISA (UK) 230 (Revised June 2016) (Updated May 2022) and the related application guidance). *N.B. This template is an optional but recommended template. Regardless of whether the engagement team uses this template, they are required to document any rolled forward accounting and audit judgements within their Apex file, alongside their consideration of whether they remain relevant to the current audit.*	Whether the audit documentation is sufficient to enable an experienced auditor, having no previous connection with the audit, to understand significant matters that have arisen in prior years' audits and remain relevant in the current audit period, the conclusions reached thereon, and significant professional judgements made in reaching those conclusions.

15.94 The auditor completes these templates and relevant Apex Workflow Step Items at the planning stage to document the understanding of the entity. Where necessary, the auditor arranges meetings or correspondence to obtain client and/or other internal team input to update these templates.

15.95 The engagement team should ensure that the matters documented in the planning templates, including those listed in ***Table 15D*** as well as the Overall Audit Strategy Audit Form and Preliminary Analytical Procedures, are taken into account in the Risk Assessment in Apex.

Understanding the entity and its environment

15.96 In general, the framework for the "industry or sector" will be common across the public sector and include requirements such as Managing Public Money, but specialised entities may be subject to other requirements.

Understanding the entity and its environment – industry factors

15.97 If the "industry" the entity is involved in gives rise to particular risks due to the nature of its operations or other factors, such as the use of significant accounting estimates in accounting for financial instruments, complex expected credit losses, biological assets, PPP/PFI transactions, etc., the engagement team should include members with appropriate skills, knowledge and experience.

Understanding the entity and its environment – regulatory factors

15.98 The NAO's audited entities are typically established under a particular legislative framework which, together with relevant accounting provisions, prescribes the form and content of the financial statements – this framework may include:

- the specific legislation that has established the audited entity and determines its activities;
- Accounts Directions;
- the Government Financial Reporting Manual and Managing Public Money;
- standards that constitute IFRS and/or UK GAAP;
- other HM Treasury guidance on the application of accounting standards, the Companies Acts and the disclosure of information;
- the Charities SORP; and
- the Pensions SORP.

15.99 Given its propensity to change each year, teams should consider whether there have been changes in the applicable legislative and regulatory framework. The entity's framework of authorities and (relevant) legislative framework should be clearly documented prior to the performance of any risk assessment procedures or audit work. Further guidance may be found in Chapter 11: Determining the framework of authorities and Chapter 31: Consideration of laws and regulations and reporting to regulators.

Understanding the entity and its environment – nature of the entity

15.100 Our understanding of the nature of the entity will include an understanding of its principal activities, the legislative background of the body, the extent of Parliamentary interest in the entity, and the way in which it is funded.

15.101 Other matters which may be considered include:

- the entity's income streams and the type of income allowable by Parliament;
- any partnerships or other arrangements for delivery of services;
- use of derivative financial instruments;
- extent of items required to be held at fair values; and
- unusual or complex transactions, in particular whether they are novel or contentious.

15.102 Significant changes from prior periods can affect the risk of material misstatement. Consideration should be given to whether changes in the nature of the entity and its activities may impact on the basis of accounting for particular balances.

15.103 The sections below give guidance on items it may be particularly relevant to understand in the context of the NAO's audited entities and additional examples are given in paragraphs A48 to A89 of ISA (UK) 315 (Revised July 2020), but neither is a required or comprehensive list of all items which may need to be considered for any particular audit.

15.104 "Tone from the top" can be considered by understanding the following:

- how integrity and ethical values are communicated and enforced;
- the entity's commitment to competence;
- the extent of participation of those charged with governance;
- management's philosophy and operating style (referring to paragraph A106 of ISA (UK) 315 (Revised July 2020));
- the organisational structure;
- how authority and responsibility in the organisation are assigned;
- human resource policies and practices (and their impact on organisational behaviours); and
- the additional considerations listed in paragraph 21(b) of ISA (UK) 315 (Revised July 2020).

Understanding the entity and its environment – objectives and strategies and related business risks

15.105 The objectives and risks of the NAO's audited entities are affected by their status as public bodies which are closely regulated, typically process a large volume of transactions, and whose reports are public. Factors to consider include whether:

- major new legislation or expenditure programmes have been introduced;
- there is the possibility of manipulation by management to achieve performance or other targets;
- an entity is likely to be wound up, reorganised, merged, sold or privatised;
- there is political pressure on an entity to complete transactions quickly; and
- the final form of account does not reflect the underlying management and accounting processes.

Understanding the entity and its environment – measurement and review of the entity's financial performance

15.106 Internal and external performance measures used to assess the entity and its management may motivate management to manipulate results. An understanding of how the entity's performance is measured and reviewed is therefore important in assessing the risk of material misstatement from fraud or error.

15.107 An understanding of the performance measures used internally by the entity could indicate risks of material misstatement where there are unexpected results or trends. In planning our preliminary analytical procedures it may be relevant to consider management's preferred performance measures.

Understanding the entity and its environment – the selection and application of accounting policies

15.108 The FReM specifies broad principles and policies so that entities that fall within its remit or a consolidation boundary use sufficiently uniform accounting policies for the purposes of Whole of Government Accounts. However, individual entities continue to have discretion in the specific application of policies so as to appropriately reflect their individual circumstances, such as in selection of useful economic lives.

15.109 Engagement teams should be alert to entities adopting novel or contentious accounting policies and determine whether they have consulted the relevant authorities if an audited entity has done so or is proposing to do so. FAPQ guidance may be sought as to the appropriateness of any such accounting policies.

15.110 If the audited entity is proposing to change accounting policies, the reasons for the change should be considered and in particular whether the new accounting policy is more appropriate than the original policy (as required by IAS 8). Retrospective adjustment for changes in accounting policy can impact upon the budgeting and estimates process. The FReM requires entities to consult prior to making retrospective changes to address this issue, and engagement teams should consider the impact of this upon the engagement as a whole and in particular any implications for our regularity work and the risk of breaching a total subject to Parliamentary or other control.

15.111 The engagement team should ensure that it understands the legal and regulatory requirements for statutory other information which is prepared alongside its financial statements. In the case of departments and executive agencies, such information would encompass the Performance Report and Accountability Report. In the case of companies, this information would include the Strategic Report and Directors' Report. The statutory other information for other entities will vary depending upon the basis of preparation of their annual report and accounts and the basis for the audit.

15.112 As stated in paragraph A10-3 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), information given in the statutory other information includes information that is included by way of cross reference to other information presented separately from the statutory other information.

Obtaining the draft annual report and accounts and underlying accounting records

15.113 As part of the process of gathering entity initial information, the engagement team should agree with the client (for example, through the client liaison schedule) to provide, at appropriate intervals agreed between the client and the engagement team:

- Copies of the General Ledger (GL) download and Trial Balance. These will be reconciled to each other and to the draft accounts as set out in Chapter 17: Risk assessment and response planning (section entitled 'Agreeing the financial statements to underlying records and examination of material journal entries').
- Copies of the draft financial statements, including accounts models and related working papers.
- Copies of the draft annual report.

Review and signoff

15.114 Once the procedures for under the Gather Entity Information Workflow Step have been completed, the Engagement Team-Leader or team member should submit these for review.

15.115 The Engagement Manager and then the Engagement Director should perform a two-stage review of the overall audit strategy in the Apex file.

Quality and reviewing guidance

15.116 The overall audit strategy guides the audit planning process. It is important to capture at this stage the Engagement Director's expectations and concerns for the audit so that the audit can be planned to address them.

15.117 As part of developing the overall audit strategy, the Engagement Director will have identified the required risk assessment procedures. The engagement team should ensure that they follow this planned approach, otherwise the planning process will not be effective and efficient.

15.118 In planning the audit, the engagement team should ensure that that all points identified in the overall audit strategy flow through to the planned approach. Where detailed audit planning provides additional information, such as information indicating that a possible risk identified in the overall audit strategy is not relevant in the current year, this should be recorded in the Apex audit file, clearly set out the basis for this conclusion and the supporting audit evidence.

Interaction with the system of quality management – planning

15.119 Chapter 4: Quality monitoring describes the NAO's system of quality management, which includes the monitoring and remediation process. Paragraph 39 of ISA (UK) 220 (Revised July 2021) requires that the Engagement Director takes responsibility for obtaining an understanding of the information from the NAO's monitoring and remediation process, as communicated by the NAO; determining the relevance and effect on the audit engagement of this information and taking appropriate action; and remaining alert throughout the audit engagement for information that may be relevant to the NAO's monitoring and remediation process and communicating such information to those responsible for the process.

15.120 The means by which the Engagement Director should obtain an understanding of information from the monitoring and remediation process is through reviewing relevant updates on the Sharepoint pages relating to the system of quality management. These updates will include actions specific to individual engagements arising from the Component Quality Risk Registers. The Engagement Director should consider, in the context of the specific engagement, how the matters noted apply and any appropriate actions to address such quality risks, taking into account the guidance provided on the page. At the planning stage, this review should be documented in Apex within the relevant Workflow Step Item within the Gather Entity Information Workflow Step.

15.121 The means by which the Engagement Director should communicate information that may be relevant to the NAO's monitoring and remediation process to those responsible for the process is through raising a Consultation within Apex and directing it to FAPQ. Such information will be passed to the individuals operationally responsible for the monitoring and remediation process through the forum of Component Quality Management meetings, as described in Chapter 4: Quality monitoring.

15.122 Where the engagement has been subject to internal or external quality review processes (including Peer and Cold Review, AQR or FAPQ Accounts Review) in the previous year and/or the year before where applicable, the engagement team collate the findings from these reviews in a single working paper and set out how the engagement team has plans to respond to the points raised. This should be documented within the Quality Review Findings template.

Chapter 16: Materiality, performance materiality and trivial threshold

Relevant standards and guidance

16.1 ISA (UK) 320 (Revised June 2016) (Updated May 2022) *Materiality in planning and performing an audit* sets out the auditor's responsibility to apply the concept of materiality in planning and performing an audit of financial statements.

16.2 Paragraphs 1-83 to 1-89 and Box 1 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* (Revised 2022) provide guidance on applying ISA (UK) 320 (Revised June 2016) (Updated May 2022) in the public sector.

16.3 Paragraphs 2-33 to 2-37 of Practice Note 10 (Revised 2022) provide guidance on applying the concept of materiality to the audit of regularity.

Setting materiality

16.4 ***Consultation required*** The Engagement Director determines a single materiality figure for the financial statements as a whole as part of the overall audit strategy. The normal range for materiality is 0.5% to 2% of gross expenditure/turnover or gross assets and 5% to 10% of surplus or profit. Where the Engagement Director wishes to set materiality outside of these ranges they must consult with FAPQ.

16.5 Materiality and performance materiality should be set taking into account the knowledge of the Engagement Director and Engagement Manager of the sensitivities of the users to values and disclosures in the accounts, considering qualitative factors.

16.6 Public bodies audited by the NAO are generally expenditure-driven, meaning gross expenditure is often the most appropriate benchmark for setting materiality. For audits of departmental financial statements, where expenditure is the selected benchmark, materiality should be set on the basis of gross expenditure presented in the Statement of Comprehensive Net Expenditure, rather than on Supply figures.

16.7 Engagement teams should also consider and clearly document their consideration of other benchmarks. In particular:

- for profit making companies engagement teams should document their consideration of using profit before tax as the materiality base;
- for profit making companies who have made a loss in year engagement teams should consider whether revenue or expenditure are more appropriate materiality bases; and
- for charities audits, teams should document their consideration of using incoming resources/ revenue as the materiality base.

16.8 Engagement teams should clearly document why other percentages were not selected when setting materiality.

16.9 In the event of becoming aware of information during the audit that would have affected the initial materiality determination, the engagement team should consider revising materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures).

16.10 In accordance with paragraph 13 of ISA (UK) 320 (Revised June 2016) (Updated May 2022), if a lower materiality than that initially determined is appropriate, the engagement team should determine whether it is necessary to revise performance materiality, and whether the nature, timing and extent of the further audit procedures remain appropriate, revisiting the Risk Assessment in Apex as necessary.

16.11 If one-off items give rise to an exceptional increase or decrease in a benchmark in the current period, it may be appropriate to use a normalised figure for the purposes of assessing materiality. Accordingly, the engagement team would normally consider current period, prior periods, and budget or forecast financial results and position in assessing materiality.

16.12 ***Consultation required*** Some audited entities may operate in volatile industries or where income and/ or expenditure fluctuates each year. Where engagement teams plan on basing the materiality benchmark on a rolling basis over a number of years to eliminate volatility they must consult FAPQ.

16.13 There is a relationship between the percentage and the chosen benchmark, such that a percentage applied to the surplus or deficit for the period will normally be higher than a percentage applied to total expenditure. For example, the engagement team may consider 5% of the surplus for the period to be appropriate for a trading fund, while the engagement team may consider 1% of total expenditure to be appropriate for a grant-giving body. Higher or lower percentages may be deemed appropriate in the circumstances and professional judgement should be applied: for example, a materiality set on expected surplus where the 'profit margin' is very high may require a lower percentage applied to the materiality base.

16.14 The ranges normally applied in the NAO are 0.5% to 2% of gross expenditure/turnover or gross assets and 5% to 10% of surplus or profit. This is summarised in ***Figure 16A*** below.

Figure 16A: Normal ranges of materiality for NAO audits

16.15 Engagement teams should consider the full range available to them and not just 0.5%, 1% or 2%: for example, thresholds of 0.9%, 1.8% etc. may be used.

16.16 Engagement teams of category C entities are expected to consider the top of the range (e.g. 2% of gross expenditure) as a starting point, given the expected low Parliamentary and public interest in these bodies.

16.17 The views and expectations of those charged with governance and management may be relevant to identifying particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements, and to determining the materiality level or levels to be applied to these.

16.18 In particular, for the majority of NAO-audited entities, specific considerations will include:

- the need for openness and transparency;
- public expectations and public interest; for example:
    - engagement teams for entities whose accounts are dominated by expenditure, such as grant-giving entities) may consider setting a materiality threshold for account balances in the Statement of Financial Position in which there is a more granular level of user interest, in addition to materiality for the financial statements as a whole based on expenditure;
    - conversely, for an audited entity whose accounts include high-value property, plant and equipment assets but whose day-to-day decision making focuses on much lower-value expenditure and income transaction streams, the engagement team may consider setting a materiality level to be applied to most or all expenditure and income transaction streams (plus, where relevant, assets or liabilities in respect of which management decisions are more frequently made than for the larger account balances, such as working capital balances or actively-managed investments), in addition to materiality for the financial statements as a whole based on the high-value assets; and
- the context in which a matter appears; for example, if the matter is also subject to compliance with authorities, legislation or regulations. For departments, this would include situations where voted control limits are exceeded. The C&AG qualifies his regularity opinion for all breaches of voted totals, regardless of the amount of excess.

16.19 While there will be an expectation that prior year figures will match exactly to the previous year's published accounts and that senior staff remuneration should be disclosed in the correct banding; certain balances, transactions or disclosures with lower materiality levels should not necessarily be 100% tested.

Setting performance materiality

16.20 The Engagement Director determines performance materiality which will be used for the purposes of assessing the risks of material misstatement and planning the nature, timing and extent of our audit procedures.

16.21 Performance materiality is determined at a value that reduces to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements.

16.22 As per paragraph A12 of ISA (UK) 320 (Revised June 2016) (Updated May 2022), the determination of performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. It is affected by the auditor's understanding of the entity, updated during the performance of the risk assessment procedures; and the nature and extent of misstatements identified in previous audits and thereby the auditor's expectations in relation to misstatements in the current period. When setting performance materiality, auditors should consider the level of prior year error, whether this is a new engagement and other matters raised in the FRC's Audit Quality Thematic Review on Materiality.

16.23 Further guidance is available in the materiality template to assist with determining an appropriate value for performance materiality, including for areas with a reduced materiality.

16.24 Performance materiality should not be set at a level higher than 75% of financial statement materiality.

16.25 For new engagements performance materiality should not be set at a level higher than 65% of financial statement materiality.

16.26 The performance materiality cap may be increased to 75% in the second year of an engagement. However, engagement teams must clearly document why an increase in the cap is appropriate.

16.27 A higher performance materiality is likely to reduce the planned scope of work, since the number of RoMMs scoped into the Risk Assessment in Apex reduces if the value associated with a Financial Reporting Activity or Financial Reporting Sub-Activity is less than performance materiality.

Setting materiality for regularity

16.28 Where a regularity opinion is provided, the Engagement Director determines materiality required for that opinion. This will commonly be the same as the materiality for the true and fair opinion, but not necessarily. Examples of situations when the engagement team may, depending on their professional judgement, determine a different materiality threshold for the audit of regularity from that for the financial statements as a whole include where:

- the audited entity makes payments to individuals or other bodies that are of significantly greater public interest than the administrative functions of the entity itself;
- the benchmark used to determine materiality for the financial statements as a whole has increased significantly (for example, due to an expansion of the audited entity's operations) but there remains user interest in the regularity of transactions at a more granular level;
- aspects of the audited entity's framework of authorities and/or regulatory oversight regime indicate that quantitatively small non-compliance with the framework of authorities would be perceived more seriously than would be apparent from assessing the amounts against materiality for the financial statements as a whole; or
- the benchmark used to determine materiality for the financial statements as a whole is based on assets or liabilities and these amounts are out of proportion to the expenditure and income transactions that are subject to the regularity opinion. It would be unusual to use an assets- or liabilities-based materiality benchmark for the regularity opinion, since the regularity opinion covers transactions recorded in the financial statements, rather than account balances.

16.29 Irregular transactions are not automatically material by their nature, and the risk of transactions being irregular should be considered in the same way as other qualitative considerations of materiality.

16.30 Where a regularity opinion is provided, the engagement team need to consider an overarching approach to auditing regularity rather than simply supplementing testing for the true and fair opinion.

16.31 Materiality is set for the financial statements as a whole for the purpose of the true and fair opinion. It is possible that the engagement team can have a different (often lower) threshold for the regularity opinion and engagement teams will need to consider whether this is necessary for their audit. This may be required when auditing a small entity (for example, to a materiality of 2% of expenditure for the true and fair opinion), but where there are some complexities relating to regularity and more testing on regularity is required in order to minimise the risk of undetected material irregularity, the engagement team may therefore decide to set regularity materiality in the region of 1% of expenditure, for example.

16.32 The discussion of qualitative considerations reflects the interaction of regularity considerations with materiality.

16.33 The engagement team need to be aware of the particular elements of the financial statements that may be of more interest to Parliament in terms of regularity, and consider what they would deem material for these, both at planning and when evaluating errors.

16.34 The Engagement Team's determination of materiality in relation to regularity should be undertaken from the perspective of the users of the financial statements. This determination is a matter of judgement and should consider both quantitative and qualitative considerations. This is because users of the financial statements might have an interest in breaches of authority even where the amounts involved may be small in relation to the financial statements as a whole.

16.35 This might mean that certain classes of transactions, accounts balances or disclosures need to be considered against a lower threshold than the materiality level. In particular, any expenditure incurred in excess of amounts authorised by Parliament is considered to be materially irregular as suggested by paragraph 2-35 of Practice Note 10 (Revised 2022). Further guidance on this may be found in Chapter 41: Parliamentary Supply.

16.36 Other areas of the financial statements that may be more sensitive, and require a lower threshold to drive higher levels of testing, from a regularity perspective could include:

- grant expenditure;
- senior staff remuneration;
- staff costs generally (pay remit, exit packages);
- related party transactions;
- areas of expenditure covered by spending controls;
- statutory fees/levies; and/or
- benefit expenditure.

16.37 The assessment of materiality is influenced by legislative and regulatory requirements and by the financial information needs of legislators and the public in relation to public sector programmes. As such, qualitative considerations are often more significant in the context of materiality for regularity. In particular, the engagement team should consider the nature of an irregularity when considering whether it is material to the financial statements.

16.38 Engagement teams may consider the following external and internal factors when determining whether an irregularity is qualitatively material.

External factors

16.39 External factors concern the extent to which the transaction is material from the perspective of the users of the accounts, and include the following:

- the principle that public bodies adhere to high levels of openness and transparency;
- the reasonable expectation that, on a balance of public interest assessment, separate disclosure is necessary;
- the context in which a matter appears;
- interest or sensitivity to the users of the accounts; and
- action taken by the entity to regularise the matter which gave rise to the irregularity.

Internal factors

16.40 Internal factors include the motivations of management in entering into the transactions, and the extent to which they were, or should have been, aware of their obligations. These are often the deciding factors with regard to whether a clear or qualified opinion is given, and include:

- the circumstances of, and reasons for, the action taken, and whether it appears to be a deliberate circumvention of the rules;
- the track record of management in relation to similar matters, any consultation by management with relevant regulatory or sponsoring bodies, and whether management tried to follow correct procedure; and

- whether the irregularity was attributable to administrative oversight or indicates potential concerns about governance and proper decision-making in the audited body.

16.41 The above lists are not exhaustive but provides some factors which engagement teams may consider when determining materiality in relation to regularity.

Materiality for particular classes of transactions, account balances or disclosures

16.42 In some circumstances (see examples in paragraph A11 of ISA (UK) 320 (Revised June 2016) (Updated May 2022)), there is one or more particular classes of transactions, account balances or disclosures (COTABDs) for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements. If this is the case, the Engagement Director determines the materiality level or levels to be applied to those particular COTABDs.

16.43 For public sector entities, this may include, for example, related party transactions.

16.44 If a materiality level is set for particular COTABDs for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements, the engagement team also determines performance materiality for those COTABDs. This is normally calculated by pro-rating performance materiality for the financial statements as a whole based on the proportional difference between materiality for the particular COTABD and materiality for the financial statements as a whole.

16.45 The effect of setting a materiality threshold to cover misstatements of lesser amounts in particular COTABDs is to drive more testing of such COTABDs than would otherwise be the case.

16.46 Where an entity is primarily intended to hold public assets, the interest of the users of the accounts are primarily in relation to the statement of financial position (or the performance statement), in which case it will be more appropriate to use a single materiality figure for the financial statements as whole without setting different thresholds for other items in the accounts.

16.47 By the nature of central government bodies' activities, the financial statements of many NAO-audited entities are disproportionately dominated by the performance statement relative to the statement of financial position, or vice versa. Where the engagement team chooses to apply the same financial statement materiality to the performance statement and statement of financial position in these circumstances (i.e. does not apply a reduced materiality to transaction streams or balances in the less significant statement), this will need to be justified in the documentation on the file. This documentation may make reference as appropriate to the guidance in Practice Note 10 (Revised 2022) on applying ISA (UK) 320 (Revised June 2016) (Updated May 2022) in the public sector, including the illustrative examples in Box 1 under paragraph 1-86. (Revised June 2016) in the public sector, including the illustrative examples in Box 1 under paragraph 1-86.

16.48 It should also be noted that the expectations and interests of users of central government financial statements will often be different from those of users of private sector financial statements, which will have an impact on the selection of materiality thresholds for different areas of the accounts.

Determining a maximum level for clearly trivial items

16.49 The level at which misstatements would be regarded as clearly trivial would normally be in the range 1-2% of materiality. The level selected is a matter of professional judgement.

16.50 The maximum level for items being assessed as clearly trivial should not be set higher than £300,000, as this threshold matches the reporting threshold in Managing Public Money.

16.51 ***Consultation required*** The £300,000 maximum level for the clearly trivial threshold does not apply for the Whole of Government Accounts and other financial statements with very large figures where an exception has been agreed with FAPQ. Where the audit team wishes to set a clearly trivial threshold in excess of £300,000 and there is no existing agreed exemption from the cap, they should consult FAPQ. An exemption is likely to be approved in cases where all of the following apply:

- the entity reports in to the nearest £1m (or higher);
- the framework of authorities does not require the entity to comply with *Managing Public Money* (the driver of the £300,000 value); and
- the chosen trivial threshold is less than 2% of materiality.

Other considerations

16.52 Materiality and performance materiality must be determined for both the group and the parent. See Chapter 25: Group audit procedures for further guidance.

16.53 Materiality should be communicated to those charged with governance.

16.54 The engagement team must document on the Apex file the values used for, and the factors considered in determining:

- materiality for the financial statements as a whole;
- if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures;
- the clearly trivial threshold;
- performance materiality; and
- any revision of the above as the audit progresses.

16.55 Materiality is a matter of professional judgement, and is affected by the perceived needs of the users of the financial statements. In considering the financial information needs of users, the engagement team can assume that users:

- have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;
- understand that financial statements are prepared, presented and audited to levels of materiality;
- recognise the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and the consideration of future events; and
- make reasonable economic decisions on the basis of the information in the financial statements.

16.56 For most NAO-audited entities, Parliament and regulators are often the primary users of the financial statements. The financial statements may be used to inform decisions other than economic decisions. The determination of materiality for the financial statements of a public sector body (and, if applicable, materiality level or levels for particular classes of transactions, account balances or disclosures) is therefore influenced by law, regulation or other authority, and by the financial information needs of Parliament and the public in relation to public sector programmes. However, the assessment of materiality remains the NAO's and is not dictated directly by any explicit or implicit interest expressed by any individual, group or entity with an interest in the financial statements.

16.57 Engagement team members should be alert throughout the risk assessment procedures and audit work to indications that one or more class of transactions, account balance or disclosure may be qualitatively material.

16.58 The auditor's determination in the planning process of the tolerable level of error i.e. the level of misstatements which would be considered material, provides a basis for:

- determining the nature, timing and extent of risk assessment procedures;
- identifying and assessing the risks of material misstatement; and
- determining the nature, timing and extent of further audit procedures.

16.59 When the engagement team evaluates the uncorrected misstatements, it is possible that misstatements individually or in aggregate below materiality will be assessed as material to the financial statements on qualitative grounds or are indicative of the possibility of other misstatements. Accordingly, when evaluating misstatements, the engagement team evaluate the size, nature (systematic, isolated) and cause of misstatements.

Qualitative considerations for materiality

16.60 Qualitative factors can reduce the tolerable level of misstatement in relation to particular classes of transactions, account balances and disclosures due to either:

- the nature of the errors or irregular transactions; or
- their context in financial statements rather than just the value of the misstatement.

16.61 The first bullet point above is concerned with the inherent characteristics of a balance or group of balances rather than just their value, and how sensitive they are for the users of the accounts. Where the nature of particular account areas makes them more sensitive, the engagement team should set a lower materiality for the work performed on these balances.

16.62 The Engagement Director and Engagement Manager identify such balances at the planning stage to determine the level of accuracy that they believe the users of the financial statements reasonably expect and design audit procedures accordingly.

16.63 Particular disclosure requirements maydemand a higher degree of accuracy than would normally be expected, so that misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements. Examples of these include:

- prior year figures; and/or
- specific legal settlements or amounts which should be agreed to other accounts.

16.64 There may be other matters that are of such importance to Parliament that they will be interested in errors or omissions that may be significantly below our quantitative assessment of materiality. It is not possible to provide a comprehensive list of matters that are likely to be more sensitive as a result of Parliamentary interest, as these will vary from between audited entities. Levels of interest in non-financial audit work, or in other sources of assurance, will be helpful in identifying areas that may attract higher Parliamentary interest. More sensitive areas could arise in connection with the regularity opinion as the opinion exists because of particular parliamentary concerns. Despite this the engagement team should not automatically assume that "regularity" errors are material and should consider each case on its merits.

16.65 At the planning stage an assessment should be made about misstatements or irregularities that are more sensitive to the users of the accounts. The Engagement Director should establish a lower level of materiality and performance materiality for each of the areas of the financial statements affected.

16.66 Taking account of context is concerned with misstatements or omissions that may be important because they change the impression given by the accounts to the users. Examples include misstatements which are immaterial by value but if corrected will:

- turn a surplus into a deficit;
- mean the organisation fails to meet one of its performance targets;
- affect the level of performance payments being made to senior staff;
- mean the organisation exceeding disclosure limit/ threshold and therefore require additional disclosure for certain activities or figures in the accounts; and/or
- for a departmental account, mean expenditure exceeds voted control totals.

16.67 The review of the basis of budgets, forecasts and estimates, etc. undertaken at the planning stage of the audit may help the engagement team identify whether there are certain balances where errors are more likely to be material by context. The Engagement Director should establish a lower level of materiality and performance materiality for each of the account areas affected.

16.68 It is not practicable to design audit procedures to detect misstatements that could be material solely because of their qualitative aspects. Engagement teams should, however, consider not only the size but also the nature of uncorrected misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements.

Re-assessing materiality during the course of the audit

16.69 Materiality should be continuously considered during the engagement. If events or circumstances exist where it may be appropriate to revise materiality, the engagement team should consider doing so at the earliest possible opportunity, for example, following a machinery of government change. Any changes to materiality should be approved by the Engagement Manager and the Engagement Director.

16.70 The engagement team should re-assess materiality upon receipt of the first draft financial statements, to ensure that the planned testing approach remains appropriate in light of the disclosures in the draft financial statements. This is particularly relevant where there have been significant movements in the financial statements from the prior year or budget, where new transactions, accounts balances or disclosures may require a deeper focus. Any changes to materiality and performance materiality at this stage should be approved by the Engagement Manager and the Engagement Director.

16.71 A re-assessment of materiality should be undertaken prior to certification. This will ensure that the level of materiality adopted for the audit remains appropriate in light of the disclosures in the final financial statements. If any changes to materiality are required at this stage, this should be approved by the Engagement Manager and Engagement Director and consideration given as to whether additional procedures are required to provide the necessary assurance.

Chapter 17: Risk assessment and response planning

Relevant standards and guidance

17.1 ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards on Auditing (UK)* deals with the independent auditor's overall responsibilities when conducting an audit of financial statements in accordance with ISAs (UK), including the overall objectives of the independent auditor and the nature and scope of an audit designed to enable the independent auditor to meet those objectives.

17.2 ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deals with the specific responsibilities of the auditor regarding quality management for an audit of financial statements. Quality management activities at the planning stage include:

- ensuring compliance with relevant ethical requirements;
- acceptance and continuance of client relationships and audit engagements;
- assignment of engagement teams with appropriate competence and capabilities;
- the direction, supervision, performance, documentation and review of planning activities;
- consultation on the audit plan, where relevant; and
- the appointment of, and initial discussions with, an Engagement Quality Reviewer, if applicable.

17.3 ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* deals with the auditor's responsibility to prepare audit documentation for an audit of financial statements. This includes documentation of significant matters and related professional judgements which, at the planning stage (but also in the later stages of the audit), includes matters that give rise to significant risks (as defined in ISA (UK) 315 (Revised July 2020)).

17.4 ISA (UK) 240 (Revised June 2016) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* deals with the auditor's responsibilities relating to fraud in an audit of financial statements, which include (at the planning stage):, which include (at the planning stage):

- identifying and assessing the risks of material misstatement of the financial statements due to fraud;
- designing and implementing appropriate responses to the assessed risks; and
- recognising the risk of fraud through management override of controls as a significant risk.

17.5 Paragraphs 1-38 to 1-51 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 240 (Revised June 2016) (Updated May 2022) in the public sector.

17.6 ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance* deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements, which includes (at the planning stage), which includes (at the planning stage):

- the auditor's responsibilities in relation to the financial statement audit;
- an overview of the planned scope and timing of the audit and the significant risks identified by the auditor;
- other matters for entities that report on application of the UK Corporate Governance Code and for Public Interest Entities; and
- matters relating to auditor independence.

17.7 Paragraphs 1-61 to 1-71 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 260 (Revised November 2019) (Updated May 2022) in the public sector.

17.8 ISA (UK) 300 (Revised June 2016) (Updated May 2022) *Planning an audit of financial statements* deals with the auditor's responsibility to plan an audit of financial statements. The objective of the auditor under ISA (UK) 300 (Revised June 2016) (Updated May 2022) is to plan the audit so that it will be performed in an effective manner.

17.9 ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements.

17.10 Paragraphs 1-72 to 1-82 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 315 (Revised July 2020) in the public sector.

17.11 ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks* deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with ISA (UK) 315 (Revised July 2020) in an audit of financial statements. The objective of the auditor under ISA (UK) 330 (Revised July 2017) (Updated May 2022) is to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement, through designing and implementing appropriate responses to those risks.

17.12 Paragraphs 13-17 and A19-A80 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures* include requirements relating to risk assessment procedures for accounting estimates and identifying and assessing the risks of material misstatement relevant to accounting estimates.

17.13 Paragraphs 1-108 to 1-115 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 540 (Revised December 2018) (Updated May 2022) in the public sector.

17.14 ISQM (UK) 2 (Updated May 2023) *Engagement quality reviews* provides guidance on the responsibilities of the Engagement Quality Reviewer at the planning stage.

Summary of workflow at the planning stage

17.15 At the planning stage, the auditor gathers information on the entity, makes an assessment of materiality and uses the Risk Assessment in Apex to assess the risks of material misstatement (RoMMs) and the controls covering these. The auditor then selects appropriate controls and substantive responses to the identified risks.

17.16 The engagement team should use the lead schedule to evidence a trail between initial audit work and the final account, including documentation of how adjustments have been audited.

17.17 The Engagement Director should document their review of the accounts.

17.18 ***Figure 17A*** below summarises the risk assessment and response planning process that should be undertaken for NAO financial audit engagements.

Figure 17A: Summary of risk assessment and response planning process for financial audit engagements

Key policy choices used by the NAO in applying ISAs (UK) when planning the audit

17.19 In line with ISA (UK) 315 (Revised July 2020), the NAO's assurance model is structured around risks of material misstatement (RoMMs) and, for the audit of regularity, risks of material irregular transactions.

17.20 ISAs (UK) do not prescribe an approach to building up audit assurance and it is permissible to use either a quantitative or a qualitative approach. The NAO's assurance model uses a qualitative rather than a quantitative model.

17.21 The documentation requirements for planning activities as set out in ISAs (UK) are satisfied by using the workflow built into the Risk Assessment in Apex.

17.22 A Content Library has been developed and integrated into the Risk Assessment in Apex which is a reasonably comprehensive list of RoMMs, responses and Inherent Risk Factors (IRFs) that may arise in NAO audited entities, but NAO engagement teams may identify additional RoMMs when applying ISAs, including ISA (UK) 315 (Revised July 2020). Where additional content is required, teams should raise this through the Financial Audit Support Tool (FAST).

17.23 ***Table 17B*** below sets out the key areas at the planning stage where the NAO has made policy decisions in how to apply specific requirements of ISAs (UK).

Table 17B: Key policy choices used by the NAO in applying ISAs (UK) when planning an audit of financial statements

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
ISA (UK) 240 (Revised May 2021) (Updated May 2022)	26 47 A28-A30	When identifying and assessing the risks of material misstatement due to fraud, the auditor shall, based on a presumption that there are risks of fraud in revenue recognition, evaluate which types of revenue, revenue transactions or assertions give rise to such risks. Specific documentation is required to justify rebutting the presumed risk.	**Presumed significant risk of fraud in revenue recognition** The presumed significant risk of fraud in revenue recognition is rebuttable. Engagement teams should consider the nature of revenue and management's incentives and opportunity to manipulate revenue. This evaluation should be undertaken without reference to the impact and effect of any controls which have been put in place by management to mitigate the risk. If the risk is rebutted, the basis for this should be clearly documented in the audit file. The engagement team should discuss the risk of fraud in revenue recognition as part of the engagement team discussion on fraud as described in Chapter 30: Fraud Responsibilities. Where the engagement team is not able to rebut the risk of fraud in revenue recognition, they should ensure that the outcome of this discussion is appropriately reflected within the Risk Assessment in Apex as set out in the Engagement Team Discussion on Fraud template.
ISA (UK) 240 (Revised May 2021) (Updated May 2022)	31-33	The auditor recognises a significant risk relating to fraud through management override of controls. The auditor designs and performs specified audit procedures in response to this significant risk The auditor determines whether additional procedures are needed to address specific additional risks of management override.	**Mandatory significant risk of fraud through management override of controls** The Risk Assessment in Apex has been designed to place the RoMM for fraud through management override of controls in the High position for both Likelihood and Financial Statement Impact (magnitude) on the spectrum of inherent risk – this drives the assessment of this RoMM as a mandatory significant risk. The workflow enables the auditor to select responses to this risk consisting of the required procedures and others in response to additional management override risks. The workflow additionally involves consideration of the risk of management override of control in the context of each Assertion-level RoMM, as each Financial Statements-level RoMM is treated as an Inherent Risk Factor (IRF) for each identified Assertion-level RoMM for the Financial Reporting Activities (FRAs)

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			which the auditor determines are impacted by the financial statements level RoMM.
ISA (UK) 300 (Revised June 2016) (Updated May 2022)	10	The auditor shall update and change the overall audit strategy and the audit plan as necessary during the course of the audit.	**Continuous risk assessment** Documentation of the planning meeting reflects a point in time risk assessment and audit plan. Updates to the risk assessment and audit plan during the course of the audit should be documented in the Audit Risk and Approach Audit Response within the Continuous Risk Assessment Audit Response Group and in the final output of the Risk Assessment in Apex, which must be retained on the file. As part of the continuous risk assessment process, the risk assessment should be re-considered and confirmed by the Engagement Director prior to certification. Further guidance may be found in Chapter 19: Continuous risk assessment.
ISA (UK) 315 (Revised July 2020)	37 A236	If the auditor obtains new information which is inconsistent with the audit evidence on which the auditor originally based the identification or assessments of the risks of material misstatement, the auditor shall revise the identification or assessment.	
ISA (UK) 315 (Revised July 2020)	26(a) and 26(d)	The auditor must evaluate the design and implementation of specified types of control.	**Evaluating the design and implementation of controls** The NAO interprets these paragraphs as requiring the auditor to evaluate the design and implementation of the following controls: • Controls that address a RoMM that has either one or both of a final Financial Statement Impact (magnitude) placement or a final Likelihood placement of High (i.e., effectively, the initial assessment of the RoMM will end up in an inherent risk position of a rebuttable significant risk or higher). • Controls that address significant risks relating to regularity. • Controls surrounding journal entries. • Controls relating to the reconciliation of the trial balance to the general ledger. • Complementary user entity controls where controls assurance is being obtained from controls operated by a service organisation. • Controls which the auditor plans to test the operating effectiveness of in order to obtain controls assurance.

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			NAO engagement teams may also evaluate the design and implementation of other controls when they consider it beneficial to do so (for example, in circumstances where they are preparing to take a controls-based audit approach in a year or two and the D&I work will form part of the preparation for this).
ISA (UK) 315 (Revised July 2020)	26(b)	Based on controls identified in paragraph 26(a), the auditor shall identify the IT applications and the other aspects of the entity's IT environment that are subject to risks arising from the use of IT.	**Identifying the IT applications and the other aspects of the entity's IT environment that are subject to risks arising from the use of IT** The Information System Complexity Assessor and Information Flows completed within the Understanding the Entity's Information Systems and Control Activity Components form will ensure that the relevant IT applications and aspects of the IT environment that are subject to risks arising from IT are appropriately identified. The Information Flows Documentation Workflow Step and the Understanding the Entity's Information Systems and Control Activity Components template mandate the auditor to complete this for all significant COTABDs.
ISA (UK) 315 (Revised July 2020)	26(c)	For such IT applications and other aspects of the IT environment identified in paragraph 26(b), the auditor shall identify the related risks arising from the use of IT and the entity's general IT controls that address such risks;	**Identifying the risks arising from the use of IT and the entity's general IT controls that address such risks** IT-dependent controls are defined as automated, semi-automated or IT dependent manual controls where the IT system is relied upon for their effective operation. The 'Design' tab of the Understanding the Entity's Information Systems and Control Activity Components form provides an initial filter to identify IT-dependent controls. The auditor then performs an initial risk assessment as to whether IT dependent controls are subject to risks from IT based upon the outcome of the Information Systems Complexity Assessor and an initial high-level assessment of access and change controls. ***Consultation required*** Where the outcome of this assessment in relation to an IT-dependent control is assessed as anything other than 'No consultation required', as defined in ***Table 17F*** below, the engagement team should consult

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			the Digital Financial Audit team, as prompted by the template, who will then discuss with the engagement team and identify any risks arising from the use of the IT and general IT controls which address such risks. Further guidance on the factors determining when engagement teams should consult with IT audit specialists is provided in the section later in this Chapter entitled 'Consultation with IT audit specialists.
ISA (UK) 315 (Revised July 2020)	30	The auditor shall assess identified financial statements-level RoMMs; determine whether such RoMMs affect the assessment of assertion-level RoMMs; and evaluate the nature and extent of their pervasive effect on the financial statements.	**Using the same model for responding to Financial Statements-level RoMMs as that for Assertion-level RoMMs** The auditor identifies and responds to Financial Statements-level RoMMs using the same model as that employed for Assertion-level RoMMs, but RoMMs will not be linked to classes of transactions, account balances or disclosures (COTABDs) within the audit workflow.
ISA (UK) 315 (Revised July 2020)	31	For identified assertion-level RoMMs, the auditor shall assess inherent risk by assessing the likelihood and magnitude of misstatement.	**Assessing the inherent risk associated with a RoMM** The auditor identifies which Inherent Risk Factors (IRFs) are present for the audited entity and records this in the Risk Assessment in Apex. Each IRF within the Risk Assessment in Apex additionally has an associated weighting according to its significance, which can be amended by the auditor – the engagement team should document in the Risk Assessment in Apex any deviations from these suggested weightings. Based on the Inherent Risk Factors identified as being relevant to the audited entity and their weightings, the Risk Assessment in Apex provides the auditor with a suggested Likelihood placement (either Low, Medium or High) on the spectrum of inherent risk. This suggestion is made using the methodology set out below under the heading 'Calculating a RoMM's Likelihood placement on the spectrum of inherent risk'. The auditor either accepts or amends the Likelihood placement suggested by the Risk Assessment in Apex – the auditor must document their justification of any

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			decision to amend the suggested Likelihood placement by adding an appropriate comment within the Risk Assessment in Apex. The auditor also makes a manual assessment of the Financial Statement Impact (magnitude) placement as either Low, Medium or High and should document within the Risk Assessment in Apex the justification for this assessment. In doing so, the auditor should follow the requirements set out below under the heading 'Determining a RoMM's Financial Statement Impact (magnitude) placement on the spectrum of inherent risk'. Together the assessed Likelihood and Financial Statement Impact levels determine the RoMM's placement on the spectrum of inherent risk, as shown in ***Figure 17D*** later in this Chapter. **Calculating a RoMM's Likelihood placement on the spectrum of inherent risk** Depending on the type of RoMM, the Risk Assessment in Apex uses one of two methods to calculate the Likelihood placement: the Highest IRF Method and the Additive Method, which are described below. Highest IRF Method: Used for all RoMMs except those that use the Additive Method: • A default weighting of Low/Medium/High is applied to all IRFs within the Content Library, which the auditor is able to vary with justification. • The Likelihood score for each RoMM is calculated based upon the highest-weighted IRF that is mapped to the RoMM (for example, if a RoMM has 2 'high' weighted IRFs, 5 'medium' and 3 'low', the RoMM has a High Likelihood as this is the highest-weighted IRF relevant to the RoMM). Additive Method: Used for particular RoMMs associated with property valuation; defined benefit pension liabilities; financial instruments; and accounting estimates;

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			• A default weighting of Low/Medium/High is applied to all IRFs within the Content Library, which the auditor is able to vary with justification. • A Likelihood placement of High will be suggested for any RoMM with an associated IRF that has a weighting of High. A numerical value is then assigned to each of the weightings of non-High IRFs: Low=1 and Medium=2. The weighted scores for the IRFs mapped to each RoMM are summed to give a total score for the RoMM. For example, a RoMM with two Low IRFs and five Medium IRFs scores (2x1)+(5x2)=12. • The Likelihood placement for each RoMM is determined by its score compared to defined thresholds between Low, Medium and High. For example, if a RoMM scores 15 and its thresholds are [Low<10<Medium<20<High], the Likelihood placement for that RoMM is Medium. • The thresholds are determined individually on a RoMM-by-RoMM basis by central content developers, based on the particular characteristics of each RoMM and the IRFs which have been mapped against each RoMM. The starting point of this determination – subject to the individual assessment of the characteristics of each RoMM and IRF – is that one or more Medium IRFs leads to a Medium Likelihood placement and three or more Medium IRFs leads to a High Likelihood placement. However, this has been determined on a RoMM-by-RoMM basis based upon the bespoke and estimates IRFs mapped to the RoMM. The presence of any Generic Inherent Risk Factors (GIRFs) or any IRFs relating to fraud against the RoMM will further increase the level of risk, in proportion to the weighting of the GIRF or fraud-related IRF. Where the engagement team considers that, in relation to a scoped-in estimates-related RoMM, there is no reasonable possibility of material misstatement due to the values involved, they should revisit the estimates scoping question at the FRSA level within the Risk Assessment in Apex and, if appropriate, amend the response to this to confirm that there is no reasonable possibility that a material misstatement could occur in the estimate, which will result in the accounting

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			estimate being scoped out of the Risk Assessment (see section later in this Chapter entitled 'Scoping the audit – Financial Reporting Activities (FRAs) and COTABDs'). . **Determining a RoMM's Financial Statement Impact (magnitude) placement on the spectrum of inherent risk** The assessment of a RoMM's Financial Statement Impact (magnitude) is a matter of auditor judgement and should be a holistic assessment based upon consideration of all of the following factors: • the nature of the population affected by the RoMM; • what a potential misstatement could be; and • a comparison of the overall population of the RoMM with materiality. The engagement team should carry out the following five steps to determine each RoMM's Financial Statement Impact (magnitude) placement on the spectrum of inherent risk and document this process within the Risk Assessment in Apex: 1. Identify the population affected by the RoMM. Whilst this may often be the same as the scoping source used for the relevant Financial Reporting Sub-Activity (FRSA), it may also be specific to the RoMM concerned (for example bonus payments within payroll costs). 2. Consider the value of the population against materiality. The engagement team should bear in mind the general principle that the larger the population, the greater the impact of any misstatements identified. Whilst the assessment of impact is a matter of auditor judgement, the following principles should be considered when making a judgement of impact of the RoMM against the value of the affected population:

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			• The RoMM has at least Medium Financial Statement Impact (magnitude) where the population affected by the RoMM is greater than or equal to 5 times materiality. • The RoMM has High Financial Statement Impact (magnitude) where the population affected by the RoMM is greater than or equal to 20 times materiality. If there are specific factors to consider for the RoMM being assessed relating to any of steps (3) to (5) below, the engagement team consider amending the RoMM's Financial Statement Impact (magnitude) placement. If there are no specific matters to note for the RoMM against these considerations, the engagement team should determine the RoMM's Financial Statement Impact (magnitude) placement based on the value of the population affected by the RoMM compared to materiality. 3. Consider the nature and characteristics of the population affected by the RoMM. Factors to consider include whether: • the population consists of a large number of low value items, where a greater number of misstatements would be required for there to be a material impact; or • the population consists of a smaller number of highly material items, where a single misstatement could be material. 4. Consider what would be the implications for the financial statements of a misstatement, including: • how a potential misstatement would impact on the population; • which COTABDs a misstatement would affect; • how material a misstatement could be in relation to the nature of the population assessed in step (3) above; and • whether a misstatement would represent the whole of the item or just a part.

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			5. The engagement team should undertake a holistic assessment of the impact of a RoMM considering all of the above factors. Whilst it is likely that a consideration of the materiality of the population affected by the RoMM is likely to be the key factor in most cases, other factors may be helpful to consider in arriving at a more nuanced assessment of the impact of a RoMM. As an exception to the above process, RoMMs associated with Related Party Transactions must have at least a Medium Financial Statement Impact (magnitude) placement, but the engagement team may assign these a High Financial Statement Impact (magnitude) placement if appropriate. Justifications for all impact assessments must be made in the relevant field within the Risk Assessment in Apex. Guidance is provided to the Financial Audit Service Line to assist engagement teams in making these judgements in a consistent manner. The auditor may depart from this guidance with appropriate justification, which must be documented in the Risk Assessment in Apex.
ISA (UK) 315 (Revised July 2020)	31(b) A215-A216	When assessing the likelihood and magnitude of misstatement for assertion-level RoMMs, the auditor takes into account how financial statements-level RoMMs affect the assessment of inherent risk for each assertion-level RoMM.	**Impact of Financial Statements-level RoMMs on Assertion-level RoMMs** For each Financial Statements-level RoMM, the auditor selects the Financial Reporting Activities (FRAs) which may be impacted by that FS-level RoMM. Each of the selected FRAs will have a number of Assertion-level RoMMs attached to the FRA. The FS-level RoMM in question is treated as an Inherent Risk Factor (IRF) for all Assertion-level RoMMs that are attached to the selected FRAs. These IRFs are then treated as any other IRF for the purpose of assessing the inherent risk of those Assertion-level RoMMs.
ISA (UK) 315 (Revised July 2020)	32 12(l)	The auditor shall determine whether any of the assessed risks of material misstatement are significant risks.	**Identification of significant risks**

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			For the purpose of identifying a significant risk, the assessment of inherent risk for a RoMM is considered to be close to the upper end of the spectrum of inherent risk (due to the degree to which Inherent Risk Factors affect the combination of the likelihood of a misstatement occurring and the magnitude of the potential misstatement should that misstatement occur) in the following circumstances: • Where both Likelihood and Financial Statement Impact (magnitude) are rated as High. • Where one of Likelihood and Financial Statement Impact (magnitude) is High and the other factor is Medium. Additionally, there is a rebuttable presumption of a significant risk in the following circumstances: • Where one of Likelihood and Financial Statement Impact (magnitude) is High and the other factor is Low. Where ISA (UK) 315 (Revised July 2020) leads to the identification of a rebuttable presumed significant risk, for the purpose of the workflow in the Risk Assessment in Apex, the RoMM in question is initially labelled as a significant risk. The stand-back assessment then allows the auditor to rebut the presumed significant risk, subject to a robust justification.
ISA (UK) 315 (Revised July 2020)	35 A230-A232	The auditor evaluates whether the audit evidence obtained from the risk assessment procedures provides an appropriate basis for the identification and assessment of RoMMs, taking into account both corroborative and contradictory evidence, and performs additional risk assessment procedures if required.	**Stand-back assessment (identification of RoMMs)** The stand-back requirement within ISA (UK) 315 (Revised July 2020) is interpreted to cover consideration of the identification of RoMMs and initial placement of the RoMM on the spectrum of inherent risk. The workflow allows the engagement team to apply their judgement to make changes to the following whilst performing the stand-back assessment: • the output of the risk assessment process, particularly the identification of RoMMs relevant to the audit and where the RoMM is positioned on the spectrum of inherent risk; • the planned approach to addressing the RoMMs; and

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			• the planned testing approach when considered against COTABDs. Where judgement is applied by the auditor to deviate away from the default output of the risk assessment process (such as the placements on the spectrum of inherent risk suggested by the Risk Assessment in Apex), this will need to be approved by the Engagement Director and clearly flagged and documented on the audit file. The audit workflow requires the Engagement Director to review the output of audit procedures at the end of the risk assessment process in order to consider whether it is proportionate to the risks inherent within the audited entity. The audit workflow includes a procedure step for the Engagement Director to qualitatively and quantitatively assess whether sufficient assurance has been obtained to support the C&AG's audit opinion during the course of the audit. This consideration must be undertaken prior to submission of the certification journal to Private Office. Further guidance is provided in the section later in this Chapter entitled 'Stand-back assessment'.
ISA (UK) 315 (Revised July 2020)	36	For material COTABDs that have not been determined to be significant COTABDs, the auditor shall evaluate whether the auditor's determination remains appropriate.	**Stand-back assessment (appropriateness of determination of material COTABDs as non-significant)** In the NAO's audit methodology, significant COTABDs are identified as COTABDs which are affected by any RoMM which is placed in the Low, Medium or High position on the spectrum of inherent risk (i.e., the RoMM is not in the Target position). The evaluation required by paragraph 36 of ISA (UK) 315 (Revised July 2020) is carried out within the OAS Standback Memo template, with reference to analysis screens provided within the Risk Assessment in Apex, which the Engagement Director should review.

ISA (UK)	Paragraph	Summary of requirements of the standard	NAO policies
			Further guidance is provided in the section later in this Chapter entitled 'Stand-back assessment'.
ISA (UK) 330 (Revised July 2017) (Updated May 2022)	18	Irrespective of the assessed RoMMs, the auditor shall design and perform substantive procedures for each material COTABD.	**Material non-significant COTABDs** The workflow identifies any COTABDs where further (minimum) substantive procedures are required. The engagement team must carry out one of the following actions where they identify a material non-significant COTABD for which there are currently no substantive procedures planned: either: • amend the risk assessment and planned responses to ensure a substantive procedure is included for the material non-significant COTABD; or • add a minimum substantive procedure for that COTABD into the relevant Audit Response Group in Apex.

Defined terms

17.24 ***Table 17C*** below provides definitions of specific terms that are used in the NAO's assurance model, some of which are also defined in ISAs (UK). Terms used within these definitions that are themselves defined elsewhere in the table are given in bold. Other terms are defined in the NAO Business Glossary.

Table 17C: Defined terms

Term	Definition
Assertions	Representations, explicit or otherwise, with respect to the recognition, measurement, presentation and disclosure of information in the financial statements which are inherent in management representing that the financial statements are prepared in accordance with the applicable financial reporting framework. Assertions are used by the auditor to consider the different types of potential misstatements that may occur when identifying, assessing and responding to the risks of material misstatement. Categories of assertions are listed in paragraph A190 of ISA (UK) 315 (Revised July 2020).
Class of Transactions, Account Balance or Disclosure (COTABD)	A grouping of one or more Financial Statement Account Balances and/or Financial Statement Transactions and/or Financial Statement Disclosures which share a similar inherent risk profile for a given set of potential **Risks of Material Misstatement**.
Significant Class of Transactions, Account Balance or Disclosure (SCOTABDs) Defined in paragraph 12(l) of ISA (UK) 315 (Revised July 2020)	A **COTABD** for which there is one or more relevant assertions. An assertion about a **COTABD** is relevant when it has an identified **Risk of Material Misstatement (RoMM)**. A **COTABD** is considered to be significant where it has been scoped in within the Risk Assessment in Apex, and any of the **RoMMs** associated with the **COTABD** have been assessed as having 'low', 'medium' or 'high' inherent risk. A **COTABD** will also be considered to be significant in the circumstances where a completeness **RoMM** affecting the **COTABD** has been assessed as having 'low', 'medium' or 'high' inherent risk.

Control risk Defined in paragraph 4 of ISA (UK) 315 (Revised July 2020)	The risk that a misstatement that could occur in an **assertion** about a **COTABD** and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the audited entity's internal controls.
Financial Reporting Activity (FRA)	A grouping of **Financial Reporting Sub-Activities** which share a common scoping denominator, which will allow audit teams to determine whether the entire subset of **Financial Reporting Sub-Activities** are relevant to the audit (i.e. may contain potential **Risks of Material Misstatement**) or not.
Financial Reporting Business Process	A type of Business Process that an audited entity undertakes as a set of steps from the initiation of an Accounting Event or a Business Transaction, to the recording of an Accounting Transaction.
Financial Reporting Requirement	A part of an Accounting Standard that specifies how the accounting or reporting of an Accounting Transaction and/or a Financial Statement Disclosure should be recorded and presented in the financial statements.
Financial Reporting Sub-Activity (FRSA)	A grouping of one or more **COTABDs,** or a distinct activity required to account for those COTABDs, that share the same set of potential **Risks of Material Misstatement** based on a set of **Financial Reporting Business Processes** and/or **Financial Reporting Requirements**.
Financial Statement Risk Area (FSRA)	A group of potential risks which would impact across the Financial Statements of an Audited Entity based on a common set of **Financial Reporting Requirements**, **Financial Statement Business Process(es)** and/or one or more Legislative Bases.
Financial Statement Risk Sub-Area (FSRSA)	A fine-grained area of potential risk which could impact across the Financial Statements of an Audited Entity.
Generic Inherent Risk Factor (GIRF)	A financial statements-level **Inherent Risk Factor** derived from the auditing standards or pervasive across the auditing methodology of the NAO.

Inherent risk Defined in paragraph 4 of ISA (UK) 315 (Revised July 2020)	The susceptibility of an **assertion** about a **COTABD** to a misstatement that could be material, either individually or when aggregated with other misstatements, before consideration of any related controls.
Inherent Risk Factor (IRF) Defined in paragraph 12(f) of ISA (UK) 315 (Revised July 2020)	A characteristic of an event or condition that affects susceptibility to misstatement, whether due to fraud or error, of an assertion about a **COTABD**, before consideration of controls. Such factors may be qualitative or quantitative, and include complexity, subjectivity, change, uncertainty or susceptibility to misstatement due to management bias or other fraud risk factors insofar as they affect **inherent risk**.
Relevant assertion	An **assertion** about a **COTABD** is relevant when it has an identified **RoMM**. The determination of whether an **assertion** is a relevant assertion is made before consideration of any related controls (i.e., the **inherent risk**). Within the NAO's methodology, when the auditor identifies a **RoMM** as part of the Risk Assessment in Apex, they also identify the relevant assertions as comprising the **assertions** to which that **RoMM** is mapped within the Content Library.
Risk of Material Misstatement (RoMM) Defined in paragraph 13(n) of ISA (UK) 200 (Revised June 2016) (Updated May 2022)	The risk that the financial statements are materially misstated prior to audit. This consists of two components, at the assertion level: • **Inherent risk** • **Control risk**

Scoping the audit

17.25 The engagement team should carry out the initial scoping of the audit using the risk assessment workflow in the Risk Assessment in Apex. This process involves entering the characteristics of the engagement into the Risk Assessment in Apex, which then uses this information to filter appropriate content for use in the risk assessment.

17.26 Ahead of completing the Risk Assessment in Apex, the auditor should also complete the Going concern approach assessment tool. This tool will provide information on the Financial Statement Risk Sub-Areas and Financial Reporting Sub-Activities to scope-in for going concern within the Risk Assessment in Apex.

Scoping the audit – Generic Inherent Risk Factors

17.27 The auditor will be presented with a centrally maintained list of Generic Inherent Risk Factors (GIRFs), which are either derived from the auditing standards or pervasive across the auditing methodology of the NAO. Using the understanding of the audited entity obtained as per Chapter 15: Gathering entity initial information, the auditor should select whether each of these are relevant to the audit, not relevant, relevant only for certain Financial Reporting Activities/Financial Reporting Sub-Activities, or currently unknown. GIRFs identified as being currently unknown will be assumed to be relevant for the initial risk assessment, but the engagement team should revisit and update these when able during the course of the engagement.

17.28 Where GIRFs are relevant only to certain Financial Reporting Activities/ Financial Reporting Sub-Activities, the auditor should specify which Financial Reporting Activities/ Financial Reporting Sub-Activities they are relevant for.

Scoping the audit – Financial Statement Risk Areas (FSRAs)

17.29 The auditor will be presented with a list of Financial Statement Risk Areas (FSRAs) and Financial Statement Risk Sub-Areas (FSRSAs), which are groups of potential risks which would impact across the Financial Statements of an Audited Entity based on a common set of Financial Reporting Requirements, Financial Statement Business Process(es) and/or one or more Legislative Bases. Using the understanding of the audited entity obtained as per Chapter 15: Gathering entity initial information, the auditor should select whether each of these are relevant to the audit or not relevant. Some FSRAs should be marked as relevant for all engagements comprising an audit of financial statements: these include FSRAs relating to related parties (see Chapter 28: Related parties) and to consideration of laws and regulations (see Chapter 31: Consideration of laws and regulations and reporting to regulators).

Scoping the audit – Financial Reporting Activities (FRAs) and COTABDs

17.30 The auditor will be presented with a list of Financial Reporting Activities (FRAs) and Financial Reporting Sub-Activities (FRSAs), which are groupings of one or more COTABDs that share the same set of potential risks of material misstatement based on a set of Financial Reporting Business Processes and/or Financial Reporting Requirements. Using the understanding of the audited entity obtained as per Chapter 15: Gathering entity initial information, the auditor should select whether each of these are relevant to the audit. For each FRSA, the auditor should also answer the scoping question concerning whether there is a possibility of material misstatement arising from estimates – where there is no reasonable possibility that a material misstatement could occur in an accounting estimate (for instance, the estimate is immaterial and the engagement team has concluded the estimate is

subject to an immaterial degree of estimation uncertainty), the accounting estimate in question will not be scoped in for further consideration as part of the Risk Assessment.

17.31 The next stage is for the auditor to identify the COTABDs that make up each FRA that is relevant to the audit. COTABDs should be identified in such a way that each COTABD contains a similar inherent risk profile. The engagement team should identify and name COTABDs in a manner specific to the audited entity – they are not drawn from the central Content Library.

17.32 The auditor should then enter financial values for each of the relevant FRAs/FRSAs and COTABDs. If the value of an FRA or FRSA is above performance materiality, it is scoped in for further assessment. If the value is below performance materiality, the auditor should select whether it remains scoped out or is scoped in at their discretion. For any scoped-out FRAs/FRSAs below performance materiality, the engagement team should undertake a completeness risk assessment and, where the FRA is relevant to estimates, an estimates risk assessment (except where the estimate is scoped out due to there being no reasonable possibility that a risk of material misstatement could occur, as outlined earlier in this section). The Risk Assessment in Apex will prompt the auditor to undertake completeness and estimates risk assessments where required.

Identifying risks of material misstatement and Inherent Risk Factors

17.33 The scoping workflow in the Risk Assessment in Apex described above will systematically identify and collate:

- for each Financial Statement Risk Area/Sub-Area, relevant risks of material misstatement (RoMMs);
- for each Financial Statement Risk Area/Sub-Area, relevant Inherent Risk Factors;
- for each Financial Reporting Activity/Sub-Activity, relevant risks of material misstatement (RoMMs); and
- for each Financial Reporting Activity/Sub-Activity, relevant Inherent Risk Factors.

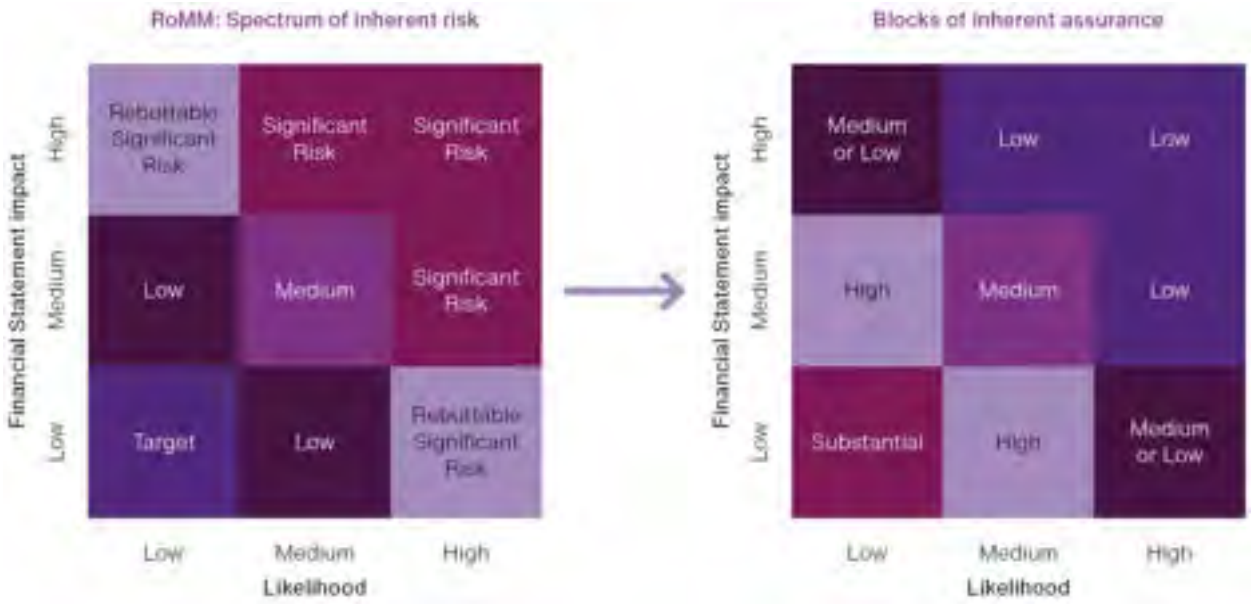
Assessing risks of material misstatement

17.34 As described above, the NAO's assurance model uses a qualitative approach to assessing risks and identifying an appropriate combination of responses to those risks.

17.35 Using the workflow in the Risk Assessment in Apex, the engagement team determines the significance of each identified RoMM (its inherent risk) through judging the combination of the RoMM's Likelihood and Financial Statement Impact (magnitude). The Likelihood and Financial Statement Impact (magnitude) placement (Low, Medium or High) for each RoMM is determined using the methodology described in the item in ***Table 17B*** above, under the heading 'Assessing the inherent risk associated with a RoMM', that describes the policy choices used by the NAO in applying paragraph 31 of ISA (UK) 315 (Revised July 2020).

17.36 The NAO uses the model shown in ***Figure 17D*** below to represent the 'spectrum of inherent risk', as referred to in ISA (UK) 315 (Revised July 2020). Each level of inherent risk on the spectrum of inherent risk (target, low, medium, rebuttable significant risk or non-rebuttable significant risk) corresponds to a block of inherent assurance as shown.

Figure 17D: The spectrum of inherent risk and blocks of inherent assurance



Building up assurance using responses selected through a qualitative approach

17.37 The level of inherent assurance over each RoMM (low, medium, high or substantial), determines what level of controls and substantive assurance (in combination) is required to address that RoMM. A RoMM is addressed by reducing the residual audit risk associated with that RoMM to the target detection risk point.

17.38 The Risk Assessment in Apex directs the engagement team to select responses that will enable these assurances to be obtained, including the substantive procedures to be performed based on particular levels of inherent assurance and controls assurance that are able to be obtained.

17.39 ***Figure 17E*** below, the 'wall of assurance', shows the options for combinations of inherent, controls and substantive assurance that can be used to address a RoMM. The engagement team should use the Risk Assessment in Apex to select a combination of controls and substantive responses to obtain complete assurance using one of the combinations set out in the wall of assurance.

Figure 17E: The wall of assurance

	Wall of assurance		
Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Medium	Low
		Low	Medium
		None	High
Medium	Low	Medium	None
		Low	Low
		None	Medium
Low	Medium	Low	None
		None	Low
Target/ No Risk	High	None	None

Control risk

17.40 Control risk is defined in paragraph 4 of ISA (UK) 315 (Revised July 2020) as the risk that a misstatement that could occur in an assertion about a COTABD and that could be material, either individually or when aggregated with other misstatements, will not be prevented, or detected and corrected, on a timely basis by the entity's system of internal control. In the NAO's methodology, control risk is considered to be the residual inherent risk after the application of controls assurance.

17.41 Controls assurance is obtained by the engagement team testing the operating effectiveness of controls (NAO engagement teams are not permitted to place reliance on the operating effectiveness of budgetary controls). A Medium level of controls assurance reduces the detection risk down two categories from its inherent state (for example, from High to Low, or from Medium to Target). A Low level of controls assurance reduces the detection risk down one category from its inherent state (for example, from High to Medium, Medium to Low or Low to Target).

17.42 If the engagement team does not test the operating effectiveness of controls, the control risk (residual inherent risk after controls assurance) is the same as the inherent risk (in accordance with paragraph 34 of ISA (UK) 315 (Revised July 2020)), since the residual inherent risk is not reduced from the original inherent risk by the application of controls assurance.), since the residual inherent risk is not reduced from the original inherent risk by the application of controls assurance.

17.43 This is reflected in the wall of assurance shown in ***Figure 17E*** as, for instance:

- where the inherent risk is Low and no controls assurance is available (i.e., the engagement team has not tested the operating effectiveness of controls), the substantive assurance required is Low, since this needs to address the control risk of Low (equal to the inherent risk given the lack of controls assurance);
- where the inherent risk is Medium and no controls assurance is available (i.e., the engagement team has not tested the operating effectiveness of controls), the substantive assurance required is Medium, since this needs to address the control risk of Medium (equal to the inherent risk given the lack of controls assurance);
- where the inherent risk is Significant and no controls assurance is available (i.e., the engagement team has not tested the operating effectiveness of controls), the substantive assurance required is High, since this needs to address the High control risk of (which reflects the Significant inherent risk given the lack of controls assurance).

17.44 However, if controls assurance is obtained through testing the operating effectiveness of controls, this reduces the residual inherent risk such that, for instance:

- where the inherent risk is Low and a Low level of controls assurance is obtained, no substantive assurance is required, since the residual inherent risk has been reduced one level by the Low controls assurance, from Low to Target. As per the section above, the RoMM is therefore addressed as the engagement team has reduced the residual audit risk associated with that RoMM to the target detection risk point;
- where the inherent risk is Significant and a Medium level of controls assurance is obtained, the substantive assurance required is Low, since the residual inherent risk has been reduced two levels by the Medium controls assurance, from High to Low (Medium being the intervening step). Only a Low level of substantive assurance is therefore required to reduce the residual audit risk associated with that RoMM to the target detection risk point.

Consultation with IT audit specialists

17.45 As set out in ***Table 17B*** above (under the NAO policies relating to paragraph 26(c) of ISA (UK) 315 (Revised July 2020)), it may be appropriate for the engagement team to consult with IT audit specialists (part of the Digital Financial Audit team) in certain circumstances: i.e., when there are complex information systems, where there are IT-dependent controls addressing RoMMs with a Financial Statement Impact (magnitude) and/or Likelihood placement of High, or where the engagement team plans to test the operating effectiveness of IT-dependent controls.

17.46 The engagement team should complete the Understanding the Entity's Information Systems and Control Activity Components (UEISCAC) form and the Information Systems Complexity Assessment (ISCA) template therein, which includes documentation of the decision points set out in ***Table 17F*** below regarding whether consultation with IT audit specialists is required.

Table 17F: Requirements to consult with IT audit specialists

Possible outcomes	Scenarios

Consultation required **Mandatory consultation** with IT audit specialists (Digital Financial Audit team)	The overall assessment of IT complexity for one or more Financial Reporting Activities (FRAs) is High.
	The overall assessment of IT complexity for one or more FRAs is Medium or Low, but **at least one** of the following individual assessments has been made on the FRA: • High complexity third party hosting or outsourcing; and/or • High or Medium complexity use of emerging technology; and/or • High complexity IT environment changes/data conversions.
	The overall assessment of IT complexity for one or more FRAs is Medium, there are IT-dependent controls addressing RoMMs with a Financial Statement Impact (magnitude) and/or Likelihood placement of High and **at least one** of the following is the case: • there are more than 5 privileged users; and/or • there are fewer than 5 privileged users but the level of access provided to these users is not appropriate; and/or • there is heightened risk from IT change and the design of the IT change policy is inadequate.
	The engagement team plans to test the operating effectiveness of IT-dependent controls.
Optional consultation with IT audit specialists (part of the Digital Financial Audit team) In these scenarios, the engagement team should document their rationale for consulting, or not consulting, in the Information	The overall assessment of IT complexity for one or more FRAs is Medium and: • **none** of the following individual assessments has been made on the FRA: o High complexity third party hosting or outsourcing; nor o High or Medium complexity use of emerging technology; nor

Systems Complexity Assessment template.	○ High complexity IT environment changes/data conversions; and • **none** of the following is the case: ○ there are more than 5 privileged users; nor ○ there is heightened risk from IT change; nor ○ the design of the IT change policy is inadequate; nor ○ there are IT-dependent controls addressing RoMMs with a Financial Statement Impact (magnitude) and/or Likelihood placement of High.
No consultation required with IT audit specialists (part of the Digital Financial Audit team) required	The overall assessment of IT complexity for one or more FRAs is Low and **none** of the following individual assessments has been made on the FRA: • High complexity third party hosting or outsourcing; nor • High or Medium complexity use of emerging technology; nor • High complexity IT environment changes/data conversions.

17.47 Engagement teams should note that the Digital Financial Audit team can only provide assurance that identified controls, interfaces and reports mitigate relevant RoMMs impacting transactions reported in the financial statements. The engagement team is responsible for assuring the final COTABD values in the financial statements and determining the coverage of the identified controls, interfaces and reports within each COTABD.

Example Inherent Risk Factors that may be particularly relevant for NAO audited bodies

17.48 The following is a non-exhaustive list of Inherent Risk Factors that may be relevant to NAO-audited entities (excluding fraud risks, which are listed in the following paragraph):

- There is a lack of personnel with appropriate accounting and financial reporting skills.
- Based on the output of the Information Systems Complexity Assessments, the overall assessment of IT complexity for one or more FRAs is Medium or High.

- There have been changes to the industry the entity operates, impacting year end valuations.
- The entity operates outside the UK in regions that are either economically unstable or exposed to volatile markets, impacting year end valuations.
- The entity is a charity.
- There has been a significant volume or value of past misstatements, a history of errors or a significant amount of adjustments at the period-end.
- Where General IT Controls (GITC) work is being carried out, the complexity of the GITCs is deemed to be high.
- There have been changes in technology with resultant impacts on asset value (i.e., through obsolescence).
- The entity is expanding its operations to new products, services, lines of business or locations.
- The entity prepares a Statement of Outturn Against Parliamentary Supply (SOPS).

17.49 The following is a non-exhaustive list of Inherent Risk Factors relating to fraud that may be relevant to NAO-audited entities:

- There are significant transactions with related parties.
- Excessive pressure exists for management to meet the requirements or expectations of third parties.
- There is excessive pressure on management or operating personnel to meet financial targets established by sponsors, Those Charged With Governance or other parties, including sales, profitability incentive goals or cost reduction goals.
- There is a complex or unstable organisational structure.
- The entity has incentives to 210anipulate their reporting income of expenditure in order to achieve control totals or budgetary targets.
- There are indications that personal financial obligations are creating pressure on management or employees with access to cash or other assets susceptible to theft to misappropriate those assets.
- There are characteristics or circumstances that increase the susceptibility of assets to misappropriation.
- Attitudes of staff and/or conditions exist which would enable staff to rationalise their actions, indicate an increased risk of fraudulent misappropriation of assets.
- Misstatement due to fraud has been identified in the course of this year's audit or the previous 2 years' audits.
- There have there been recurring attempts by management to justify marginal or inappropriate accounting on the basis of materiality.
- Financial stability or profitability is threatened by economic, industry, or entity operating conditions.
- Information available indicates that the personal financial situation of management or those charged with governance is threatened by the entity's financial performance.
- The nature of the industry or the entity's operations provides opportunities to engage in fraudulent financial reporting that can arise.
- Attitudes of staff, or other conditions, exist which would enable staff to rationalise their actions and indicate an increased risk of fraudulent financial reporting.
- There are incentives which increase the risk of misappropriation of assets by individuals or groups external to the entity.

- There are adverse relationships between the entity and employees with access to cash or other assets susceptible to theft that may motivate those employees to misappropriate those assets.
- There is a history or expectation of misappropriation of assets by individuals or groups external to the entity.
- Allegations of fraud have come to the attention of the auditor.
- Responses to inquiries with those charged with governance, management and others in the organisation are inconsistent.

17.50 Other examples are given in Appendix 2 to ISA (UK) 315 (Revised July 2020). All the examples given are either treated as generic Inherent Risk Factors or Financial Statement-level RoMMs in the NAO's methodology. All the examples given are either treated as generic Inherent Risk Factors or Financial Statement-level RoMMs in the NAO's methodology.

Audit procedures responsive to significant Assertion-level RoMMs

17.51 The engagement team should design and perform further audit procedures whose nature, timing, and extent are based on and are responsive to the assessed Assertion-level RoMMs following the requirements in paragraphs 6 to 23 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) and the related application guidance.

17.52 The Engagement Director and Engagement Manager should plan an audit approach to address each significant risk that reflects the most effective and efficient way of obtaining sufficient appropriate audit evidence over each assertion and audit area affected by the significant risk.

17.53 Assurance can be obtained through substantive testing or through a combination of controls and substantive testing, such as:

- substantive analytical procedures that are predictive in nature;
- computer assisted audit techniques;
- re-performance of testing by internal audit or management's experts; and/or
- other tests of detail.

17.54 Further guidance on these types of procedure may be found in Section 9: Testing techniques.

17.55 The engagement team should ensure the nature, timing and extent of the planned approach to address the significant risk at the assertion level is based on and specifically responsive to that risk and reflects the understanding of the relevant entity controls.

17.56 The engagement team should evaluate the design and implementation (D&I) of controls over the risk, reporting to management and those charged with governance if the controls are either not present or do not have an appropriate D&I.

17.57 If there are not appropriately designed and implemented controls in place to address the risk, the engagement team should discuss with management how they intend to obtain sufficient assurance over the balance to be able to approve the financial statements.

17.58 The primary responsibility for the financial statements remains with management and those charged with governance, and if they do not have appropriate control procedures in place to address significant Assertion-level RoMMs this would usually be a significant deficiency in internal control which should be reported to the audit committee and would normally also be reflected in the Governance Statement. Further guidance on reporting significant deficiencies in internal control to those charged with governance may be found in Chapter 57: Reporting to Those Charged With Governance.

17.59 The engagement team should document the following in the Apex audit file:

- the nature of the risk and the planned response;
- the work to evaluate the design and implementation of controls addressing the risk in the relevant Audit Response Group; and
- the nature, timing and extent of controls and substantive procedures performed to respond to the risk in the relevant Audit Response Group including the conclusions of the work performed.

17.60 Significant RoMMs are significant documentation matters. The engagement team should refer to paragraphs 8I and A8 to A11 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* and to Chapter 5: Direction and review of the engagement for requirements to document significant documentation matters. for requirements to document significant documentation matters.

17.61 The engagement team should discuss responses to significant RoMMs with the Engagement Quality Reviewer (EQR) (if allocated) as the EQR's responsibilities include performing an objective evaluation of the significant judgements made by the engagement team and conclusion reached in formulating the auditor's report. See Chapter 7: Engagement Quality Review for further guidance.

17.62 As well as affecting the nature, timing and extent of the planned procedures, the risks identified may affect whether more than one procedure should be performed in combination; for example, where there is a significant Assertion-level RoMM, it may be appropriate to confirm the completeness of the terms of a contract with the counterparty, in addition to inspecting the document.

17.63 The timing of planned procedures should reflect the nature of the risk. The higher the risk of material misstatement, the more likely it is that the engagement team will decide it is more effective to perform substantive procedures nearer to, or at the period end, or to perform audit procedures unannounced or at unpredictable times, such as performing audit procedures at selected locations on an unannounced basis.

17.64 Performing audit procedures before the period end may assist the engagement team in identifying significant matters at an early stage of the audit, and consequently resolving them with the assistance of management or developing an effective audit approach to address such matters.

17.65 The timing of audit procedures may also be affected by:

- the control environment;
- when information is available; for example, electronic files may subsequently be overwritten, or procedures to be observed may occur only at certain times;
- the nature of the risk; for example, if there is a fraud risk from subsequent creation of documentation, the engagement team may wish to examine contracts available on the date of the period end; and
- the period or date to which the audit evidence relates.

17.66 Increasing the extent of an audit procedure is only effective if the audit procedure itself is relevant to the risk being tested. It may be more effective and efficient to change the nature of the test being performed when a significant risk at the assertion level is identified. For example:

- the use of CAATs and data analytics may enable more extensive testing of electronic transactions and account files. Such techniques can be used to select sample transactions from electronic files, to sort transactions with specific characteristics, or to test an entire population instead of a sample for example
- the quantity of the evidence may be increased, or evidence obtained that is more relevant or reliable: for example, by placing more emphasis on obtaining third party evidence or by obtaining corroborating evidence from a number of independent sources

17.67 Parliament and the public generally expect public bodies to have effective controls in place to mitigate the risks that affect them. Therefore, the expectation should be that there are appropriately designed and implemented controls in place to address significant risks at the assertion level. This, in combination with the requirements of paragraph 26 of ISA (UK) 315 (Revised July 2020), drives the need to perform a design and implementation assessment for controls over significant Assertion-level RoMMs.

Audit procedures responsive to significant Assertion-level RoMMs – audit evidence

17.68 The reliability of audit evidence is often one of the main issues when responding to significant risks at the assertion level. Although there will be exceptions, such as when information obtained from an independent external source may not be reliable if the source is not knowledgeable, or a management's expert may lack objectivity, the following general guidance on reliability of evidence may be helpful:

- the reliability of audit evidence is increased when it is obtained from independent sources outside of the entity;
- the reliability of audit evidence that is generated internally is increased when the related controls, including those over its preparation and maintenance, imposed by the entity are effective;
- audit evidence obtained directly by the engagement team, such as observation of the application of a control, is more reliable than audit evidence obtained indirectly or by inference, such as inquiry about the application of a control;
- audit evidence in documentary form, whether paper, electronic, or other medium, is more reliable than evidence obtained orally; for example, a written record of a meeting made at or just after the time of the meeting is more reliable than a subsequent oral representation of the matters discussed; and

- audit evidence provided by original documents is more reliable than audit evidence provided by copies or after the original has been transferred to an electronic medium. In most cases it is normal to accept an electronic copy but always maintain and document your professional scepticism, particularly for significant risks at the assertion level. For example, a scanned invoice that is made into a .pdf from the scanner is more reliable than an invoice emailed to the audited entity as a MS Word© document which could later be amended up or down in value or have its date changed.

17.69 When considering the appropriateness of using the work of others, it is unlikely to be appropriate to use the work of employees of the entity in addressing significant risks that may relate to fraud by management. By contrast, work by the entity to quantify the extent of irregular transactions due to fraud and error by benefit or grant claimants may well be appropriate to use.

17.70 Confirmations may be particularly appropriate for significant Assertion-level RoMMs, as external confirmations received directly by the engagement team from appropriate confirming parties may assist the engagement team in obtaining audit evidence with the high level of reliability that is required to respond to significant risks, whether due to fraud or error.

17.71 Determining whether to use confirmations is a matter of professional judgement. For some significant Assertion-level RoMMs, the engagement team may consider that they are unable to obtain sufficient appropriate audit evidence without using external confirmations. However, for other significant RoMMs, external confirmations may not provide relevant audit evidence. For example, external confirmations provide relevant audit evidence about the existence of accounts receivable balances, but less relevant audit evidence about their recoverability – although the counter-party may acknowledge the debt, they may be unable to repay it.

Audit procedures responsive to significant Assertion-level RoMMs – using a controls and substantive approach

17.72 Where controls addressing the significant risks at the assertion level have an appropriate D&I, the engagement team should consider whether it will be effective and efficient to test their operating effectiveness.

Audit procedures responsive to significant Assertion-level RoMMs – using a substantive approach

17.73 The engagement team should carefully consider the audit response if appropriately designed and implemented controls are in place, but it is not effective and efficient to test them.

17.74 It may be appropriate to request management to perform additional work to assist the engagement team in obtaining an appropriate level of assurance.

17.75 ***Consultation required*** Computer assisted audit techniques (CAATs) may be used if they are an effective and efficient response to significant RoMMs. The engagement team should consult with the Financial Audit Data Analytics team within the Analysis hub (DART) if a CAAT involves macros, scripts or other forms of coding that have not been produced and approved by DART.

17.76 ***Consultation required*** Responses to significant RoMMs that will use data analytics should be discussed with FAPQ to ensure that the analysis/analytic performs in terms of functional logic and is accurate – code reviews may be required.

17.77 It is not possible to obtain the substantive assurance required for a Significant RoMM through Substantive Analytical Procedures (SAPs) alone: i.e. at least some tests of detail should be performed if using a SAP. SAPs are capable of providing a maximum of Medium substantive assurance. However, even where Low or Medium substantive assurance is required to address a Significant RoMM (i.e. where controls assurance is also obtained), paragraph 21 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) requires that the substantive response to a Significant RoMM must include a test of detail.

- If using sample testing, the samples must be relevant to addressing the significant RoMM and the team may wish to consult FAPQ on their proposed level of sampling to ensure it is sufficient and effective.
- Responses to significant risks relating to accounting estimates should be consistent with the requirements of ISA (UK) 540 (Revised December 2018) (Updated May 2022) and Chapter 36: Accounting estimates.

Audit procedures responsive to significant Assertion-level RoMMs – using work by the entity

17.78 Depending on by whom the work is performed, the engagement team should consider and comply with the requirements of ISA (UK) 500 (Updated May 2022) *Audit evidence* and ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors*. *Using the work of internal auditors*.

17.79 Often management or internal audit perform additional work in order to provide management with sufficient assurance over the balance to be able to approve the financial statements. This work may involve improving existing controls or putting in place additional control procedures. Where this is the case, the engagement team should evaluate the design and implementation of the control and reassess the approach to addressing the significant RoMM.

17.80 If management is unable or unwilling to put in place appropriate controls, the engagement team should report this to those charged with governance along with the audit approach planned based upon focussed substantive procedures, which may, for example, include CAATs to analyse an entire population and segment it into risk categories.

17.81 If management's planned response is for management or internal audit to perform procedures, it may be appropriate to plan to use this work and perform procedures to earn the right to do so.

17.82 The engagement team should consider whether it would be appropriate to use the work of management, their experts or internal audit by evaluating:

- the nature and scope of the specific work performed or to be performed;
- the nature of the significant RoMM;
- the degree of subjectivity involved in the evaluation of the audit evidence being gathered by their work; and
- whether the work is likely to be adequate for the purposes of the audit.

17.83 The engagement team should consider whether external confirmation procedures should be performed as a substantive audit response, in accordance with the requirements of paragraphs 19 and A48 to A51 of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

Audit procedures responsive to significant Assertion-level RoMMs – accounting estimates

17.84 Paragraphs 16 to 30 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures* and the related application guidance set out requirements for identifying and assessing RoMMs, including significant RoMMs, relating to accounting estimates and designing audit procedures responsive to those assessed risks.

17.85 Further guidance is provided in Chapter 36: Accounting estimates.

Nature, timing and extent of audit procedures over RoMMs that are not significant risks

17.86 The engagement team should design and perform procedures in accordance with paragraphs 6 to 14, 16 to 20 and 22 to 23 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) (paragraphs 15 and 21 are not applicable where there is no significant risk).

17.87 For RoMMs that are not significant risks, assurance may be obtained from:

- controls procedures together with tests of detail, using the work of others, digital techniques such as analytics;
- controls procedures together with substantive analytical procedures;
- tests of detail alone (including CAATs; for example, for recalculation or using the work of others); and
- substantive analytical procedures alone.

17.88 Further guidance on these types of procedure may be found in Section 9: Testing techniques.

17.89 When testing the operating effectiveness of controls, the engagement team should evaluate the design and implementation of the relevant control every year. The engagement team should plan to test its operating effectiveness at least every three years, and only when using evidence from prior periods is appropriate.

17.90 With regard to the requirement in paragraph 19 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) to consider whether external confirmation procedures should be performed as substantive audit procedures, the engagement team should request bank confirmations as appropriate for any bank accounts containing balances which are not held with the Government Banking Service (GBS). The engagement team should consider the necessity of these confirmations based upon factors including the value of past balances, the current balance, whether the account is closing, the frequency of transactions and the nature of the balance. Further guidance on bank confirmations may be found in Chapter 34: Tests of detail.

17.91 The engagement team should consider requesting confirmation from the audited entity's external legal counsel/lawyers to confirm there are no unresolved litigation or claims at the year end.

17.92 The engagement team should consider whether it is effective and efficient to perform audit procedures at an interim date and perform 'roll forward' testing to the year end. See Chapter 47: Interim audit procedures, including hard close audits for further information.

17.93 The timing of the planned procedures reflects the nature of each identified risk of material misstatement.

17.94 The volume of transactions and whether the audit is multi-location will also affect the timing of procedures.

17.95 The engagement team should determine the extent of the controls and substantive procedures required based upon materiality, assessed risk, and how much assurance the engagement team plan to obtain from each of controls and substantive assurance.

17.96 Increasing the extent of an audit procedure is effective only if the audit procedure itself is relevant to the identified risk of material misstatement which it has been designed to address.

17.97 The risks identified may affect whether a combination of procedures is required.

Audit approach for RoMMs where there is an expectation of material misstatement

17.98 The engagement team should carefully consider the audit response if there is an expectation of material misstatement: i.e., if there is an error rate which is known to be close to or above materiality or where there is a possibility of a limitation of scope in our audit.

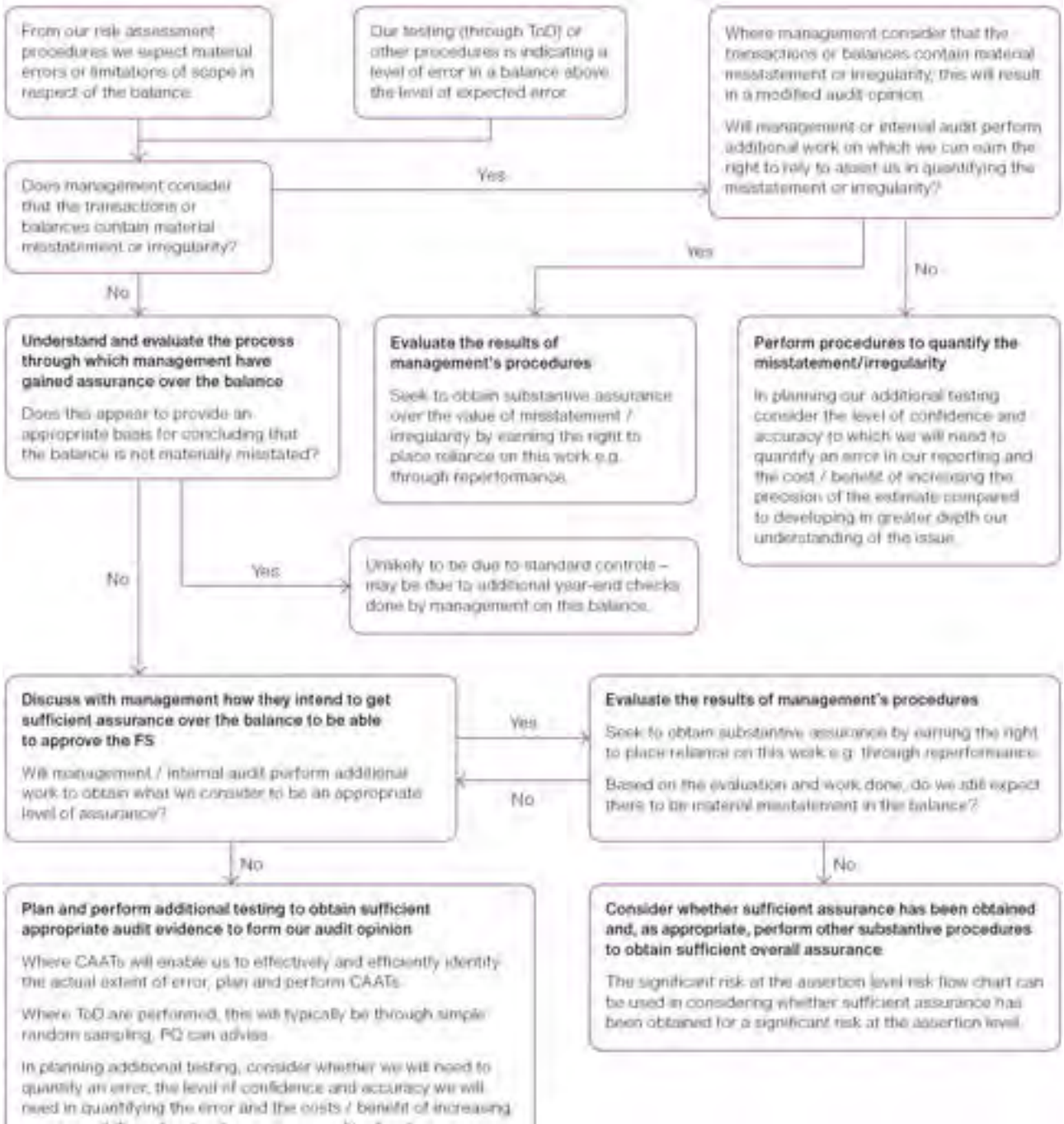
17.99 Chapter 18: Regularity risk assessment and response planning states that the approach set out in this section may also be applied in respect of the regularity opinion where there is an expectation of material irregular transactions.

17.100 ***Consultation required*** The engagement team should consider whether the objective of the audit procedures is:

- to identify with reasonable assurance whether there is a material misstatement; or
- to obtain reasonable assurance over the size of the misstatement in the financial statements – this may require significant work so engagement teams must consult with FAPQ to agree an efficient and effective approach.

17.101 ***Figure 17G*** illustrates the decision process for addressing significant risks where there is an expectation of material misstatement.

Figure 17G: Approach to significant risks at the assertion level when expecting material misstatement


From our risk assessment procedures we expect material errors or limitations of scope in respect of the balance
Our testing (through ToD) or other procedures is indicating a level of error in a balance above the level of expected error
Where management consider that the transactions or balances contain material misstatement or irregularity, this will result in a modified audit opinion
Will management or internal audit perform additional work on which we can claim the right to rely to assist us in quantifying the misstatement or irregularity?
Does management consider that the transactions or balances contain material misstatement or irregularity?
Yes
No
Yes
No
Understand and evaluate the process through which management have gained assurance over the balance
Does this appear to provide an appropriate basis for concluding that the balance is not materially misstated?
Evaluate the results of management's procedures
Seek to obtain substantive assurance over the value of misstatement / irregularity by earning the right to place reliance on this work e.g. through reperformance.
Perform procedures to quantify the misstatement/irregularity
In planning our additional testing consider the level of confidence and accuracy to which we will need to quantify an error in our reporting and the cost / benefit of increasing the precision of the estimate compared to developing in greater depth our understanding of the issue.
No
Yes
Unlikely to be due to standard controls – may be due to additional year-end checks done by management on this balance.
Discuss with management how they intend to get sufficient assurance over the balance to be able to approve the FS
Will management / internal audit perform additional work to obtain what we consider to be an appropriate level of assurance?
Yes
No
Evaluate the results of management's procedures
Seek to obtain substantive assurance by earning the right to place reliance on this work e.g. through reperformance.
Based on the evaluation and work done, do we still expect there to be material misstatement in the balance?
No
No
Plan and perform additional testing to obtain sufficient appropriate audit evidence to form our audit opinion
Where CAATs will enable us to effectively and efficiently identify the actual extent of error, plan and perform CAATs.
Where ToD are performed, this will typically be through simple random sampling. PQ can advise.
In planning additional testing, consider whether we will need to quantify an error, the level of confidence and accuracy we will need in quantifying the error and the costs / benefit of increasing
Consider whether sufficient assurance has been obtained and, as appropriate, perform other substantive procedures to obtain sufficient overall assurance
The significant risk at the assertion level risk flow chart can be used in considering whether sufficient assurance has been obtained for a significant risk at the assertion level.

17.102 Where there is an expectation of material misstatement, primary responsibility for determining whether this is the case and correcting the financial statements rests with management.

17.103 The engagement team should inquire of management how they intend to obtain sufficient assurance over the risk to approve the financial statements, which will be an iterative process if management's responses are insufficient. The engagement team should evaluate whether this provides an appropriate basis for concluding the balance is not materially misstated.

17.104 For an expectation of material misstatement, or if there is a potential limitation of scope of our audit, there is an expectation that the evaluation of the design and implementation of controls to prevent or detect and correct the misstatement will show they are inadequate. If controls were adequate (and operating effectively), they would prevent or detect and correct misstatements.

17.105 If management accept that there is material misstatement, then our audit opinion will be modified.

17.106 The engagement team should consider the extent of our understanding of the issue and of the error necessary to prepare the C&AG's report, including considering the cost/benefit of increasing the precision of the estimate of the error through testing additional items, as opposed to developing our wider understanding of the issue.

17.107 It may be appropriate to request management perform work to quantify the misstatement and then perform procedures to test this work. In other circumstances, the engagement team may perform procedures to quantify the issue.

17.108 If management's approach appears appropriate, the engagement team should evaluate the results of management or internal audit's procedures and test the work performed.

- If these are in effect an additional control, the engagement team should test the operating effectiveness of the control.
- If they are in effect a check of items for errors, the engagement team should earn the right to use management's or internal audit's work in support of the opinion, referring to the requirements of ISA (UK) 500 (Updated May 2022) *Audit evidence* and ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors* as appropriate.

17.109 In evaluating the appropriateness of the scope of checks performed by management or internal audit, it will usually be appropriate to evaluate the assurance obtained as though the work is a random sample.

17.110 If having done this work, the engagement team no longer expect there to be material misstatement in the balance, the engagement team should conclude on the issue as per any other significant risk.

17.111 If management's approach does not appear adequate, or if having tested their work it is still expected that there is a material misstatement in the balance, the engagement team should discuss further with management how they intend to obtain sufficient assurance over the balance to be able to approve the financial statements.

17.112 If the engagement team is unable to obtain assurance from using the work performed by management or internal audit, they should plan and perform the necessary substantive testing required to obtain sufficient appropriate audit evidence.

17.113 If the engagement team no longer considers that there will be material misstatement in a balance, they should consider whether they have obtained sufficient assurance over the significant risk at the assertion level or whether additional procedures are required. Engagement teams should then follow the requirements of ISAs (UK) and this Manual for responding to significant Assertion-level RoMMs where a material misstatement is not expected.

Audit approach to significant Financial Statements-level RoMMs

17.114 Significant Financial Statements-level risks of material misstatement include the presumed significant risk of fraud through management override of controls. The engagement team should understand and evaluate the design and implementation of control activities relevant to addressing significant risks at the financial statement level.

17.115 Significant risks at the financial statements level may relate to regularity; for example, where there has been a history of irregular payments in an organisation, or there does not appear to be an appropriate "tone from the top" about regularity of transactions. Significant risks at the assertion level may relate to regularity; for example, where there is a history of irregular grant payments. These are risks of material irregular transactions rather than RoMMs and covered in Chapter 18: Regularity risk assessment and response planning.

17.116 The relationship between significant FS-level RoMMs and significant Assertion-level RoMMs is dealt with in ***Table 17B*** above, under the item entitled 'Impact of Financial Statements-level RoMMs on Assertion-level RoMMs', which sets out the NAO policy on applying paragraphs 31(b) and A215 to A216 of ISA (UK) 315 (Revised July 2020).

17.117 A strong control environment may support the use of interim testing or controls reliance. Conversely, an ineffective control environment may have the opposite effect. Engagement teams may respond to deficiencies in the control environment in a number of ways, including:

- conducting more audit procedures as at the period end;
- developing a substantive response which addresses the significant risk;
- obtaining more extensive audit evidence from substantive procedures; and

- increasing the number of locations in the audit scope.

17.118 If the engagement team plans to test the operating effectiveness of control over a significant risk, they should test the relevant controls in the current period. The nature of FS-level RoMMs means that teams should be clear in their documentation as to whether the presumed fraud risks affect reliance on the controls.

17.119 Issues around IT general controls may represent significant FS-level RoMMs or increase the level of inherent risk within other FS-level RoMMs due to their impact across the organisation. Risks to internal control arising from IT systems which may give rise to significant risks include:

- reliance on systems or programs that are inaccurately processing data, processing inaccurate data, or both;
- unauthorised access to data that may result in destruction of data or improper changes to data, including the recording of unauthorised or non-existent transactions, or inaccurate recording of transactions; Particular risks may arise where multiple users access a common database;
- the possibility of IT personnel gaining access privileges beyond those necessary to perform their assigned duties thereby breaking down segregation of duties;
- unauthorised changes to data in master files;
- unauthorised changes to systems or programs;
- failure to make necessary changes to systems or programs;
- inappropriate manual intervention; and
- potential loss of data or inability to access data as required.

Presumed significant risk of fraud through management override of controls

17.120 Management is in a unique position to perpetrate fraud because of management's ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities. Due to the unpredictable way in which such override could occur, it is a risk of material misstatement due to fraud and thus a significant risk.

17.121 Therefore, every engagement will have a significant Financial Statements-level RoMM of fraud through management override of controls. The engagement team should identify the nature of the risk of management override in the context of the entity, which may give rise to the identification of further significant risks.

17.122 Irrespective of the assessment of the risks of management override of controls, paragraph 32 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires the auditor to design and perform audit procedures over journal entries, bias in accounting estimates and significant transactions outside the

normal course of business for the entity or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment and other information obtained during the audit.

17.123 The Engagement Director and Engagement Manager should determine whether, in order to respond to the identified risks of fraud through management override of controls, the engagement team needs to perform other audit procedures in addition to those specifically required by the standard. That is, where there are specific additional risks of management override that are not covered as part of the procedures required for every audit engagement.

Journal entries – risk assessment

17.124 As part of understanding the entity's internal control, the engagement team must assess the design and implementation of controls covering manual and automated journals and any associated risks. The approach to testing journals should reflect this understanding and the other risks identified in the audit.

17.125 Engagement teams need to understand the journals processes and controls sufficiently to support the derivation of the journals population. Engagement teams must document the evidence obtained to assess whether the list of journals selected for testing is complete.

17.126 Engagement teams are required to conduct a robust risk assessment of management override of controls prior to the use of the AIMS Journals App and should ensure that the results of this assessment are accurately reflected in the analysis. The identification of Inherent Risk Factors within the Risk Assessment in Apex will assist the auditor with this.

Identifying and selecting journal entries

17.127 When identifying and selecting journal entries and other adjustments for testing and determining the appropriate method of examining the underlying support for the items selected, the engagement team should consider the matters described in paragraphs A44 to A45 of ISA (UK) 240 (Revised May 2021) (Updated May 2022).

17.128 The AIMS Journals App is designed to assist with identifying and selecting journal entries and other adjustments for testing and draws on this application guidance. Starting from an entity's general ledger, it allows the engagement team to determine the population of journals and other manual adjustments, identify classes of journals processed in the normal course of business, review for indicators of potential fraud risk and select individual journals (or groups of journals) for testing.

17.129 The engagement team, may, based on their understanding of the entity and their fraud risk assessment, determine that the risk of management override of controls relating to specific classes of journals processed in the normal course of business is minimal or addressed by alternative audit procedures. For example, management might set up automated journals to post the depreciation entries calculated by a separate fixed asset register to the GL on a monthly basis. The engagement team may, in this case, decide that the risk of fraudulent override is minimal.

17.130 Such classes may be excluded from further analysis for fraud risk characteristics in order to appropriately focus procedures on areas of higher risk. For every such class, the engagement team must document the basis for their judgement, including why and how alternative audit procedures address the risk of fraudulent use of journals. This documentation should refer to the engagement team's fraud risk assessment and the incentives and opportunities for fraud identified. It is not enough to confirm that journals are within the sample population of, for example, a separate test of detail. Such procedures may not be responsive to fraud risk and separate analysis of journals may be required to provide sufficient, appropriate evidence.

17.131 ***Consultation required*** All engagement teams must use the most recent version of the AIMS Journals App for auditing journals. Where an engagement team does not believe they will be able to use the most recent journals analytic tool (or it is efficient to review 100% of journal entries due to the size of the entity) they must consult FAPQ to discuss alternative methods.

17.132 Risk characteristics must be relevant to the audited entity in terms of opportunity, rationale and incentive to manipulate the accounts (fraudulent financial reporting) or to cover the misappropriation of assets. Chapter 30: Fraud responsibilities provides further information on the types of journals and tests associated with designing an audit approach that stands a reasonable chance of detecting fraud.

17.133 The AIMS Journals App suggests risk characteristics and associated parameters for use in identifying and selecting journal entries for testing. The engagement team must consider the relevance of these to the entity, tailor where appropriate and carry out further analysis where they identify other characteristics of possible fraud that are specific to the audited entity. In doing so, the engagement team may determine that certain characteristics are only relevant indicators of fraud risk when they are seen in combination.

17.134 In considering the relevance and completeness of risk characteristics, the engagement team should consider the Inherent Risk Factors relating to fraud that are relevant to the audited entity and any RoMMs relating to fraud, as well as other factors considered within the engagement team's risk assessment, including the outcome of the Engagement Team Discussion on Risk and Fraud.

Reviewing accounting estimates for biases

17.135 The review of accounting estimates for biases required by paragraphs 33(b) and A46 to A48 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) should normally be performed by the Engagement Team-Leader or Engagement Manager, as they will have an overview of the audit as a whole to be

able to consider all accounting estimates. should normally be performed by the Engagement Team-Leader or Engagement Manager, as they will have an overview of the audit as a whole to be able to consider all accounting estimates.

17.136 The engagement team should document which accounting estimates are considered to be significant for the purposes of this review, and why other estimates are not considered to be significant.

17.137 The engagement team should consider whether differences identified in the review represent prior period misstatements.

17.138 In the public sector, fraudulent financial reporting through intentional misstatement of accounting estimates (as described in paragraph A46 of ISA (UK) 240 (Revised May 2021) (Updated May 2022)) may also involve making inappropriate year-end accruals to utilise budgets or moving costs between control totals.) may also involve making inappropriate year-end accruals to utilise budgets or moving costs between control totals.

17.139 In considering whether there are indicators of bias, possible factors to consider include:

- strong political or regulatory pressure to achieve a particular estimate;
- changing or unstable political, operational or regulatory environment;
- higher than normal expectations to meet budget; and/or
- reductions in budgets without corresponding reduction in service delivery expectations.

17.140 Differences between amounts recognised in the prior period financial statements and the outcome of accounting estimates do not necessarily represent prior period misstatements. However, they may do if the difference arises from information available at the time that should have been taken into account in the preparation of the prior period financial statements and was not taken into account.

17.141 The evaluation of the judgements and decisions made by management in making accounting estimates included in the current year financial statements is an overall evaluation of all accounting estimates, including estimates such as:

- allowance for doubtful accounts;
- inventory obsolescence;
- warranty obligations;
- depreciation method or asset useful life;
- outcome of long term contracts;
- costs arising from litigation settlements and judgments;
- expected credit losses;
- valuations of complex financial instruments, which are not traded in an active and open market; and

- valuations of property or equipment held for disposal.

17.142 Accounting estimates that are significant COTABDs may not all be significant accounting estimates for the purposes of this review, depending on the nature of the accounting estimate and the level of estimation uncertainty involved. For example, depreciation may be a significant account balance, but not considered to be a "significant accounting estimate".

17.143 The retrospective review of prior period accounting estimates is not intended to call into question the prior year audit judgements based on information available at the time but is intended to identify whether there are indications of possible bias on the part of management.

17.144 A retrospective review of accounting estimates is performed to identify and assess RoMMs due to, for example, the unreliability of management's estimates or the inherent level of estimation uncertainty in an estimate. It is usually efficient to combine this risk assessment procedure with our consideration of whether there are indications of bias in prior period significant accounting estimates.

17.145 A more detailed review would normally be appropriate for accounting estimates with high estimation uncertainty or significant changes year-on-year, whereas routine accounting estimates might be reviewed using just analytical procedures.

Business rationale for significant transactions

17.146 The requirement to evaluate the business rationale for significant transactions that are outside the normal course of business for the entity, or that otherwise appear to be unusual given the auditor's understanding of the entity and its environment and other information obtained during the audit is set out in paragraphs 33(c) and A49 of ISA (UK) 240 (Revised May 2021) (Updated May 2022).

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17.147 Indicators that may suggest that significant transactions are outside the normal course of business for the entity, or that otherwise appear to be unusual, may have been entered into to engage in fraudulent financial reporting or to conceal misappropriation of assets include:

- the form of such transactions appears overly complex e.g. the transaction involves multiple entities within a consolidated group or multiple unrelated third parties;
- management has not discussed the nature of and accounting for such transactions with those charged with governance of the entity, and there is inadequate documentation;
- management is placing more emphasis on the need for a particular accounting treatment than on the underlying economics of the transaction;
- transactions that involve non-consolidated related parties, including special purpose entities, have not been properly reviewed or approved by those charged with governance of the entity; and

- the transactions involve previously unidentified related parties or parties that do not have the substance or the financial strength to support the transaction without assistance from the entity under audit.

17.148 Examples of possible significant transactions outside the normal course of business include:

- economic development incentives;
- onerous provisions in contracts;
- real-estate purchases or sales;
- land swaps;
- granting of easements;
- public/private partnerships;
- privatisation, or other transfers between sectors, of services;
- early extinguishment of debt; and
- government guarantees or assurances to rescue private sector entities if they have financial difficulties.

17.149 Chapter 18: Regularity risk assessment and response planning sets out requirements to consider the regularity of transactions identified in this review.

Actions to maintain professional scepticism

17.150 A response of maintaining professional scepticism should be linked to one or more actions such as:

- specifying how the audit approach will be varied to give rise to a critical assessment of audit evidence, such as requiring original copies of documentation, or increased use of confirmations;
- reduced reliance on management representations;
- requiring additional supporting evidence of management explanations for variances on analytical procedures;
- additional consideration of accruals and large judgemental items around the year-end;
- an extended engagement team discussion to consider in more detail fraud risk factors identified;
- planning a follow-up engagement team discussion to consider the nature and cause of identified control deviations and misstatements during the course of the audit; and/or
- increased procedures to address the risk of management override of controls.

Actions to provide more supervision

17.151 A response of more supervision of the engagement team should be linked to one or more actions such as:

- first-stage review performed by Engagement Manager rather than Audit Lead in circumstances where the Audit Lead might otherwise have performed this task;
- increased review by Engagement Director of detailed work papers;
- Engagement Manager and Engagement Director reviewing on site;
- Engagement Manager arranging to be on site during final audit to provide guidance as needed (dealing with other engagements remotely); and/or
- appointment of an EQR.

Agreeing the financial statements to underlying records and examination of material journal entries

17.152 The engagement team should evaluate the design and implementation of the principal control activities around the financial statement close process and report any weaknesses to management. Typically, it will be appropriate to ask management to address these control weaknesses ahead of the year-end audit.

17.153 If management does not address identified control weaknesses, the engagement team should consider the impact on the planned nature, timing and extent of work on the financial statements and adjust the approach accordingly.

17.154 If the evaluation of controls indicates there are significant risks relating to the financial statement close process, the engagement team should identify and treat these like any other significant FS-level RoMM.

17.155 The engagement team should perform the substantive procedures related to the financial statement closing process required by paragraph 20 of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

17.156 Where audited entities use a software package or spreadsheet to translate the trial balance in to the accounts, the engagement team should confirm the software is appropriately set up, which includes confirming the right TB is used, the mappings and formulas are correct and all codes are used only once. A spreadsheet audit tool should be used to confirm the logical function and accuracy when spreadsheets are used for this purpose. OAK is available for this purpose with associated guidance. Where a tool is not used, the engagement team should document how assurance will be obtained over the logical function and accuracy.

17.157 ***Consultation required*** All engagement teams should use the most recent AIMS GL-TB Application to reconcile the general ledger to the trial balance and accounts. Where an engagement team does not believe they will be able to use the most recent TB to GL tool, they should consult FAPQ.

17.158 The procedures around year-end journal entries will normally be combined with the procedures performed in responding to the significant RoMM of fraud through management override of controls. If there is a specific year-end journal process, the engagement team should ensure that the testing includes all material year-end journals.

17.159 In some accounting systems, year-end journals are reflected in an additional 'period 13' accounting period, or otherwise segregated within the system. In other entities, adjustments may be posted directly to the financial statements, without entries in the underlying records (ledger). These are sometimes called 'on the face' adjustments.

17.160 The nature and extent of procedures on journal entries and other adjustments in preparing the financial statements depends on the nature and complexity of the financial reporting close process and associated risks.

17.161 It is usually most efficient for the final audit to begin after management have prepared draft accounts. Examples of procedures for agreeing the financial statements to supporting records and examining journals and other adjustments (where management has already prepared draft accounts) are as follows:

- Before beginning testing as part of the year-end audit:
    - obtaining management's mapping from the trial balance to the financial statements
    - checking that the mapping of individual lines to COTABDs is appropriate
    - identifying adjustments between the trial balance and the draft account
    - preparing the lead schedule based upon the draft account
- In performing testing as part of the year-end audit:
    - testing material journal entries in the preparation of the draft account
    - testing material adjustments between the trial balance and the draft account
    - testing other journal entries and adjustments in the preparation of the draft account where appropriate (typically most adjustments in preparing the draft account will be tested)
- In auditing the final financial statements:
    - update the lead schedule for adjustments between draft and final account
    - testing material journal entries between the draft and final account
    - testing material adjustments between the draft and final account
    - testing other journal entries and adjustments in the preparation of the final account where appropriate (typically most adjustments in preparing the final account will be tested)
- Assurance is therefore built up out of:
    - audit of the draft account figures, including journal entries and other adjustments between the trial balance and draft account

- audit of adjustments between draft account and final account

17.162 Where it is not possible/practicable to audit from a draft account, it may be necessary to perform the audit work from the trial balance and later perform procedures on the financial statements. This approach may also be appropriate in some circumstances when auditing components of groups to facilitate the consolidation process. Example procedures (where audit work is performed from the trial balance before management has prepared draft accounts) are set out below:

- Before beginning testing as part of the year-end audit:
  - obtaining from the audited entity a mapping of the trial balance to financial statement note lines
  - checking that the mapping of individual lines to COTABDs is appropriate
  - using the mapped TB figures as the "draft" figures for each audit area (either preparing the analysis ourselves or tying back a audited entity prepared analysis)
  - for SoFP items, adding summarised in-year movements to the opening TB balances
- In performing testing as part of the year-end audit:
  - testing material journal entries in the preparation of the trial balance figures (typically as part of responding to the pervasive risk of management override of controls)
  - if management has prepared "mapped" figures, testing material adjustments between the trial balance and the COTABD balances
  - if management has prepared "mapped" figures, testing other journal entries and adjustments in the preparation of the COTABD balances where appropriate (typically most adjustments will be tested)
- In auditing the final financial statements:
  - update lead schedules for adjustments between the trial balance and the final account
  - testing material journal entries between the trial balance and final account
  - testing material adjustments between the trial balance and final account
  - testing other journal entries and adjustments in the preparation of the final account where appropriate (typically most adjustments in preparing the final account will be tested)
- Assurance is therefore built up out of:
  - audit of the trial balance figures, including of the mapping of the trial balance to COTABDs
  - audit of journal entries and other adjustments between the trial balance and final account

Adequacy of presentation of the financial statements and disclosures

17.163 The engagement team will need to perform the audit procedures to evaluate the overall presentation of the financial statements required by paragraphs 24 and A59 of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

17.164 This includes evaluating whether:

- the individual financial statements are presented in a manner that reflects the appropriate classification and description of financial information in accordance with the FReM (or other applicable financial reporting framework);
- the form, arrangement, and content of the financial statements and their appended notes is in accordance with the FReM (or other applicable financial reporting framework); and
- the terminology used, the amount of detail given, the classification of items in the statements, and the accounting bases used are in accordance with the FReM (or other applicable financial reporting framework).

17.165 The engagement team should complete the relevant NAO disclosure guide for each set of accounts.

17.166 The Engagement Manager and Engagement Director should be involved in auditing the financial statements for compliance with the FReM (or other applicable financial reporting framework).

Addressing concerns raised in the risk assessment process

17.167 ***Consultation required*** If as a result of the risk assessment process there are doubts about the entity's auditability, the engagement team should consult with FAPQ in order to determine whether a qualified or disclaimed opinion is required.

Stand-back assessment

17.168 At the conclusion of the risk assessment and response planning process as set out in this Chapter, the engagement team should document a stand-back assessment within the OAS Standback Memo template. The stand-back assessment serves as a sense check for the work performed and the output of the Risk Assessment in Apex, ensuring the engagement team is content with the risk assessment and the judgements made.

17.169 As part of the stand-back assessment, as required by paragraph 36 of ISA (UK) 315 (Revised July 2020), the engagement team should evaluate the appropriateness of their determination of material COTABDs that have not been determined to be significant COTABDs. In the NAO's audit methodology, significant COTABDs are identified as COTABDs which are affected by any RoMM which is placed in the Low, Medium or High position on the spectrum of inherent risk (i.e., the RoMM is not in the Target position). This evaluation should be informed by a review by the Engagement Director of the following Standback Summary screens within the Risk Assessment in Apex:

- the listing of all material COTABDs with no substantive responses selected; and
- the breakdown of relevant COTABDs into significant and non-significant COTABDs.

17.170 The stand-back assessment should include consideration of:

- RoMM placement:
  a) whether the risk assessment placement for all RoMMs is complete;
  b) whether the judgements (particularly those where the engagement team has overridden a recommended risk placement or weighting in the Risk Assessment in Apex or rebutted a presumed significant risk) make sense and are consistent;
  c) whether the risk assessment makes sense, is consistent with the engagement team's expectations and other risks identified;
  d) whether the assessment of the Financial Statement Impact (magnitude) of each RoMM is consistent within the context of the other RoMMs within the same FRA or FSRA;
  e) based upon a review of the assertions impacted by RoMMs through the engagement team's risk assessment shown in the Risk Assessment in Apex stand-back screen, whether these impacts are complete and in line with the engagement team's expectations;
  f) whether the list of significant and non-significant COTABDs shown in the Risk Assessment in Apex stand-back screen is reasonable and in line with the engagement team's expectations; and
  g) whether there is a completed information flow for each significant COTABD;
- substantive responses:
  a) whether the controls and substantive responses to risks make sense and are consistent with other similar areas;
  b) whether any quantitatively material COTABDs have no substantive procedures assigned;
  c) how any quantitatively material COTABDs with no substantive procedures will be tested; and
  d) whether all necessary Financial Reporting Activities and Sub-Activities have been scoped in.

Planning matters addressed in other Chapters of the FAM

17.171 Planning matters in relation to the following matters are addressed in the Sections and Chapters of the FAM listed below in ***Table 17H***.

Table 17H: List of other Sections and Chapters of the FAM that address specific planning matters

Matters that may be relevant to planning	Relevant Sections or Chapters
Quality management (including individuals' responsibility for quality; direction and review; consultation; Audit Planning Consultation Meetings; and Engagement Quality Review)	Section 3: Quality management
Ethical requirements	Chapter 8: Ethical considerations

Acceptance and continuation of client relationships and engagements	Chapter 9: Engagement acceptance (statutory and non-statutory)
Assignment of engagement team members	Chapter 12: Roles, delegations and licences
Materiality	Chapter 16: Materiality, performance materiality and the trivial threshold
Group audits	Chapter 25: Group audit procedures
Fraud responsibilities, including anti-money laundering procedures	Chapter 30: Fraud responsibilities
Selection of audit responses	Section 9: Testing techniques
Accounting estimates	Chapter 36: Accounting estimates
Going concern status	Chapter 27: Going concern
Contracted-out audits	Section 10: Contracted-out work
Company audits	Chapter 42: Companies
Charity audits	Chapter 43: Charities
Pension scheme audits	Chapter 44: Pension schemes
Public Interest Entities	Chapter 45: Public Interest Entities
Service organisations and shared service centres	Chapter 46: Service organisations and shared service centres
Engaging an auditor's expert	Section 12: Use of experts

Chapter 18: Regularity risk assessment and response planning

Relevant standards and guidance

18.1 Part 2 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* sets out guidance on public sector auditors' considerations of regularity and related matters.

18.2 International Standards on Auditing (UK) do not directly apply to the audit of regularity. However, both Practice Note 10 (Revised 2022) and this Manual require the auditor to apply the principles in particular ISAs (UK) for certain aspects of the audit of regularity, as described. ISAs (UK) have also influenced the design of the NAO's audit methodology for regularity.

The Regularity Risk Assessment

18.3 The engagement team should use the Regularity Risk Assessment template to identify and document the audited entity's framework of authorities and the applicable risks of material irregular transactions.

18.4 Within the Regularity Risk Assessment template, the engagement team should make an assessment of the risks of material irregular transactions associated with each aspect of the possible frameworks of authorities listed in the template, categorising these as follows:

- No risk: there is no risk of material irregular transactions, either because that aspect of the possible frameworks of authorities is not relevant to the audited entity or because the value of affected transactions is immaterial.
- Significant: there is a heightened risk of material irregular transactions.
- Low: by exception, there is some risk of material irregular transactions, but the risk of their crystallising is very low due either to the nature of the risk or the counterparties involved.
- Medium: there is a risk of material irregular transactions, but this is not a heightened level of risk or a low level of risk (i.e., all other levels of risk).

18.5 Based on this work, the engagement team should then select appropriate procedures to respond to the risks of material irregular transactions in the context of the applicable framework of authorities. The engagement team may adapt the standard procedures set out within the template and design additional procedures in response to particular circumstances and risks for the individual audited entity.

18.6 Risks of material irregular transactions are recorded in the Regularity Planning template rather than the Risk Assessment in Apex. Risks of material irregular transactions may be treated as significant risks. Indicators of increased inherent risk relating to regularity matters may include a history of irregular

payments in an organisation (either generally or particularly for certain transaction streams, such as grant payments), or if there does not appear to be an appropriate “tone from the top” about the regularity of transactions.

18.7 The guidance in the remainder of this Chapter should be referred to by engagement teams when selecting appropriate procedures and/or individually-designed or adapted controls and substantive responses to address the risks of material irregular transactions.

Approach to auditing regularity

18.8 The nature and range of work required to obtain assurance in support of the C&AG’s opinion on regularity will depend upon the complexity of the entity’s framework of authorities and the controls which the entity has put in place to ensure compliance with that framework of authorities.

18.9 Understanding the framework of authorities applicable to the audited entity’s transactions is fundamental to the audit of regularity. This understanding should be obtained upon accepting a new client and updated for each period of the engagement. Chapter 11: Determining the framework of authorities provides guidance on obtaining and updating this understanding.

18.10 As part of the risk assessment process, engagement teams should understand and document the controls which have been put in place by the entity to prevent and detect material irregular transactions.

18.11 Based upon its assessment of the risk of material irregular transactions and evaluation of the controls in place to prevent or detect this, the engagement team should plan and perform audit procedures to determine whether in all material respects the entity's expenditure and income comply with the relevant authorities. These procedures must include consideration of the qualitative issues and aspects.

18.12 The engagement team should design and perform controls and/or substantive audit procedures whose nature, timing, and extent are based on and are responsive to the assessed risks of material irregularity for each transaction stream and for the financial statements as a whole. These should be summarised in the Regularity Planning Template in the audit file. The procedures to be performed should be directly linked to the risks of material irregular transactions relevant to the entity and its framework of authorities.

18.13 The general approach to planning and performing procedures to obtain assurance over regularity is the same as for the true and fair opinion. As such, the guidance provided by ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor’s responses to assessed risks* and within the rest of this Manual applies equally in the context of assurance in support of the regularity opinion.

18.14 Analytical procedures on their own are unlikely to provide sufficient appropriate audit evidence in support of the regularity opinion. They may nonetheless assist the engagement team in confirm that amounts recorded in the financial statements are consistent with expectations (paragraph 2-49 of Practice Note 10 (Revised 2022)).

18.15 Evidence in support of the regularity opinion may be obtained as part of an integrated approach to the audit of the financial statements. As such, certain testing may provide assurance in support of both the “true and fair” and regularity opinions. Where this is the case, the engagement team should ensure that the objective of the test provides sufficient appropriate assurance to support the regularity opinion.

18.16 The engagement team should be aware of, and remain alert to the possibility of, the risk of material irregular transactions throughout the work which is undertaken during the course of the audit of the financial statements. For example, work performed in testing key balances or disclosures or in reviewing the Governance Statement might provide indications of material irregular transactions which would need to be considered in the context of the C&AG’s regularity opinion.

18.17 The testing of regularity should be integrated with other audit procedures, as far as appropriate, and to the extent that our overall performance of procedures is efficient.

18.18 The audit work over regularity will normally be a mixture of controls and substantive procedures. Substantive procedures may include, for example:

- tests of detail of transaction streams;
- reliance on the work of internal audit over the correct application of grants by recipients against the conditions of the grant; and
- a review of the entity's management accounts to identify unusual transaction streams or account balances.

18.19 The extent of the substantive procedures will depend upon the assessed risk and the evaluation and testing of the relevant controls. The evidence which is obtained in support of the regularity opinion will often provide assurance in respect of the true and fair audit assertions.

Sample tests of detail for regularity

18.20 Targeted tests of detail (based on an assessment of where the likely risks of material irregular transactions exist in the account) are often more effective than blanket tests covering all transaction streams.

18.21 If tests of controls (with basic substantive assurance) or substantive analytical procedures would provide sufficient appropriate audit evidence over audit assertions, but do not cover regularity, it would not be appropriate to then conduct sample testing to obtain assurance over regularity without considering:

- whether the area could contain material irregularity; and, if so
- what alternative procedures could be conducted to obtain the required assurance.

18.22 In some circumstances, it may be appropriate to sample test particular income and expenditure streams, checking each sampled item to appropriate evidence that it is regular. In taking this approach, it is important to be clear in planning the test and in our documentation how the tests performed provide evidence of the regularity of sampled items. For some transaction types, such as means-tested benefits, this may be an involved process.

18.23 In general, however, sample tests of income and expenditure in support of the true and fair opinion will not include specific checks of the regularity of the sampled items. Nonetheless, where the engagement team identifies a potential regularity issue while carrying out sample testing, they should investigate; consider any implications for the audit approach and/or continuous risk assessment; and record and report any identified irregular transactions as appropriate in the circumstances.

Briefing the engagement team on regularity issues

18.24 In order to facilitate the understanding of an entity's framework of authorities by engagement team members, the Engagement Manager and Engagement Team-Leader are encouraged to explain the entity's framework of authorities to engagement team members as part of team briefings prior to audit visits. This may be done as part of the engagement team discussion on risk and fraud.

Minimum procedures to support the regularity opinion

18.25 Where the C&AG provides an opinion on regularity, there are a number of procedures which must be performed to support that opinion, regardless of the nature of the entity and complexity of its framework of authorities. These procedures are performed to provide assurance that the entity's general activities are in line with its framework of authorities.

18.26 The minimum procedures which must be performed in support of the regularity opinion are:

- review of income and expenditure for new transaction streams (or, for initial engagements, all material transaction streams), and consideration whether these are in line with what is permitted under the framework of authorities;
- consideration of the impact of any changes in the entity's remit and/or framework of authorities on the entity's transaction streams;
- consideration if there are indications that the pay remit (if applicable) may have been breached;
- scrutiny of income and expenditure for unusual and therefore potentially irregular items;
- procedures responsive to any identified material fraud risks for the entity (which would be significant risks); and

- inquiry of management and those charged with governance as to the existence of known irregularities (this is usually performed at the planning stage of the audit). Further guidance is available in Chapter 15: Gathering entity initial information.

18.27 The above minimum procedures are incorporated within regularity content within Apex.

18.28 In addition to this, engagement team members are expected to have an understanding of the entity's framework of authorities as set out in Chapter 11: Determining the framework of authorities. They should use this to understand the risk of irregular transactions which they may identify during the course of their work on the financial statements as a whole.

18.29 Where the entity has a more complex framework of authorities, the engagement team should plan a suitable response to the risks of material irregular transactions in addition to performing these minimum procedures.

Regularity of grant expenditure – risk assessment procedures

18.30 Paragraphs 2-51 to 2-52 and 2-65 to 2-68 of Practice Note 10 (Revised 2022) provide guidance on obtaining assurance over the regularity of grant expenditure. provide guidance on obtaining assurance over the regularity of grant expenditure.

18.31 The payment of grants is a significant function for a number of the NAO's audited entities. Where a regularity opinion is provided on an entity which pays grants, the engagement team will need to obtain assurance that the grant expenditure has been incurred in accordance with the entity's framework of authorities (in addition to the assurance required that the grant transactions are fairly stated in the financial statements).

18.32 Entities that paying grants should do so based on appropriate authorities, which are likely to vary significantly depending on the nature and purpose of the grant. These authorities will define the rules, regulations, policies and conditions that apply in respect of the grant stream. The engagement team should obtain an understanding of these authorities in order to assess the risks (both risks of material irregular transactions and risks of material misstatement) associated with the grant stream. Such authorities fall into two categories and the engagement team's understanding of each authority should include consideration of which of these categories each authority falls into (i.e. whether or not they form part of the audited entity's framework of authorities).

18.33 The first category is rules, regulations and conditions derived directly from the framework of authorities applicable to the entity. Transactions that do not comply with these authorities are usually irregular:

- An entity's authority to pay grants will usually be set out in legislation: either directly through primary legislation or through secondary legislation (such as regulations or statutory instruments) issued under the authority of primary legislation. This legislation may directly set the rules and conditions under which the grant must be paid, or must not be paid, and the amounts to be paid in particular circumstances.

18.34 The second category is internal rules, policies and conditions set by the entity and not imposed by an external authority. Transactions that do not comply with these parameters may still be regular.

- The legislation covering the grant may permit the entity to establish its own rules, policies and conditions or apply discretion, or alternatively may not set any conditions for payment of the grant.
- Where this is the case, any rules, policies and conditions set by the grant-paying entity on this basis would not usually be considered to form part of the entity's framework of authorities. This is due to the fact that such rules and requirements have not been set by an external authority to the entity and the entity is not accountable to an external entity for complying with them.
- Where no conditions are set in the entity's framework of authorities for the payment of grant, the level of audit work to obtain assurance over the regularity that grant stream will be minimal (although additional work may still be required to obtain assurance over the grant stream for the purpose of the true and fair opinion).
- For the purpose of the regularity opinion, the engagement team only need to obtain assurance over compliance with rules, regulations and conditions surrounding grant payments where these fall within the framework of authorities of the entity. Consequently, the engagement team are not required to obtain assurance over compliance by grant recipients with grant conditions set by the entity where these do not form part of the framework of authorities. However, compliance with such rules, regulations and conditions may be relevant to the recognition and measurement of grant payments and therefore additional assurance over compliance may need to be obtained for the purpose of the true and fair opinion.

18.35 The inherent risk associated with the regularity of grant streams is influenced by the complexity of the rules, regulations, policies and conditions applicable to each grant stream. The likelihood associated with risks of material irregular transactions for with a grant stream with more complex rules, regulations, policies and conditions may be more likely to arise than for a less complex grant stream.

18.36 Where Managing Public Money is relevant to the grant-paying entity, risks of material irregular transactions may arise from its requirements and these may go beyond the rules, regulations and conditions directly applicable to the grant based on the entity's framework of authorities and internal policies. For example, grants may be paid that are novel, or could cause repercussions elsewhere in the public sector. If not approved by HM Treasury, such transactions may be irregular, even if ostensibly in line with the grant rules.

18.37 In addition, Managing Public Money includes requirements relating to losses, overpayments and write-offs. Failure to adhere to rules and conditions set by the grant-paying entity may result in losses, overpayments and write-offs, even where such rules and conditions are not derived directly from the framework of authorities. These losses, overpayments and write-offs may give rise to risks of material irregular transactions; for example, an overpayment written off without consulting HM Treasury (if required) may be irregular.

18.38 Based on the understanding of the grant stream and its rules, regulations, policies and conditions (including the extent to which these form part of the entity's framework of authorities), the engagement team should identify the risks of material irregular transactions associated with each grant stream and

design and perform controls and substantive procedures in response to the identified risks, as set out in the following section entitled 'Regularity of grant expenditure – controls and substantive responses'.

18.39 The procedures required to consider the regularity of the expenditure by the recipient body will depend upon the restrictions placed upon the use of the grants:

- where there are few restrictions, it may be sufficient to consider whether there are any indications of non-compliance with the grant rules, regulations, policies or conditions in the expenditure of the recipient body. This may be through, for example, review of current or prior period audited accounts and opinion or consideration of statements from the finance directors of recipients.
- where there are more restrictions, it will usually be necessary to test a sample of grants to evidence that they have been spent for the purposes intended, such as certificates from the recipient's auditors. If this evidence is not collected by the entity, the engagement team should consider the impact upon our audit approach and whether this represents a control deficiency.

Regularity of grant expenditure – controls and substantive responses

18.40 Where an entity pays a grant to another entity, it will usually establish controls and a system of monitoring to ensure that the recipient entity complies with the grant conditions (as described in paragraph 2-65 of Practice Note 10 (Revised 2022)). This expectation is written into Managing Public Money.

18.41 Where the engagement team have assessed that the controls put in place by the entity to obtain assurance over a grant recipient's compliance with the terms and conditions of a grant are adequately designed and implemented, they should consider testing the operating effectiveness of these controls. However, this should only be done where the assurance provided by these controls is relevant to the terms and conditions of the grant set out through the entity's framework of authorities.

18.42 A number of the procedures to obtain assurance over the regularity of grant expenditure require the engagement to place reliance upon the work of others. In doing so, the engagement team should have regard to the requirements of ISA (UK) 500 (Updated May 2022) *Audit evidence*, ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors* and ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert*. Further guidance is available in Section 12: Use of experts.

18.43 Where the engagement team seek to obtain assurance through certificates or reports issued by the auditor of the grant recipient, they will need to ensure that:

- the instructions issued to the auditor of the grant recipient address the regularity considerations satisfactorily;
- the scope of the work performed by the auditor of the grant recipient is sufficient to provide appropriate assurance of compliance with the framework of authorities for the grant; and

- the quality of the work performed by the auditor of grant recipient is appropriate to enable assurance to be obtained. This is usually undertaken through reviewing the quality control procedures undertaken on this work.

18.44 Where the engagement team places reliance upon work commissioned by the management of the grant-paying entity to be performed by the auditor of a grant recipient, this should be treated as reliance upon the work of management's expert in accordance with ISA (UK) 500 (Updated January 2020) (Updated May 2022) *Audit evidence*. Further guidance may be found in Section 12: Use of experts.

18.45 Where the auditor of a grant recipient is required to provide a report or certificate on regularity to the grant-giving entity, it is often the case that this occurs some time after the period being audited. The engagement team should ensure that only the evidence available to the entity which relates to the relevant period should be used. Where this is not possible, or where the audited entity and grant recipients have different year-end dates, the engagement team should consider performing alternative procedures to obtain assurance.

18.46 Management should establish controls and processes to provide the Accounting Officer with assurance that grants have been used by recipients in line with the regulations which form part of the entity's framework of authorities. Engagement teams should evaluate the design and implementation of such control frameworks as it will usually be more efficient to place reliance upon these processes established by management.

18.47 Where deficiencies are identified in the controls and processes established by management to provide assurance that grants have been used by recipients in line with the regulations which form part of the entity's framework of authorities, the engagement team should consider reporting this to those charged with governance as a significant deficiency in internal control under ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management*. Further guidance on this may be found in Chapter 57: Reporting to those charged with governance.

18.48 The C&AG's statutory rights of access should provide engagement teams with sufficient access to records held by recipients of grants by audited entities to enable sufficient audit procedures to be performed in support of the regularity opinion. Such access rights should be confirmed through being written into grant agreements or funding agreements issued by the audited entities. Where the engagement team have concerns surrounding rights of access to grant recipients to facilitate work in support of the regularity opinion, they should consult with the Legal and Policy team. Further guidance on the C&AG's statutory access rights can be found in Chapter 3: Status and functions of the Comptroller and Auditor General.

18.49 Where an engagement team does not have sufficient access to a grant recipient or access to other sources to obtain sufficient appropriate audit evidence in support of the regularity opinion, then this may constitute a limitation of scope on the audit. Where material, such circumstances may lead to a modification of the regularity opinion. Engagement teams may consult FAPQ where these circumstances arise.

Regularity of fees and charges

18.50 A number of the NAO's audited entities will charge fees for services which they provide to members of the public. The basis for charging such fees should be set in statute. As part of understanding the framework of authorities for the entity, the engagement team should understand and document the statutory and legislative basis upon which such fees and charges are made by the entity.

18.51 The legislation permitting entities to charge fees and charges for services will normally set out the basis upon which such fees and charges should be calculated and made. This will vary from permitting the entity to calculate the fees and charges in a manner they see fit to setting out detailed calculations and guidance for the fees and charges to be made. Engagement teams should also be mindful of the guidance on Fees and Charges contained in Managing Public Money.

18.52 Where such conditions are set out in legislation or elsewhere in an entity's framework of authorities, any income incorrectly received as a result of a non-compliance with these conditions would be irregular.

18.53 Paragraphs 2-55 and 2-56 of Practice Note 10 (Revised 2022) provide guidance on auditing the regularity of fees and charges levied by public sector entities. provide guidance on auditing the regularity of fees and charges levied by public sector entities.

18.54 The engagement team should plan and perform appropriate procedures to ensure that any fees and charges made by the entity have been made in accordance with the regulations setting out the basis upon which they are made. Such procedures may include assurance from controls put in place by management to ensure that fees and charges are made in accordance with these regulations and/or substantive testing to ensure that fees and charges have been made in accordance with the regulations.

18.55 Where entities are required to prepare their financial statements under the FReM and must comply with Managing Public Money, they are required to include a disclosure of the income and expenditure associated with services for which fees and charges are made. For Departments, this disclosure should be included within the Parliamentary Accountability disclosures within the Accountability Report.

18.56 The engagement team should ensure that any disclosures included within the financial statements or the Accountability Report comply with the disclosure requirements of the FReM and Managing Public Money and are complete and accurate.

Considerations for the audit of group financial statements

18.57 As part of the work in understanding the structure of the group, the Group Engagement Team should ensure that they understand the relevant framework of authorities of components in the group and whether or not the component auditor provides a regularity opinion. Further guidance is available in Chapter 25: Group audit procedures.

18.58 Paragraphs 2-62 to 2-64 of Practice Note 10 (Revised 2022) provide guidance on using the work of others that is relevant to regularity in group audits.

18.59 In addition to following this guidance, the Group Engagement Team should collate any non-trivial irregular transactions identified by component auditors.

18.60 Where the entity prepares group financial statements and also requires a regularity opinion, the regularity opinion will apply to the group financial statements as a whole.

18.61 Frameworks of authorities are specific to individual entities. Therefore, each entity within a group will have its own framework of authorities. Therefore, the parent entity's framework of authorities is not considered to apply to the group as a whole. Consequently, there may be inconsistencies between the frameworks of authorities applying to entities within the group.

18.62 The group regularity opinion will provide assurance that the entities within the group have materially complied with their individual frameworks of authorities in the context of the group financial statements.

18.63 Some individual entities within a group for which a regularity opinion is provided may not have a framework of authorities. This is likely to be particularly relevant for components which are companies. In such circumstances, it may be sufficient for the Group Engagement Team to simply obtain assurance over any fraud considerations relevant to the component in order to obtain sufficient assurance in support of the group regularity opinion.

18.64 As part of the work undertaken by the engagement team in understanding the nature and scope of an entity's group, the Group Engagement Team should obtain an understanding of the framework of authorities of each entity within the group. This should inform the Group Engagement Team's judgement to the extent of work which is required to obtain assurance over regularity in respect of the group regularity opinion.

18.65 Where the component auditor provides a regularity opinion on the audit of the component entity, this is likely to be sufficient to provide assurance for the purpose of the group regularity opinion. This is due to the fact that the group regularity opinion provides assurance that the individual entities within the group have complied with their frameworks of authorities.

18.66 Where the Group Engagement Team wishes to obtain assurance over regularity from a regularity opinion provided by the component auditor, they should ensure that their understanding of the framework of authorities of the component entity is consistent with that of the component auditor. Where differences exist, the Group Engagement Team should consider whether further procedures are required to obtain assurance over the compliance of the component entity with its framework of authorities.

18.67 Where the component auditor did not provide an opinion on regularity in support of the component's financial statements, the Group Engagement Team should assess what further procedures are required to provide appropriate sufficient audit evidence from the component in support of the group regularity opinion. The Group Engagement Team may then decide to specify procedures relating to regularity to be performed by the component auditor within the group audit instructions to provide the necessary assurance.

18.68 Where the Group Engagement Team place reliance on the work of component auditors in support of the group regularity opinion, they should ensure that they comply with the requirements of ISA (UK) 600 (Revised September 2022). This would include obtaining the relevant confirmations from the component auditor of compliance with auditing standard and the FRC's Ethical Standard. Such confirmations are required regardless of whether the component auditor is performing specific procedures in support of the group regularity opinion or if the Group Engagement Team are taking assurance from the component auditor's opinion on regularity in the component's financial statements. Further guidance is available in Chapter 25: Group audit procedures.

18.69 Where the Group Engagement Team is unable to obtain sufficient assurance from component auditors to support the group audit opinion, they should consider performing their own procedures to obtain assurance that the component entity has complied with its framework of authorities. Such procedures may require accessing data or information held by the component entity.

18.70 The C&AG's statutory access rights should provide the Group Engagement Team with suitable access to the component entity. However, where difficulties in exercising these rights at component entities occur, the team should consult with the Legal and Policy team. Chapter 3: Status and functions of the Comptroller and Auditor General provides further guidance on the C&AG's statutory right of access.

18.71 ***Consultation required*** Where the Group Engagement Team is unable to obtain right of access to a component entity or other sources of appropriate evidence to support the group regularity opinion, there may be a limitation of scope on the audit. This may require a modification of the auditor's report. In such circumstances, the engagement team must consult with FAPQ in the first instance.

The risk of fraud in the audit of regularity

18.72 Paragraphs 2-79 to 2-82 of Practice Note 10 (Revised 2022) provide guidance on addressing the risk of fraud in the audit of regularity. provide guidance on addressing the risk of fraud in the audit of regularity.

18.73 There is some overlap between the work undertaken to address the risk of management override of control and the audit of regularity. Therefore, the work undertaken in accordance with ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* may also provide assurance to support the regularity opinion. may also provide assurance to support the regularity opinion.

18.74 In performing testing in support of the regularity opinion, the engagement team may become aware of instances of actual or suspected fraud. In such circumstances, the engagement team should be aware of both the impact on the financial statements and the potential need to comply with money laundering requirements. Further guidance may be found in Chapter 30: Fraud responsibilities.

18.75 In undertaking the review of the business rationale for significant transactions required by paragraphs 33(c) and A49 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team should consider the regularity of the significant or unusual transactions identified, and whether they may have been entered into to conceal irregular transactions., and whether they may have been entered into to conceal irregular transactions.

Legal advice

18.76 Judgements and consideration around regularity may involve interpretation of legislation and legal judgement. Where there is doubt as to the compliance of transactions with the entity's framework of authorities, there is an expectation in the first instance that management obtains a legal opinion to clarify the situation. Where management are unwilling to obtain a legal opinion in such circumstances, the engagement team may consult FAPQ.

18.77 ***Consultation required*** Where an entity has either refused to obtain legal advice concerning a judgement as to whether a transaction complies with the entity's framework of authorities or where the legal advice obtained by the entity is unclear, the engagement team may wish to obtain a separate legal opinion on the matter. In such cases, the engagement team should consult with the Legal and Policy team. However, in determining whether legal advice is required, the engagement team should first consider:

- the materiality of the matter in the context of the financial statements;
- the risk of irregularity based upon the nature and complexity of the framework of authorities; and
- the availability of other audit evidence, in particular whether or not the entity has sought its own legal advice.

18.78 The Legal and Policy team has access to external legal advice Where external legal advice is obtained on a matter concerning regularity, the lawyer will be considered an auditor's expert. Therefore, the requirements of ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert* must be followed. Further guidance on this can be found in Section 12: Use of experts.

18.79 Where the engagement team becomes aware of a potential breach of legislation which may lead to an irregularity in the entity's financial statements, they should discuss this with management in the first instance, unless they are unable to do so. Where there is uncertainty surrounding the interpretation of legislation which the engagement team considers the entity may be in breach of, the engagement team should encourage management to obtain legal advice as to whether the entity is in breach of the relevant legislation.

18.80 The engagement team should assess any legal advice obtained by management on such matters by treating the lawyer as management's expert in accordance with ISA (UK) 500 (Updated May 2022) *Audit evidence*. Further guidance on this may be found in Section 12: Use of experts.

18.81 Where either management do not obtain legal advice relating to a matter where there is uncertainty over the interpretation of a point of law, or the legal advice which they have received is inconclusive, the engagement team may consult FAPQ and the Legal and Policy team as to whether the NAO should obtain independent legal advice on the matter.

Consulting the framework setters

18.82 A number of elements of frameworks of authorities followed by NAO audited entities are set by other Government Departments or bodies; for example, HM Treasury and the Cabinet Office. Where an engagement team is uncertain of an interpretation of a framework of authorities set by these bodies, they should determine first whether management have obtained clarification on interpretation from the relevant body.

18.83 Where management have either been unable to obtain the necessary clarification or interpretation of the framework of authorities from the relevant body or refuse to do so, the engagement team should consider whether it is necessary to seek advice directly from the relevant authority. In such circumstances, the engagement team may first consult with FAPQ.

18.84 Where an entity has breached a framework of authority which is set by a Government Department or body, they may wish to seek retrospective approval from the relevant body for doing so. Where such retrospective approval is obtained, this regularises the relevant transaction, in such a way that it is no longer considered to be irregular.

18.85 Government Departments and other relevant authorities which set elements of the framework of authorities for entities are able to retrospectively approve or regularise breaches in such frameworks. Where an approval has been obtained by an entity which is ambiguous or unclear, or where it is unclear whether the relevant authority has the appropriate level of authority to provide approval the engagement team may contact FAPQ. FAPQ may then decide to explore the matter further with the relevant authority.

Disclosures in the financial statements

18.86 An entity's framework of authorities or financial reporting framework may introduce additional requirements for disclosure in the financial statements in respect of regularity. For example, the Statement of Outturn against Parliamentary Supply is required to be prepared by Departments. The entity may also be required to disclose any instances of non-compliance with the framework of authorities.

18.87 ***Consultation required*** Taking into account considerations of materiality, the engagement team should consider the implications of any lack of or inadequate disclosure of any such requirements for the C&AG's audit report in consultation with FAPQ.

18.88 The engagement team should ensure that sufficient assurance to support the “true and fair” opinion on the financial statements is obtained over any disclosures concerning regularity which are required to be included in the financial statements by the entity’s framework of authorities or financial reporting framework. In particular, further guidance on the audit of the Statement of Outturn against Parliamentary Supply may be found in Chapter 41: Parliamentary Supply.

Audit approach where there is an expectation of material irregular transactions

18.89 The approach set out in the section in Chapter 17: Risk assessment and response planning entitled ‘Audit approach for RoMMs where there is an expectation of material misstatement’ may also be applied in respect of the regularity opinion where there is an expectation of material irregular transactions.

Chapter 19: Continuous risk assessment

Relevant standards and guidance

19.1 Paragraphs 37 and A236 of ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* include requirements to revise the identification or assessment of the risks of material misstatement where the auditor obtains new information.

19.2 Paragraphs 1-72 to 1-82 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 315 (Revised July 2020) in the public sector.

Purpose of the continuous risk assessment

19.3 Risks of material misstatement and of material irregular transactions evolve during the course of an audit as the circumstances of an audited entity change and additional information is identified during the course of the audit. It is therefore important for the auditor to go back and revise the initial assessment of risk after the completion of initial fieldwork to reflect both developments at the audited entity and further relevant information identified during the course of the audit. This is in addition to the stand-back assessment described in Chapter 17: Risk assessment and response planning.

Audit risk

19.4 The engagement team should continuously review their assessment of audit risk and overall audit approach as the audit progresses. Prompts for the engagement team to revisit their risk assessment would include the identification of significant audit issues or changes in circumstances, such as:

- failed controls testing necessitating a change to substantive testing;
- additional understanding meaning the engagement team are able to move to a controls-based approach;
- a significant fraud is uncovered;
- the engagement team has cause to believe that senior management no longer has sufficient integrity; or
- the announcement of a machinery of government change.

The engagement team must revisit their risk assessment and audit approach prior to the commencement of final audit fieldwork and again immediately prior to certification

19.5 This review should include considering whether the risk assessment and audit approach remain appropriate in light of the findings of audit work performed so far. The engagement team should additionally carry out such a review in the case where significant issues arise on the audit or the circumstances relating to the engagement and/or the audited entity change such that the overall audit risk may be significantly impacted.

19.6 In particular, the engagement team should consider whether the risk assessments carried out as per Chapter 17: Risk assessment and response planning and Chapter 18: Regularity risk assessment and response planning remain appropriate in light of the information obtained so far during the audit.

19.7 The engagement team should consider whether additional information would change their scoping of Financial Reporting Activities and Generic Inherent Risk Factors and/or the planned responses to Generic Inherent Risk Factors within the Risk Assessment in Apex and/or the judgements made on the placement of RoMMs on the spectrum of inherent risk (Likelihood and Financial Statement Impact).

19.8 The engagement team should consider whether its audit approach remains appropriate in light of the findings of work performed so far as part of the audit. In particular, this should focus upon whether the planned responses continue to address the identified RoMMs and risks of material irregular transactions (as updated for the continuous risk assessment). The engagement team should also confirm that substantive procedures will be performed over all material COTABDs (based on an updated assessment of materiality) as required by paragraph 18 of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

19.9 Engagement teams may find it helpful to undertake this review through an engagement team meeting led by the Engagement Director.

19.10 After revisiting the risk assessment, the engagement team should update the Risk Assessment in Apex as appropriate. Any changes made should be approved by the Engagement Manager and Engagement Director and also be reflected within the relevant Apex Audit Response Groups.

19.11 Any amendments to the significant risks previously reported to those charged with governance at the planning stage or new significant risks to the audit should be communicated to management and those charged with governance at the earliest opportunity.

Engagement risk

19.12 The engagement team should continuously review their assessment of engagement risk as the audit progresses. Prompts for the engagement team to revisit their risk assessment would include the identification of significant audit issues or changes in circumstances, such as:

- failed controls testing necessitating a change to substantive testing;
- additional understanding meaning the engagement team are able to move to a controls-based approach;
- a significant fraud is uncovered;

- the engagement team has cause to believe that senior management no longer has sufficient integrity; or
- the announcement of a machinery of government change.

19.13 The Engagement Director should confirm that the assessment of engagement risk documented in the Engagement Risk Assessment Audit Form remains appropriate prior to the commencement of final audit fieldwork and again immediately prior to certification.

19.14 In particular, for delegated audits, the portfolio director should confirm that the delegation remains appropriate in light of matters identified so far as part of the audit. Where the portfolio director considers that the delegation no long remains appropriate, they should assume the role of Engagement Director and re-review the audit work undertaken thus far.

Other matters to consider in the continuous risk assessment

19.15 As part of the continuous risk assessment, the engagement team should additionally:

- Update their understanding of the accounting policies for significant transaction streams and balances and ensure the planned substantive and/or controls testing addresses the identified risks.
- Obtain assurance that the accounting policies (including for recognition, measurement, presentation and disclosure) applied comply with the relevant reporting framework and are appropriate for the entity.
- For group audits, review their assessment of group audit risk and overall audit approach and challenge whether the component engagement teams' risk assessments remain appropriate in light of the findings of audit work performed so far.
- Confirm that the audit approach has been updated to reflect the requirements of any Financial Audit Bulletins issued during the year.
- Consider whether it is necessary to revisit the engagement team discussion on fraud in light of any actual or suspected frauds identified or any changes to our overall fraud risk assessment.

Interaction with the system of quality management – continuous risk assessment

19.16 Chapter 4: Quality monitoring describes the NAO's system of quality management, which includes the monitoring and remediation process. Paragraph 39 of ISA (UK) 220 (Revised July 2021) requires that the Engagement Director takes responsibility for obtaining an understanding of the information from the NAO's monitoring and remediation process, as communicated by the NAO; determining the relevance and effect on the audit engagement of this information and taking appropriate action; and remaining alert throughout the audit engagement for information that may be relevant to the NAO's monitoring and remediation process and communicating such information to those responsible for the process.

19.17 The means by which the Engagement Director should obtain an understanding of information from the monitoring and remediation process is through reviewing relevant updates on the Sharepoint pages relating to the system of quality management. These updates will include actions specific to individual engagements arising from the Component Quality Risk Registers. The Engagement Director should re-consider, in the context of the specific engagement, how the matters detailed in the relevant updates apply and any appropriate actions to address such quality risks, taking into account the guidance provided on the page. At the continuous risk assessment stage, this review should be documented in Apex within the relevant Audit Response within the Continuous Risk Assessment Audit Response Group.

19.18 The means by which the Engagement Director should communicate information that may be relevant to the NAO's monitoring and remediation process to those responsible for the process is through raising a Consultation concerning the matter within Apex and directing this to FAPQ. Such information will be passed to the individuals operationally responsible for the monitoring and remediation process through the forum of Component Quality Management meetings, as described in Chapter 4: Quality monitoring.

Templates that should be updated as part of the continuous risk assessment

19.19 As part of the continuous risk assessment, the engagement team should ensure the Risk Assessment in Apex and the following templates have been updated:

- Continuous Risk Assessment Audit Response Group in Apex.
- Engagement Risk Assessment Audit Form
- Regularity Planning template
- Accounting policies template
- Going concern approach assessment
- Group Audit Test Plan (for group audits only)
- Engagement team discussion on fraud

19.20 Where changes to the risk assessment and/or audit approach are made as a result of the continuous risk assessment, the engagement team should ensure planning documentation is updated for these changes, including the Risk Assessment in Apex.

Chapter 20: Evidence assessment and evaluation

Relevant standards and guidance

20.1 ISA (UK) 500 (Updated May 2022) *Audit evidence* explains what constitutes audit evidence in an audit of financial statements and deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion.

Timing of fieldwork

20.2 If testing has been performed before the audit plan has been approved, such as due to the required timing of a visit to a remote location, a stock take, or because it is more effective to perform substantive or controls tests alongside risk assessment procedures for particular RoMMs or classes of transactions, account balances or disclosures (COTABDs), the engagement team should clearly document the reasons for this on the Apex audit file.

20.3 An interim audit can be an effective means to enable audits to be completed before the Parliamentary Summer Recess. Where the audited entity has a strong month-end close process, it may be appropriate to perform a hard close' audit of the performance statement and statement of financial position at Period 9, 10 or 11 and then limited roll-forward procedures to the year-end. The process for a hard-close audit is discussed in Chapter 47: Interim audit procedures, including hard close audits.

Obtaining sufficient appropriate audit evidence

20.4 Paragraphs A5 to A29 of ISA (UK) 500 (Updated May 2022) include discussion of what comprises sufficient appropriate audit evidence; sources of audit evidence; and audit procedures for obtaining audit evidence.

20.5 Sufficiency of audit evidence (as discussed in paragraph A8 of ISA (UK) 500 (Updated May 2022)) is affected by our assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and by the quality of audit evidence (the higher the quality, the less may be required). Obtaining more audit evidence may not compensate for poor quality evidence.

20.6 It is difficult to generalise about what makes audit evidence more reliable. There will be exceptions: for example, information obtained from an independent external source may not be reliable if the source is not knowledgeable. Paragraphs A35 to A38 of ISA (UK) 500 (Updated May 2022) include discussion of the reliability of audit evidence.

Agreeing client deliverables

20.7 Based on the output from the Risk Assessment in Apex produced as described in Chapter 17: Risk assessment and response planning and the responses to regularity identified as per Chapter 18: Regularity risk assessment and response planning, the engagement team should prepare a client liaison schedule. The client liaison schedule sets out the evidence required from the client to perform the planned audit procedures, who is responsible for delivering each item and by when these are expected to be delivered to the NAO team.

20.8 The team should agree the items to be delivered and target delivery dates in the client liaison schedule with the client.

Reviewing the draft annual report and accounts

20.9 The Engagement Director and Engagement Manager should complete an overall review of the draft financial statements and the draft annual report. This should include a review of the completion of the relevant disclosure guides covering both the annual report and accounts sections of the document.

Carry out planned audit procedures in response to identified risks

20.10 An appropriate member or members of the engagement team, based on the skills required and resources available, should carry out each of the agreed procedures based on the output from the Risk Assessment in Apex produced as described in Chapter 17: Risk assessment and response planning and the Regularity Testing Plan as described in Chapter 18: Regularity risk assessment and response planning.

20.11 These responses may consist of tests of controls; sample tests of detail; substantive analytical procedures; and other procedures. Guidance on performing these procedures is available in other Chapters of the FAM, in the testing procedures in Apex and in templates. In the FAM, engagement teams should refer particularly to Section 9: Testing techniques.

20.12 ***Consultation required*** Where required by the procedures set out in the Apex Audit Response or by the FAM or otherwise agreed with the Engagement Manager or Engagement Director, the engagement team should consult with one or more of: an auditor's expert; Centres of Expertise; FAPQ; and/or the Engagement Quality Reviewer. The engagement team should implement the results of this consultation when carrying out the planned procedures and/or update the audit approach accordingly.

20.13 ***Consultation required*** Where the audit evidence obtained is not sufficient or appropriate to meet the requirements of the test, the engagement team should discuss the issue with the client and determine a course of action in accordance with the requirements of ISAs (UK), Practice Note 10 (Revised 2022) and the FAM. If the engagement team is unable to resolve the issue through discussion with management, they should consult FAPQ.

Use of information produced by the entity

20.14 Information produced by the entity (IPE) is that which is generated by a computer and which can be used to support controls the engagement team may wish to test or which may support other audit procedures such as sampling populations such as the general ledger, aged debtors or automated accruals.

20.15 IT-dependent manual controls are manually performed, but may require IPE, for example, review and follow-up of exceptions on a payroll exception report. IT dependent manual controls are affected by IT general controls.

20.16 Reliance should only be placed on system/computer generated reports, including the general ledger download, if there is sufficient evidence to prove that the information produced is accurate and complete.

20.17 Where the engagement team chooses a substantive approach (i.e. no controls assurance) to obtain assurance over a RoMM or COTABD, the primary requirement of the technology in use is to understand the source of the data used as the basis for their substantive procedures. For example, this could be a report of transactions used to select a sample which has been reconciled back to the general ledger. This is predicated on assurance having been obtained that the general ledger report itself is accurate and complete.

20.18 Paragraphs 9 and A60 to A62 of ISA (UK) 500 (Updated May 2022) *Audit evidence* include requirements on evaluating the reliability of information produced by the entity. Procedures to obtain evidence of the accuracy and completeness of such information may include two-way testing between source and report.

20.19 Chapter 33: Analytical procedures includes requirements relating to the use of IPE within substantive analytical procedures over payroll costs (see the section of that Chapter entitled ‘Testing of staff reports used in payroll SAPs’).

External information sources

20.20 External information sources are defined in paragraph 5(ca) of ISA (UK) 500 (Updated May 2022). Paragraphs A1 to A4 and A39 to A44 of ISA (UK) 500 (Updated May 2022) provide application guidance on external information sources.

20.21 Paragraphs 1-113 and 1-114 of Practice Note 10 (Revised 2022) provide guidance on the use of external information sources in the public sector.

20.22 In the public sector, an external information source may be derived from the financial reporting framework. For example, HM Treasury directs government departments to adhere to the requirements of PES papers, which state the discount rates entities should apply to balance sheet items.

20.23 ***Consultation required*** In the circumstances envisaged by paragraph A44 of ISA (UK) 500 (Updated May 2022) (the auditor does not have a sufficient basis with which to consider the relevance and reliability of information from an external information source), the engagement team should consult FAPQ if sufficient appropriate audit evidence cannot be obtained through alternative procedures.

Professional scepticism

20.24 In accordance with paragraph 14 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements*, the NAO's policy is to assume that documents reviewed during the course of the audit are genuine, unless the engagement team becomes aware of reason to believe the contrary. If conditions identified during the audit cause the engagement team to believe that a record or document may not be authentic or that terms in a document have been modified but not disclosed to the engagement team, they should investigate further.

20.25 In accordance with paragraph 14-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team should remain alert for conditions that indicate a record or document may not be authentic.

First- and second-stage review and quality assurance procedures

20.26 Audit fieldwork should be subject to a first- and second-stage review process as set out in Chapter 5: Direction and review of the engagement.

20.27 Other quality assurance procedures relevant to fieldwork may include Hot Review, FAPQ review of accounts and Engagement Quality Review. These should be performed and responded to in accordance with the requirements of Section 3: Quality management and guidance in Apex testing procedures.

Chapter 21: Perform certification activities

Relevant standards and guidance

21.1 ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance* deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements.

21.2 Paragraphs 1-61 to 1-71 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 260 (Revised November 2019) (Updated May 2022) in the public sector.

21.3 ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* deals with the auditor's responsibility to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditor has identified in an audit of financial statements.

21.4 ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* deals with the auditor's responsibility to form an opinion on the financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

21.5 Paragraphs 1-203 to 1-216 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) in the public sector.

Interaction with the system of quality management – pre-certification

21.6 Chapter 4: Quality monitoring describes the NAO's system of quality management, which includes the monitoring and remediation process. Paragraph 39 of ISA (UK) 220 (Revised July 2021) requires that the Engagement Director takes responsibility for obtaining an understanding of the information from the NAO's monitoring and remediation process, as communicated by the NAO; determining the relevance and effect on the audit engagement of this information and taking appropriate action; and remaining alert throughout the audit engagement for information that may be relevant to the NAO's monitoring and remediation process and communicating such information to those responsible for the process.

21.7 The means by which the Engagement Director should obtain an understanding of information from the monitoring and remediation process is through reviewing relevant updates on the Sharepoint pages relating to the system of quality management. These updates will include actions specific to

individual engagements arising from the Component Quality Risk Registers. The Engagement Director should re-consider, in the context of the specific engagement, how the matters detailed in the relevant updates apply and any appropriate actions to address such quality risks, taking into account the guidance provided on the page. At the pre-certification stage, this review should be documented in Apex within the relevant Workflow Step Item within the Certification Workflow Step.

21.8 The means by which the Engagement Director should communicate information that may be relevant to the NAO's monitoring and remediation process to those responsible for the process is through raising a Consultation within Apex concerning the matter and directing this to FAPQ. Such information will be passed to the individuals operationally responsible for the monitoring and remediation process through the forum of Component Quality Management meetings, as described in Chapter 4: Quality monitoring.

Concluding and reporting

21.9 The engagement team should follow the procedures set out in Section 13: Concluding and reporting on forming an audit opinion, certifying and reporting on the annual report and accounts.

Chapter 22: Finalise, close and destroy audit file

Relevant standards and guidance

22.1 Paragraphs 14-16 and A21-A24 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* include requirements for the assembly of the final audit file.

22.2 Paragraphs 14 to 17 and A16a to A18-1 of ISA (UK) 560 *Subsequent events* include requirements relating to facts which become known to the auditor after the financial statements have been issued.

22.3 Paragraphs 1-120 to 1-141 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 560 in the public sector.

Assembly of the final audit file

22.4 The engagement team need to prepare audit files which support the C&AG's opinion. Our audit documentation provides:

- evidence of the basis for our conclusion about the achievement of our overall objectives; and
- evidence that the audit was planned and performed in accordance with ISAs (UK), NAO policy and applicable legal and regulatory requirements.

22.5 Completion procedures enable the engagement team to capture information and knowledge obtained during the audit which is relevant to the wider objectives of the NAO.

22.6 Prior to closure of the Apex audit file, the engagement team should complete the tasks required in the Closure Workflow Step. The Engagement Manager and Engagement Director should review this Workflow Step.

22.7 The engagement team should ensure that the following information has been updated within Engagement Details in the Apex audit file prior to file closure:

- audit opinion, providing further narrative in the event of modification of the certificate and report; and
- certification date.

22.8 The engagement team should ensure that key summary documents held in Apex allow easy knowledge sharing, ensuring also that the file complies with key provisions of the Security Manual and relevant laws and regulations. Summary documents normally include:

- the Signature Brief;
- the Audit Completion Report and (where relevant) Management Letter; and
- where relevant, documents relating to the C&AG's report.

22.9 ***Consultation required*** Paragraph 14 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) requires that the assembly of the final audit file shall be completed no later than 60 days from the date of the auditor's report. However, it is NAO policy that the Apex audit file should be closed and locked within 20 working days of the date of the auditor's report. If in exceptional circumstances, the engagement team does not consider it practicable to close the audit file within 20 working days, they must consult FAPQ.

22.10 Chapter 24: File management: Store documents and information and manage evidence provides further guidance on managing financial audit records and maintaining a standing information folder as part of the audit file.

Issuing a separate Management Letter

22.11 If the engagement team wishes to communicate control observations and recommendations through a Management Letter and the Management Letter has not been issued prior to the date of the auditor's report (for example, as part of the Audit Completion Report), the engagement team may issue a separate Management Letter to those charged with governance either during or after the file closure period. If a Management Letter is issued after the file closure period, the engagement team should not re-open the Apex audit file, but should instead store the Management Letter in an appropriate folder on Sharepoint. See Chapter 57: Reporting to Those Charged with Governance for further guidance on Management Letters.

22.12 Where a separate Management Letter is issued after the date of the auditor's report, all matters that are required to be communicated to those charged with governance under ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance* and ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* (and not already communicated in the Audit Planning Report or otherwise) should already have been met within the Audit Completion Report, which must be issued prior to certification.

Printing and publication by the NAO

22.13 If the NAO is responsible for laying and publishing the accounts, the engagement team should liaise with the Design and Publishing team.

22.14 Where the NAO arranges the printing of accounts certified by the C&AG, the Publications Section is responsible for co-ordinating the printing programme and liaising with the printer.

22.15 The Engagement Manager should:

- agree firm dates with audited entities for the preparation of draft and final printer's copy of accounts; and
- ensure that proofs are corrected to the agreed deadlines.

22.16 The electronic copy is provided to the Publications Section who typeset and proof-read the document.

22.17 Engagement Managers must ensure that audited entity -printed accounts are the same as the certified version. Where possible, proof-read the accounts prior to printing, otherwise compare the published and printed accounts to the certified account at the earliest opportunity. Pay particular attention to ensuring the C&AG's opinion and report are printed correctly. Immediately notify the audited entity of any discrepancies in writing. Where the discrepancies are significant, request that the audited entity correct the accounts; for example, by issuing an erratum slip.

22.18 The pdf file and checklist is then sent to the Engagement Manager, and should be cast, both vertically and horizontally, and should be read against the certified account or, if the account has not been certified, against the signed account (or a copy of it). Ensure that any amendments to signed accounts are carried into the proofs and check all alignments.

22.19 Any corrections to the proof should be made clearly, in red ink, and where the printer's correction marks do not adequately demonstrate the correction required, use the Authors' Query box on the checklist. Where transposed figures/letters are to be corrected, then in addition to the normal correction marks, the correct figure/word should be written out in full, again in red, (and circled) in the margin.

22.20 Having made all necessary corrections and amendments to the proof, the Engagement Manager should tick one of the three boxes on the checklist, and sign and date the checklist. After checking, this should be returned directly to the Publications Section.

22.21 Once a proof has been cleared for press the Publications Section is responsible for ensuring that the version printed is the same as the version that was cleared for press.

22.22 Once the proofs have been signed off as cleared for printing, the Publication Section returns them to the printer where they will then be printed to the agreed schedule. Accounts are generally published at 14.00 hours on the date that the Publications Section have agreed with the printer.

22.23 The Publications Section arrange for a PDF file to be made available on Merlin on the day of publication.

Other completion activities

22.24 At the completion stage, the engagement team should update the Certification Workflow Step in the Apex audit file to reflect the outputs from the audit, including the C&AG's opinion and details of any report.

22.25 The engagement team should record all financial impacts following the guidance available on Sharepoint.

22.26 The engagement team should consider whether the audit has identified any issues of general application, for which office-wide guidance may be required. Where this is the case, engagement teams may consult FAPQ.

Corrections to published accounts

22.27 Audited entities that need to make corrections to annual reports and accounts laid before one or both of the Houses of Parliament may do so using the correction procedure set out in paragraph 59 'Corrections to papers' of the House of Commons Journal Office guide to laying papers. The guide states that there are two options where a paper that has been laid before the House needs to be corrected:

- Correction slips will be accepted for minor, typographical errors that are obvious on the face of the paper.
- If the correction is substantive, it may be necessary to withdraw the paper and lay it again.

22.28 It is ultimately for the House authorities to determine which method of correction would be acceptable to the House. The guidance indicates that laying bodies should contact the Journal Office (using the contact details in the 'Contacts for further advice' section of the guide linked above) if a correction needs to be made. The Journal Office is expected to notify the NAO if an audited entity amends its laid accounts.

22.29 ***Consultation required*** If the audited entity amends the published financial statements, the engagement team should follow the requirements of paragraphs 15, 16 and A17 of ISA (UK) 560. The engagement team should consult FAPQ on the proposed new or amended C&AG's certificate or report. The engagement team may also refer to the Financial Reporting Council's Bulletin: Auditor's reports on revised accounts and reports in the United Kingdom (March 2020).

22.30 For company audits, the engagement team should note the legislative requirements governing revised financial statements and directors' reports, where the revision is voluntary, set out in Section 454 of the Companies Act 2006 and the Companies (Revision of Defective Accounts and Reports) Regulations 2008.

22.31 ***Consultation required*** Where the audited entity amends, or intends to amend, the published annual report, even where this does not impact the financial statements, the engagement team should consult FAPQ on the implications for the C&AG's certificate or report, including whether a new or

amended certificate or report will need to be re-issued. The C&AG may wish to withdraw and re-issue his certificate or report if, for example, a substantive amendment arises from a fact that, had it been known to the engagement team at the date of the C&AG's certificate or report, may have caused the engagement team to amend the section of the C&AG's certificate or report on 'Other information', which is required by paragraphs 21 and 22 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), or the 'Opinion on other matters' section, which is included under paragraph 43 of ISA (UK) 700 (Revised November 2019) (Updated May 2022).

22.32 ***Consultation required*** In the circumstances envisaged by paragraph 17 of ISA (UK) 560 (management does not take the necessary steps to ensure that anyone in receipt of the previously issued financial statements is informed of the situation and does not amend the financial statements in circumstances where the auditor believes they need to be amended), the engagement team should consult FAPQ on how to proceed. In these circumstances, the C&AG has the option of withdrawing his certificate or making an additional report to Parliament.

Retention and destruction of audit files

22.33 The NAO has established policies and procedures that apply adequate provision on confidentiality and professional secrecy in relation to all information and documents to which the NAO has access when carrying out an engagement and ensure that the NAO complies with applicable legal and regulatory requirements relating to the confidentiality of information received in the course of the engagement (as required by paragraph 34-1(m) of ISQM (UK) 1). These are set out in Apex user guidance and Information Security Policies available on Sharepoint.

22.34 In the context of individual engagements, these include:

- limiting access to the Apex audit file to authorised users; and
- back-up routines for electronic engagement documentation at appropriate stages during the engagement.

22.35 The NAO's policy is to retain engagement documentation for 6 years from the date of certification. Audit files are destroyed after this period. Signed accounts and related papers should be retained for 7 years after the year of account, except unpublished accounts, which should be retained for 25 years. The usual safeguards should be applied to the destruction of security classified material.

22.36 The retention period for audit files of 6 years from the date of certification is sufficient to permit the Compliance and Quality Unit and those carrying out external quality monitoring to evaluate the Office's compliance with its system of quality control.

22.37 Destruction of Apex audit files in line with these policies is carried out by the Audit Technology Support team, in consultation with FAPQ where required.

Chapter 23: Follow-up: Ensure continuous improvement of the audit

Internal and external feedback

23.1 After the final audit file is assembled and the Apex audit file is locked, the engagement team should hold an internal 'lessons learned' meeting. This should include consideration of any feedback from the client, Hot Reviewer, Engagement Quality Reviewer, FAPQ and/or Private Office, as applicable.

23.2 The engagement team should also hold a wash-up meeting with the audited entity and agree actions to be followed up in the following period.

23.3 The results of the internal lessons learned meeting and the external wash-up meeting should be noted and passed on to the engagement team for the following period.

Chapter 24: File management: Store documents and information and manage evidence

Relevant standards and guidance

24.1 ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* deals with the auditor's responsibility to prepare audit documentation for an audit of financial statements. The objective of the auditor under ISA (UK) 230 (Revised June 2016) (Updated May 2022) is to prepare documentation that provides:

- a sufficient and appropriate record of the basis for the auditor's report; and
- evidence that the audit was planned and performed in accordance with ISAs (UK) and applicable legal and regulatory requirements.

Boundary of the audit file

24.2 Paragraph 6 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) defines the audit file as one or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement. It also defines audit documentation as the record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached. It further clarifies that (in the UK) audit documentation includes all documents, information, records and other data required by ISAs (UK) and applicable legal and regulatory requirements.

24.3 The audit file for an NAO engagement performed in Apex comprises the information and attachments held within the relevant Audit Engagement record in Apex and the contents of the Workflow Step Items, Audit Response Groups, Audit Responses, Audit Forms, Risk Assessments, Misstatement records, Finding records, Recommendation Records, Quality Assurance Procedure records, Review records, Engagement Details records, Team Tasks, Consultation records, Milestone records, Team Roles and Team Members records, Certification records and Comments which are created under that Audit Engagement record, either automatically by the system or by the engagement team, and not subsequently deleted prior to closure of the audit file. The audit file does not include the information shared with engagement teams through Guidance tabs shown alongside any of the records listed above, since these are not records of performance of the engagement, but rather a means of highlighting central guidance alongside relevant Audit Response requirements.

24.4 Each Audit Engagement in Apex has an associated subfolder in Sharepoint that is linked to the Audit Engagement, where documents associated with the Audit Engagement are held (the subfolder for an engagement can be viewed via the Documents tab in the Audit Engagement record) – the audit file includes all documents held within this folder. Apex is built on a Sharepoint platform, but references elsewhere within this Manual to information being held on Sharepoint refer to the aspects of Sharepoint which serve as the NAO's intranet and general document repository, not to information held within Apex.

24.5 Team Tasks and Comments may be raised within Apex for administrative or temporary purposes, including notifying other team members of outstanding work. They may otherwise be used to record details of the direction, supervision and review of the work of the engagement team – the engagement team may wish to retain these on the audit file in order to demonstrate compliance with ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*, for example – or be used to record points to keep in view for audits in future periods. The engagement team should make judgements about whether to delete any remaining Team Tasks or Comments before closing the audit file (bearing in mind the possibility that the presence of numerous comments from an intermediate stage of work might impede the clarity of understanding of a reviewer and/or obscure the prominence of more pertinent information), as any undeleted Team Tasks or Comments will form part of the final audit file, even if they are marked as 'complete' or 'closed'.

24.6 Hyperlinking to a document held within Sharepoint and/or within another Apex Audit Engagement is not sufficient to bring that document onto the audit file, where this is necessary for compliance with the requirements of ISAs (UK) and/or this Manual. Such documents do not form part of the audit file where the only association is that a hyperlink to that document is included somewhere within the engagement.

Timeliness of documentation

24.7 Paragraph 7 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) requires that the auditor prepare audit documentation on a timely basis. As set out in paragraph A1 of ISA (UK) 230 (Revised June 2016) (Updated May 2022), preparing sufficient and appropriate audit documentation on a timely basis helps to enhance the quality of the audit and facilitates the effective review and evaluation of the audit evidence obtained and conclusions reached before the auditor's report is finalised. Documentation prepared after the audit work has been performed is likely to be less accurate than documentation prepared at the time such work is performed.

24.8 In addition, timely preparation and appropriate storage of audit documentation facilitates the timely review of audit work (and therefore the identification of issues earlier in the audit process, when they can more easily be addressed), central monitoring of progress across the wider Financial Audit Service Line and a reduced likelihood of lost work due to IT issues.

24.9 Accordingly, there is a general expectation that, in so far as is reasonably practicable and consistent with considerations of wider resourcing priorities and audit quality, engagement teams should endeavour to prepare audit documentation and bring this onto the Apex audit file either at the time of carrying out the underlying work or soon afterwards.

Managing financial audit records

24.10 Apex is the principal document store for financial audit working papers. Teams should ensure that, to comply with the requirements of ISAs (UK) and this Manual, all evidence necessary to support the C&AG's audit opinion is stored within Apex.

24.11 Teams may also find it useful to retain some documentation obtained or created as part of the audit in separately within Sharepoint:

- Key outputs – for example, Audit Planning and Completion Reports and other key outputs. Under previous guidance, this was mandated. If stored in Sharepoint, this sort of material should be kept in the Audit Assurance folder.
- Information required for wider work – for example, Board papers that contribute to client insight and sector understanding. Such information should be retained within an appropriate client area within Sharepoint – Standing Information, Research and Resources or Client Insight, bearing in mind security classifications.

24.12 Audit evidence that is not needed to support the C&AG's audit opinion and not required for wider work, should be destroyed or returned to the audited entity. AIMS should be used for the storage of bulk data.

24.13 Engagement teams should not delete or discard audit documentation of any nature from the completed audit file before the end of its 6-year retention period. This ensures compliance with the requirement in paragraph A23 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) to retain audit files for a period of at least five years from the date of the auditor's report. After 6 years following the date of certification, audit files are destroyed.

24.14 After the final audit file is archived, the engagement team should not modify documentation or add new documentation. If, due to exceptional circumstances, such a modification or addition is required, the engagement team should:

- ***Consultation required*** consult FAPQ with their proposed course of action;
- document the specific reasons for modifying the audit file; and
- document when and by whom the modifications or additions were made and reviewed.

24.15 In the approach to the end of each financial year, the Audit Technology Services team will contact portfolio directors to plan the review and destruction of financial audit records which are more than six years old. If there is a business reason to retain any records beyond the retention schedule (for example, if they contain 'audit precedent' material or relate to an unpublished account) these records should be identified and moved to an appropriate folder. Such audit precedent documents should, however, be stored on Apex to support brought forward audit judgements.

24.16 The Audit Technology Services team will coordinate this exercise with FAPQ so that Apex records which are more than six years old (that is, six years after the date of certification) are destroyed at the same time.

24.17 Where financial models or other audit evidence in the form of large or unstable files cannot be included in the Apex audit file, the engagement team should save these files to Sharepoint as a record and clearly reference these documents in the Apex audit file.

24.18 Supporting electronic files should not ordinarily be held outside of the Apex audit file. Where supplementary material is stored in Sharepoint a clear reference in the Apex audit file can be included for reference.

Standing information

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24.19 The engagement team should maintain a standing documentation folder in Sharepoint to reduce duplication of effort in future years. The team should update and review the contents of the standing documentation folder each year to ensure its completeness and relevance“”.

24.20 The standing information relevant to an audit depends upon the nature of the entity and the environment in which it operates. Copies of the following information are expected as a minimum:

- The letter of engagement/understanding
- The Accounting Officer’s letter of appointment (where relevant)
- The accounts direction (where relevant)
- Evidence to support relevant prior-year audit judgements
- Prior year financial statements
- Authorising legislation
- Additional regulations under authorising legislation
- Evidence of other activities authorised by Parliament i.e. ambit of the vote or framework agreement with the sponsor department (where relevant)
- Business plan/strategy
- Key performance metrics/ management information
- Details of delegated approval from HM Treasury, Cabinet Office or the sponsor department (where relevant)

24.21 In addition, the standing information folder may also include:

- Organisational charts, showing principal financial officers and their functions and key Internal Audit officers
- Details of relevant contacts
- Trend data for data analysis purposes
- Supporting papers on items of continuing significance
- Prior-year management letters
- Systems descriptions
- Details of the internal control system
- Internal audit plans

24.22 The relevant standing information folder must be included within the Apex audit file.

Amending the audit file after file closure

24.23 As required by paragraph 16 of ISA (UK) 230 (Revised June 2016) (Updated May 2022), if the engagement team finds it necessary to modify existing audit documentation or add new audit documentation after the assembly of the final audit file has been completed, other than due to performing new procedures or drawing new conclusions, regardless of the nature of the modifications or additions, they should document on the Apex audit file:

- the specific reasons for making them; and
- when and by whom they were made and reviewed.

24.24 If, in exceptional circumstances, the engagement team performs new or additional audit procedures or draws new conclusions after the date of the auditor's report, in accordance with paragraph 13 of ISA (UK) 230 (Revised June 2016) (Updated May 2022), the engagement team should document:

- the circumstances encountered;
- the new or additional audit procedures performed, audit evidence obtained, and conclusions reached, and their effect on the auditor's report; and
- when and by whom the resulting changes to audit documentation were made and reviewed.

24.25 ***Consultation required*** If the circumstances in either of the preceding two paragraphs apply and the Apex audit file for the engagement has already been closed, the engagement team should consult FAPQ, who will, if appropriate, liaise with the Audit Technology Services team to arrange for the re-opening of the closed file. If the re-opening of the file occurs more than 60 days after the date of the audit report and therefore breaches the time limit for completion of the assembly of the final audit file prescribed in paragraph A21 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) and paragraph A83 of ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements*, the engagement team should prepare a note to be included on the revised file setting out the circumstances of the amendment(s) and the reasons for the breach of the 60 day limit. When the file has been re-closed, FAPQ and the Audit Technology Services team will review any changes made since the file was re-opened to confirm that they have been made in line with the rationale under which the file was re-opened.

Availability of working papers

24.26 Unauthorised disclosure of working papers could result in public embarrassment, loss of credibility with NAO audited entities, and legal repercussions.

24.27 Information and data are of key importance to the NAO's business. The management of data used for audit purposes page on Sharepoint sets out policies and procedures for handling data, whether personal data as defined by the Data Protection Act or other sensitive data. Key elements of the NAO's Data Protection Framework have been incorporated into Apex Workflow Steps.

24.28 Bulk audited entity data should be stored securely within AIMS.

24.29 Information provided by audited bodies should be protected to the standards that they determine. Where this is not feasible, the engagement team should discuss the issue with the audited body's departmental security officer to determine whether they can agree alternative secure working arrangements. If local agreement cannot be reached the engagement team should refer the issue to the NAO's Head of Information Security.

Data protection legislation

24.30 Statutory safeguards are provided by the Data Protection Act 2018 and the UK General Data Protection Regulation (UK GDPR): (UK GDPR):

- The DPA 2018 sets out the framework for data protection law in the UK. It updates and replaces the Data Protection Act 1998, and came into effect on 25 May 2018. It was amended on 01 January 2021 by regulations under the European Union (Withdrawal) Act 2018, to reflect the UK's status outside the EU. It sits alongside and supplements the UK GD–R - for example by providing exemptions.
- The UK GDPR is a UK law which came into effect on 1 January 2021. It sets out the key principles, rights and obligations for most processing of personal data in the UK, except for law enforcement and intelligence agencies. It is based on the EU GDPR (General Data Protection Regulation (EU) 2016/679) which applied in the UK before that date, with some changes to make it work more effectively in a UK context.

Data policies

24.31 All staff must be familiar with the NAO Security Manual and must formally acknowledge that they have read and understood its contents before they are authorised to use the NAO network.

24.32 In line with the NAO Security Manual, wherever possible or practicable, audited entity data should not be removed from the audited entity's premises in any format. Where a decision is made by the Engagement Director that the data will be transferred, examined, analysed and stored on NAO equipment or premises, it should as soon as practicable be imported to a secure location and deleted from insecure locations. Secure locations are currently AIMS, Apex or secured folders in Sharepoint. Huddle is not for long term storage and data should be deleted as soon as downloaded and placed in a secure location. Bulk data must not be stored in the audit file.

24.33 The use of AIMS is currently mandatory for all medium to high-volume (i.e. greater than 500 records) data obtained from audited entities, regardless of whether low-, medium- or high-sensitivity.

24.34 Team members should not retain any audit-specific information on their personal computers or on transport media such as memory stick.

24.35 Retention of personal data should be in accordance with the NAO's data protection framework. Personal data should be destroyed when no longer required.

Section 8: Financial statements-level procedures

Chapter 25: Group audit procedures

Relevant standards and guidance

25.1 ISA (UK) 600 (Revised September 2022) deals with special considerations that apply to a group audit, including in those circumstances when component auditors are involved.

25.2 Paragraphs 1-186 to 1-196 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 600 in the public sector.

25.3 These requirements apply to all group audits, including where:

- a single individual from the NAO is the Group Engagement Director and also the Engagement Director for all components;
- the Engagement Director for one or more components is a different individual from the Group Engagement Director, but all components are audited by the NAO; or
- another firm or national audit agency is the auditor of one or more components of the group.

Definition of a component

25.4 Paragraph 14(b) of ISA (UK) 600 (Revised September 2022) defines a component as an entity, business unit, function or business activity, or some combination thereof, determined by the group auditor for purposes of planning and performing audit procedures in a group audit.

25.5 The definition of a component is based around the preparation of financial information, rather than the legal structure of the group. Examples of components in the NAO context may be:

- individual subsidiary bodies (such as NDPBs or companies);
- departments or branches; and

- individual functions, processes or services, when financial reporting within the group is organised in this way.

25.6 In some cases, a group will have sub-groups within it (subject to the terms of the relevant designation order – see the FReM for accounting guidance). When this is the case, the group engagement team can identify components at the sub-group level; for example:

- the Department for Culture, Media and Sport group accounts include the BBC, which incorporates a range of subsidiary entities in the BBC's own group accounts; and
- the Department of Health and Social Care group includes a sub-group at the NHS summarised accounts level.

25.7 Component auditors include:

- members of the group engagement team performing work on a component;
- other NAO teams;
- non-NAO teams who have been provided with referral instructions; and
- non-NAO teams who have not been provided with instructions, but whose work is intended to be used in the group audit.

25.8 ***Consultation required*** The approach of performing risk assessment procedures in aggregate for multiple components with a similar inherent risk profile should only be used in relatively limited circumstances where the inherent risk profile is similar across the entities. Prior to adopting such an approach for the first time, the Group Engagement Team should consult FAPQ (if approved for one reporting period, there is no requirement to consult FAPQ in future periods). The approach prescribed by this Manual for large sector consolidations is set out later in this Chapter in the section of ***Table 25I*** entitled 'Identifying and assessing the Risks of Material Misstatement – Aggregating components for risk assessment purposes'.

Leadership responsibilities for a group audit

Table 25A: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Leadership responsibilities for a group audit

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
16 to 16-1	In applying ISA (UK) 220 (Revised July 2021), the group engagement partner is required to take overall responsibility for managing and achieving quality on the	For NAO audits, the Engagement Director for the group audit (the Group Engagement Director) fulfils the role of the group engagement partner. The Group Engagement Director, in the role of group engagement partner, is

	group audit engagement. In doing so, the group engagement partner shall: (a) take responsibility for creating an environment for the group audit engagement that emphasises the expected behaviour of engagement team members; (b) be sufficiently and appropriately involved throughout the group audit engagement, including in the work of component auditors, such that the group engagement partner has the basis for determining whether the significant judgments made, and the conclusions reached, are appropriate given the nature and circumstances of the group audit engagement. In the UK, the group engagement partner shall bear overall responsibility for compliance with the requirements of ISA (UK) 600 (Revised September 2022), and all ISAs (UK) relevant to the audit, including those requirements related to engagement performance and for ensuring that the auditor's report issued is appropriate in the circumstances. The group engagement partner's firm shall bear overall responsibility for the design, implementation, and operation of a system of quality management that supports the group engagement partner in fulfilling their responsibilities.	responsible for the direction, supervision and performance of the group audit engagement in compliance with professional standards and applicable legal and regulatory requirements, and whether the auditor's report that is issued is appropriate in the circumstances. The Group Engagement Director, as group engagement partner, is a Key Audit Partner in accordance with paragraph 14(j) of ISA (UK) 600 (Revised September 2022). The Group Engagement Team should also designate a Key Audit Partner from each component auditor for material subsidiaries, in accordance with paragraph 14(n) of ISA (UK) 600 (Revised September 2022). This is interpreted as applying to all components where there is a balance on an individual class of transactions, account balance or disclosure which is larger than materiality for the group financial statements as a whole.

Engagement acceptance and continuance

Table 25B: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Engagement acceptance and continuance

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
17 to 18	Before accepting or continuing the group audit engagement, the group engagement partner shall determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained to provide a basis for forming an opinion on the group financial statements. If, after the acceptance or continuance of the group audit engagement, the group engagement partner concludes that sufficient appropriate audit evidence cannot be obtained, the group engagement partner shall consider the possible effects on the group audit.	**Acceptance and continuance** In determining whether to accept or continue with an engagement, the Group Engagement Director should determine whether sufficient appropriate audit evidence can reasonably be expected to be obtained in relation to the consolidation process and the financial information of the components on which to base the group audit opinion. In particular, Group Engagement Teams should consider whether they: • will have unrestricted access to those charged with governance of the group, group management, those charged with governance of the component, component management, component information, and the component auditors (including relevant audit documentation sought by the group engagement team); and • will be able to perform necessary work on the financial information of the components.
19	In applying ISA (UK) 210 (Revised June 2016) (Updated May 2022), the group auditor shall obtain the agreement of group management that it acknowledges and understands its responsibility to provide the engagement team with: (a) access to all information of which group management is aware that is relevant to the preparation of the group financial statements such as records, documentation and other matters;	**Terms of the engagement** The terms described in paragraph 19 of ISA (UK) 600 (Revised September 2022) are incorporated into the template Letter of Understanding/Engagement.

	(b) additional information that the engagement team may request from group management or component management for the purpose of the group audit; and (c) unrestricted access to persons within the group from whom the engagement team determines it necessary to obtain audit evidence.	
20	If the group engagement partner concludes that group management cannot provide the engagement team with access to information or unrestricted access to persons within the group due to restrictions that are outside the control of group management, the group engagement partner shall consider the possible effects on the group audit.	**Restrictions on access to information or people outside the control of group management** ***Consultation required*** Where the Group Engagement Team is unable to obtain or gain access to a component auditor's working papers for the purposes of the group audit, they should consult FAPQ, as there may be a requirement to refer the matter to the Financial Reporting Council.
21	If the group engagement partner concludes that: (a) it will not be possible for the group auditor to obtain sufficient appropriate audit evidence due to restrictions imposed by group management; and (b) the possible effect of this limitation will result in a disclaimer of opinion on the group financial statements, the group engagement partner shall either: (i) in the case of an initial engagement, not accept the engagement, or, in the case of a recurring engagement, withdraw from the engagement, when withdrawal is possible under applicable law or regulation; or (ii) when law or regulation prohibit an auditor from declining an engagement or when withdrawal from an engagement is	**Restrictions on access to information or people imposed by group management** ***Consultation required*** Where the Group Engagement Team becomes aware of restrictions imposed by group management which may impede them from obtaining sufficient appropriate audit evidence, they should consult FAPQ, as there may be a requirement to refer the matter to the Financial Reporting Council.

	not otherwise possible, having performed the audit of the group financial statements to the extent possible, disclaim an opinion on the group financial statements.	

Overall group audit strategy and group audit plan

Table 25C: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Overall group audit strategy and group audit plan

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
22	In applying ISA (UK) 300 (Revised June 2016) (Updated May 2022), the group auditor shall establish, and update as necessary, an overall group audit strategy and group audit plan. In doing so, the group auditor shall determine: (a) the components at which audit work will be performed; and (b) the resources needed to perform the group audit engagement, including the nature, timing and extent to which component auditors are to be involved.	**Overall group audit strategy and group audit plan** The group audit plan should be documented through: • the Group Audit Risk Assessment Scoping Template (GARAST); • the Group Risk Assessment in Apex; and • any additional Risk Assessments added within Apex used by the Group Engagement Team to perform risk assessment activity over components. The output of the GARAST: • informs the parameters to be entered into the Group Risk Assessment; • informs risk assessment activities which are performed by component auditors for the purpose of the group audit; and • records the outcome of risk assessment activities which are performed on component financial information by both the group auditor and component auditors for the purpose of the group audit.

		Overall group audit strategy and group audit plan – stand-back assessment The Group Engagement Team should perform a stand-back assessment upon completion of the group audit plan (principally the GARAST), which involves considering whether the identified significant risks at the group level are appropriately addressed in the group audit plan. The Group Engagement Team should document their stand-back assessment within the GARAST, including: • tab 'C2. FRA Level Standback' (stand-back assessment on the group risk assessment scoping at COTABD level); and • tab 'D2. FRA Group Standback' (stand-back assessment on the overall group audit risk assessment). The stand-back assessment on the group audit plan should be a top-down assessment of how the risks of material misstatement of the group accounts are addressed in the group audit plan. As part of this assessment, the Group Engagement Team should ensure that the procedures set out in the group audit plan incorporate sufficient coverage to provide assurance over each material COTABD in the group accounts. If the Group Engagement Team does not consider that the identified significant risks at the group level are appropriately addressed in the group audit plan, they should design additional audit procedures to be performed by the Group Engagement Team to address these risks and update the group audit plan to reflect these. The Group Engagement Director should be involved in the stand-back assessment set out in this section.

23 to 24	In establishing the overall group audit strategy and group audit plan, the group engagement partner shall evaluate whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor. As part of this evaluation, the group auditor shall request the component auditor to confirm that the component auditor will cooperate with the group auditor, including whether the component auditor will perform the work requested by the group auditor.	**Early consideration of component auditors' planned responses** The quality of a group audit is dependent upon the quality of the work performed upon the components of the group, which will depend upon the professional competence of the component auditor, their independence, and appropriate interaction with the group engagement team. If component auditors do not appropriately address significant risks to the group financial statements, then there will not be an appropriate basis for the group audit opinion. It is therefore essential that the Group Engagement Director and Group Engagement Manager consider as early as possible: • what are the significant risks to the group financial statements; • who are the component auditors; • based on the Group Engagement Team's understanding of the component auditors and the risks, what involvement is needed in their work; and • whether the component auditors' planned responses which are relevant for group purposes are appropriate for the purposes of the group audit. This will enable the group engagement team to establish effective communication with component auditors. **Evaluating whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor** A confirmation from component auditors that the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor is built into the Group Audit Instructions template. The Group Engagement Director's evaluation of whether the group auditor will be able to be sufficiently and appropriately involved in the work of the component auditor should take into account component auditors' responses to this requested confirmation.

		Considerations when component auditors are involved Forms of involvement in component auditors' work should include one or more of the following: • meeting with component management or the component auditors to obtain an understanding of the component and its environment; • reviewing the component auditors' overall audit strategy and audit plan; • performing risk assessment procedures to identify and assess the risks of material misstatement or irregularity at the component level. These may be performed with the component auditors, or by the group engagement team; • designing and performing further controls or substantive procedures. These may be designed and performed with the component auditors, or by the group engagement team; • participating in the closing and other key meetings between the component auditors and component management; and/or • reviewing other relevant parts of the component auditors' audit documentation. The Group Engagement Team should document their evaluation and review of the work performed by the component auditor for the purpose of the group audit (as required by paragraph 51-1(a) of ISA (UK) 600 (Revised September 2022)) within a 'Using the work of component auditors' Audit Response Group in Apex for each component where the Group Engagement Team plans to use any part of the component auditor's risk assessment. Where the Group Engagement Team plans to obtain assurance from the work of component auditors, they must ensure that the reporting timetable for the audit of the component is sufficient to meet the needs of the group reporting timetable. Where the component auditor is unable to meet the reporting timetable for the

		group, the Group Engagement Team will need to perform alternative procedures to obtain assurance over the financial information of the component for the purposes of the group audit. Good early communication with the component auditors about their planned responses to risks is important, as it reduces the risk of additional work being required after the completion of the component auditor's work. The Group Engagement Team may wish to mitigate such risks by reviewing component auditors' risk assessment activity at an early stage – this, combined with issuing a second set of Group Audit Instructions after the Group Engagement Team's review of the component auditor's risk assessment is complete (and before work on responses is carried out), may mean that component auditors' initial scope of work is more aligned to the Group Engagement Team's expectations and therefore less likely to require additional follow up work. Additional testing may be difficult to arrange and unwelcome to the audited entity, particularly if the component auditor has already issued their statutory audit report, or the requirement comes from another audit body. As set out in paragraph A43-1 of ISA (UK) 600 (Revised September 2022), there are statutory obligations on UK-based corporate subsidiary undertakings, and their auditors and other parties, to provide the auditor of a corporate parent undertaking with such information and explanations as that auditor may reasonably require for the purposes of the audit. These requirements also extend to central government entities. Where there is no such statutory obligation (e.g. for non-corporate entities and overseas subsidiary undertakings), permission may be needed by the auditors of the subsidiary undertakings, from those charged with governance of the subsidiary undertakings, to disclose information to the auditor of the parent undertaking. Permission may also be

		needed from those charged with governance of the subsidiary undertakings for the auditor of the parent undertaking to pass those disclosures on to those charged with governance of the parent undertaking. The auditor of the parent undertaking seeks to ensure that appropriate arrangements are made at the planning stage for these disclosures. Normally, such arrangements for groups are recorded in the instructions to the auditors of subsidiary undertakings and relevant engagement letters.

Relevant ethical requirements, including those related to independence

Table 25D: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Relevant ethical requirements, including those related to independence

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
25 to 25-1	In applying ISA (UK) 220 (Revised July 2021), the group engagement partner shall take responsibility for: (a) component auditors having been made aware of relevant ethical requirements that are applicable given the nature and circumstances of the group audit engagement; and (b) confirming whether the component auditors understand and will comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement. In the UK, this shall include obtaining confirmation from the component auditors that they are able to comply with the requirements of the	**Relevant ethical requirements, including those related to independence** The confirmations described in paragraph 25 of ISA (UK) 600 (Revised September 2022) are built into the Group Audit Instructions templates. ***Consultation required*** The template also outlines a mechanism for component auditors to report any breaches of the FRC's Revised Ethical Standard or other ethical considerations relevant to the group audit to the Group Engagement Director for consideration. The Group Engagement Team should report any such breaches notified by component auditors to the Ethics Function. ***Consultation required*** Template Group Audit Instructions for 2024-25 audits include a request for confirmation that component auditors will comply with the Revised Ethical Standard 2024. This reflects the NAO's policy choice to apply

	FRC's Revised Ethical Standard that are relevant to the group audit engagement. Prior to dating the auditor's report, the group engagement partner shall take responsibility for obtaining confirmation from the component auditors that the ethical requirements that are relevant to the group audit engagement, including those related to independence, have been fulfilled.	the Revised Ethical Standard 2024 to all 2024-25 audits regardless of the engagement start date. However, it is possible that a component auditor will continue to apply the Revised Ethical Standard 2019 where the engagement for the audit of the component commenced prior to 15 December 2024 – in these circumstances, they would not be able to provide the requested confirmation. If a component auditor declines to confirm that they will comply with the Revised Ethical Standard 2024, the Group Engagement Team should consult FAPQ.

Engagement resources

Table 25E: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Engagement resources

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
26 to 27	In applying ISA (UK) 220 (Revised July 2021), the group engagement partner shall: (a) determine that component auditors have the appropriate competence and capabilities, including sufficient time, to perform the assigned audit procedures at the component; and (b) if information about the results of the monitoring and remediation process or external inspections related to the component auditor has been provided by the group auditor's firm or has otherwise been made available to the group engagement partner, determine the relevance of such information to the group auditor's determination in (a) above.	**Component auditors' competence and capabilities, including sufficient time** In completing the assessment required by paragraph 26(a) of ISA (UK) 600 (Revised September 2022), the group auditor should draw on information available at the firm level for the component auditor, but the assessment should be sufficiently granular to facilitate a consideration of the skills and capabilities of the particular individuals performing audit work in support of the group audit opinion. In the case of large sector consolidation exercises, the evaluation should initially be drawn at the firm level, with consideration on a more granular basis as part of any file review exercises. The consideration of capabilities and competencies of the component auditor should include:

	The group auditor shall obtain sufficient appropriate audit evidence relating to the work to be performed at the component without involving the component auditor if: (a) the component auditor does not comply with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement; or (b) the group engagement partner has serious concerns about the matters in paragraphs 23–26 of ISA (UK) 600 (Revised September 2022).	• any specialist skills required by the component auditor; • the use of experts by the component auditor; and • whether the component auditor has sufficient resourcing to be able to complete the work required to support the group audit opinion in line with the timetable. **Quality management relating to component auditors** FAPQ will issue central communications to Group Engagement Teams to enable them to assess information about the monitoring and remediation process or external inspections related to component auditors which are either contractor audit firms for NAO audits or which perform audit work under the Code of Audit Practice. For individual component auditors which are not captured through this process, the Group Engagement Team should: • review publicly-available reports on the component auditor from the Financial Reporting Council's Audit Quality Review team and from the Institute of Chartered Accountants in England and Wales's Quality Assurance Department, using the Component Auditor External Reporting Review template to document this review; and • request a copy of the firm's own evaluation of the firm's system of quality management (performed under paragraph 53 of ISQM (UK) 1) and review this if provided. The Group Engagement Team is only required to review information on quality management matters relating to component auditors which is available to the Group Engagement Team. If no information is available from external reporting and a component auditor declines to share the firm's own evaluation of the firm's system of quality management with the Group Engagement Team, then the Group Engagement Team should treat the component auditor as subject to a

		greater degree of quality risk and document how they will respond to the greater risk – such a response may include a closer review of the component auditor's work, which may be performed by more senior NAO staff than would otherwise be the case. ***Consultation required*** The Group Engagement Team should report any concerns arising from their consideration of the work of the component auditor as an Apex Consultation (system of quality management report) for consideration as part of the monitoring and remediation process in accordance with paragraph 39 of ISA (UK) 220 (Revised July 2021).

Engagement performance

Table 25F: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Engagement performance

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
28	In applying ISA (UK) 220 (Revised July 2021), the group engagement partner shall take responsibility for the nature, timing and extent of direction and supervision of component auditors and the review of their work, taking into account: (a) areas of higher assessed risks of material misstatement of the group financial statements, or significant risks identified in accordance with ISA (UK) 315 (Revised July 2020); and (b) areas in the audit of the group financial statements that involve significant judgement.	**Direction, supervision and review of the work of component auditors** The Group Engagement Director should document how they will exercise their responsibilities for direction, supervision and review of the work of component auditors. Actions which may be taken to exercise these responsibilities include: • attendance at risk assessment discussions with component auditors; • issuing Group Audit Instructions which have been reviewed by the Group Engagement Director prior to issue; • review of component auditor working papers; and • ongoing discussions with component auditors during their work.

		Areas of work performed by component auditors which require direct supervision and review by the Group Engagement Director in order to discharge their ISA (UK) 220 (Revised July 2021) responsibilities include: • where a significant risk is contained within a single component and the component auditor is directly performing the risk assessment and response on behalf of the group; • where a significant risk is being addressed entirely by component auditors. • where a significant accounting estimate is being addressed by component auditors; or • where a matter considered centrally by the group auditor is affected or informed by work performed by a component auditor. Where a significant risk, significant judgement or significant accounting estimate is relevant to multiple components, the Group Engagement Director should use their professional judgement on the extent to which they should review the work of the various component auditors for these components. At a minimum, the Group Engagement Director should directly review the underlying work on the risk, judgement or accounting estimate performed by a reasonably representative selection of at least two components (giving consideration to rotating the components reviewed between reporting periods). The Group Engagement Director should be satisfied that they have directly reviewed sufficient component auditor work on the risk, judgement or accounting estimate such that the Group Engagement Director has the basis for determining that the significant judgements made and the conclusions reached are appropriate given the nature and circumstances of the work performed for the purpose of the group audit. Where risk assessment activities are performed directly by the component auditor, the Group Engagement Director should document their review of the component auditor's risk assessment in one of the following ways:

		• The Group Engagement Team retains the component auditor's risk assessment documentation on the group audit file, along with evidence of Group Engagement Director review. • The Group Engagement Director reviews the risk assessment performed by the component auditor directly on the component auditor's file and adds evidence that they have done so onto the group audit file. • A member of the Group Engagement Team reviews the component auditor's risk assessment and documents a detailed summary of this on the group file. The Group Engagement Director also discusses the risk assessment with the component auditor. Documentation of both the review of the risk assessment and the Group Engagement Director's discussion of the risk assessment is held on the group audit file. The Group Engagement Director should document their review of fieldwork performed by the component auditor for the purpose of the group audit in one of the following ways: • The Group Engagement Team retains the component auditor's fieldwork working papers on the group audit file, along with evidence of Group Engagement Director review. • The Group Engagement Director reviews the component auditor's fieldwork working papers directly on the component auditor's file and adds evidence that they have done so onto the group audit file. • A member of the Group Engagement Team reviews the component auditor's fieldwork working papers and documents a detailed summary of these on the group file. The Group Engagement Director also discusses the work performed and its outcome with the component auditor. Documentation of both the review of the work performed and the Group Engagement Director's discussion of the work is held on the group audit file.

		The Group Engagement Director should complete the relevant checklist at the conclusion stage of the audit to document they have discharged their responsibilities for direction, supervision, and review of the work of component auditors performed for the purpose of the group audit.

Communications with component auditors

Table 25G: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Communications with component auditors

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
29 to 29-1	The group auditor shall communicate with component auditors about their respective responsibilities and the group auditor's expectations, including an expectation that communications between the group auditor and component auditors take place at appropriate times throughout the group audit. The group auditor shall request the agreement of the component auditor to the transfer of relevant documentation during the conduct of the group audit as a condition of the use by the group auditor of the work of the component auditor.	**Communications with component auditors** The Group Engagement Team should prepare Group Audit Instructions using the appropriate template. The draft Group Audit Instructions must be reviewed by the Group Engagement Director, in order to demonstrate their fulfilment of their direction responsibilities under ISA (UK) 220 (Revised July 2021). The template Group Audit Instructions reflect the following expectations of the Group Engagement Team: • the (Principal) Accounting Officer is responsible for the group financial statements as a whole (or, for companies, the board is responsible); • the communication between the Group Engagement Team and the component auditors should be unrestricted to the extent possible under law or regulation; • important communications between the component auditors, those charged with governance of the component, and component management, including communications on significant deficiencies in

		internal control, should additionally be communicated to the Group Engagement Team; • important communications between regulatory authorities and components related to financial reporting matters should be communicated to the Group Engagement Team; • to the extent the Group Engagement Team considers necessary, they should be permitted access to component information, those charged with governance of components, component management, and the component auditors (including audit documentation sought by the Group Engagement Team); and to the extent the Group Engagement Team considers necessary, it should be permitted to perform work or request a component auditor to perform work on the financial information of the components. The Group Engagement Team should supplement the formal communications required by ISA (UK) 600 (Revised September 2022) with informal discussions with component auditors at appropriate stages throughout the audit.

Understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control

Table 25H: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies	
30 to 32	In applying ISA (UK) 315 (Revised July 2020), the group auditor shall take responsibility for obtaining an understanding of the following: (a) the group and its environment, including:	**Understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control**	

	(i) the group's organisational structure and its business model, including: (a) the locations in which the group has its operations or activities; (b) the nature of the group's operations or activities and the extent to which they are similar across the group; and (c) the extent to which the group's business model integrates the use of IT; (ii) regulatory factors impacting the entities and business units in the group; and (iii) the measures used internally and externally to assess the entities or business units' financial performance; (b) the applicable financial reporting framework and the consistency of accounting policies and practices across the group; and (c) the group's system of internal control, including: (i) the nature and extent of commonality of controls; (ii) whether, and if so, how, the group centralizes activities relevant to financial reporting; (iii) the consolidation process used by the group, including sub-consolidations, if any, and consolidation adjustments; and (iv) how group management communicates significant matters that support the preparation of the group financial statements and related financial reporting responsibilities in the information system and other components of the	The Group Engagement Team should obtain an understanding of the group's components and their environments to assist in identifying risks of material misstatement at the group level. This should be documented in the groups sections of the Understanding the Entity and Its Environment and Understanding the Entity's System of Internal Control templates. In gathering the information to build up that understanding, the Group Engagement Team may wish to discuss relevant matters pertaining to the group with group management, component management and component auditors. **Understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control – assurance from group-wide controls** If the Group Engagement Team plans to take assurance from group-wide controls, either they or component auditors should test the operating effectiveness of these controls. Group-wide controls may provide assurance over the Group Engagement Team's work on the consolidation process or on the financial information of components. **Understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control – Group Engagement Team discussion on risk and fraud** As described in paragraph A91 of ISA (UK) 600 (Revised September 2022), in applying ISA (UK) 315 (Revised July 2020), the group engagement partner and other key Group Engagement Team members are required to discuss the application of the applicable financial reporting framework and the susceptibility of the group's financial statements to material misstatement. The group engagement partner's determination of which members of the Group Engagement Team to include in the discussion and the topics to be discussed, is affected by matters such as initial expectations about the risks of material	

	group's system of internal control to management of entities or business units. The group auditor shall communicate to component auditors on a timely basis: (a) matters that the group auditor determines to be relevant to the component auditor's design or performance of risk assessment procedures for purposes of the group audit; (b) in applying ISA (UK) 550 (Updated May 2022), related party relationships or transactions identified by group management, and any other related parties of which the group auditor is aware, that are relevant to the work of the component auditor; and (c) in applying ISA (UK) 570 (Revised September 2019) (Updated May 2022), events or conditions identified by group management or the group auditor, that may cast significant doubt on the group's ability to continue as a going concern that are relevant to the work of the component auditor. The group auditor shall request component auditors to communicate on a timely basis: (a) matters related to the financial information of the component that the component auditor determines to be relevant to the identification and assessment of the risks of material misstatement of the group financial statements, whether due to fraud or error; (b) related party relationships not previously identified by group management or the group auditor; and	misstatement and the preliminary expectation of whether to involve component auditors (see following paragraph). The Group Engagement Team should communicate, through Group Audit Instructions to component auditors: • matters relating to fraud which the Group Engagement Director considers appropriate to communicate to component auditors; and • a request that component auditors communicate matters relating to fraud to the Group Engagement Team. As described in paragraph A92 of ISA (UK) 600 (Revised September 2022), the discussion provides an opportunity to: • Share knowledge of the components and their environments, including which components' activities are centralised. • Exchange information about the business risks of the components or the group, and how inherent risk factors may affect susceptibility to misstatement of classes of transactions, account balances and disclosures. • Exchange ideas about how and where the group financial statements may be susceptible to material misstatement due to fraud or error. ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires the engagement team discussion to place particular emphasis on how and where the entity's financial statements may be susceptible to material misstatement due to fraud, including how fraud may occur. • Identify policies followed by group or component management that may be biased or designed to manage earnings that could lead to fraudulent financial reporting. • Consider known external and internal factors affecting the group that may create an incentive or pressure for group management, component management, or others to commit fraud, provide the opportunity for fraud to be perpetrated, or indicate a culture or environment that enables	

	(c) any events or conditions identified by the component auditor that may cast significant doubt on the group's ability to continue as a going concern.	group management, component management, or others to rationalise committing fraud. • Consider the risk that group or component management may override controls. • Discuss fraud that has been identified, or information that indicates existence of a fraud. • Identify risks of material misstatement relevant to components where there may be impediments to the exercise of professional scepticism. • Consider whether uniform accounting policies are used to prepare the financial information of the components for the group financial statements and, if not, how differences in accounting policies are identified and adjusted (when required by the applicable financial reporting framework). • Share information about risks of material misstatement of the financial information of a component that may apply more broadly to some, or all, of the other components. • Share information that may indicate non-compliance with national laws or regulations, for example, payments of bribes and improper transfer pricing practices. • Discuss events or conditions identified by group management, component management or the Group Engagement Team that may cast significant doubt on the group's ability to continue as a going concern. • Discuss related party relationships or transactions identified by group management or component management, and any other related parties of which the Group Engagement Team is aware. **Understanding the group and its environment, the applicable financial reporting framework and the group's system of internal control – groups without a parent entity managed on a single entity basis** Some group financial statements audited by the NAO represent aggregations of whole sector information and are therefore managed on a single entity basis	

		rather than a group basis. In such a scenario, components of the system of internal control (for example risk assessment) may not exist at the group-level. The absence of a component of the system of internal control at group-level in such cases does not automatically equate to a significant deficiency in internal control. In this scenario, in assessing whether a significant deficiency in internal control exists, the Group Engagement Team should consider the context of the group and whether equivalent controls may be in place at component level.	

Identifying and assessing the Risks of Material Misstatement

Table 25l: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Identifying and assessing the Risks of Material Misstatement

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
33 to 34	In applying ISA (UK) 315 (Revised July 2020), based on the understanding obtained in paragraph 30 of ISA (UK) 600 (Revised September 2022), the group auditor shall take responsibility for the identification and assessment of the risks of material misstatement of the group financial statements, including with respect to the consolidation process. In applying ISA (UK) 315 (Revised July 2020), the group auditor shall evaluate whether the audit evidence obtained from the risk assessment procedures performed by the group auditor and component auditors provides an appropriate basis for the identification and assessment of	**Identifying and assessing the Risks of Material Misstatement** The Group Engagement Team should undertake the identification and assessment of risks of material misstatement of the group financial statements in the following three stages: 1. Scoping the areas of the group financial statements which should be subject to risk assessment. 2. Scoping the components which need to be considered as part of the risk assessment: a. at the financial statements level; and b. at the assertion level. 3. Stand-back assessments to overlay group considerations and coverage

	the risks of material misstatement of the group financial statements.	This scoping should be documented within the Group Audit Risk Assessment Scoping template (GARAST). **Identifying and assessing the Risks of Material Misstatement – scoping the group financial statements** Based upon a review of the group financial statements, the Group Engagement Team should: • document whether each Financial Statements Risk Area (FSRA) is relevant at the group level and document this within the GARAST (tab 'A. FSRA Group Audit Approach'); and • record scoping values for each class of transactions, account balance and disclosure (COTABD) and document this within the GARAST (tab 'C1. FRA Component Scoping'). **Identifying and assessing the Risks of Material Misstatement – financial statements-level risks – group-level** For FSRAs relating to risks managed at the level of the group financial statements which cannot be directly linked to a component, the Group Engagement Team must directly perform the risk assessment, but with information or assistance from component auditors where appropriate. The Group Engagement Team should document in the GARAST (tab 'A. FSRA Group Audit Approach') whether each FSRA is relevant at the group level and if so that they have been appropriately scoped into the Group Risk Assessment. **Identifying and assessing the Risks of Material Misstatement – financial statements-level risks – specific components**

		For FSRAs relating to risks which arise within individual components which may be material to the group financial statements as a whole, the Group Engagement Team should document the relevant component and whether these will be risk assessed by the component auditor or the Group Engagement Team. The Group Engagement Team should ensure the list of such FRSAs is complete: for example, through discussions with component auditors and group management, work performed to understand the group and its environment, and review of returns received from component auditors. This should be documented in the GARAST (tab 'A. FSRA Group Audit Approach'). **Identifying and assessing the Risks of Material Misstatement – financial statements-level risks – management override of controls** The Group Engagement Team should scope in the management override of controls FSRA within the Group Risk Assessment. The resulting Risk of Material Misstatement addresses the consideration of management override of controls risks at the component level, which the Group Engagement Team should consider for all components for which any element has been scoped in for risk assessment purposes. **Identifying and assessing the Risks of Material Misstatement – financial statements-level risks – going concern** Where group financial statements are prepared without a parent entity (for example, sector consolidations), the Group Engagement Team should scope in the going concern FSRA, following the approach for group-level FSRAs described above. **Identifying and assessing the Risks of Material Misstatement – financial statements-level risks – laws and regulations**

		The Group Engagement Team should consider the laws and regulations FSRA both at the group level, following the approach for group-level FSRAs described above, and at the component level following the approach for specific components described above. **Identifying and assessing the Risks of Material Misstatement – scoping the components at the assertion level** The Group Engagement Team should document their assertion-level risk assessment scoping within the GARAST (tab 'C1. FRA Component Scoping'). The Group Engagement Team should scope in COTABDs at the group-level either by value (where the COTABD scoping value for the group exceeds group performance materiality, or the level of group performance materiality applied to that particular COTABD) or judgementally (for example, due to qualitative materiality considerations). The Group Engagement Team should then determine whether each COTABD will be: • risk assessed by the Group Engagement Team on an aggregated basis – the related FRAs should be scoped into the Group Risk Assessment in Apex; or • risk assessed at the component level – these should be scoped in at component level either by value (where the COTABD scoping value for the component exceeds component performance materiality) or judgementally. The Group Engagement Team may scope in a COTABD for a component for Estimates RoMMs only or for Completeness RoMMs only. The Group Engagement Team should determine whether the risk assessment at the component level should be performed by:

		o the Group Engagement Team – the Group Engagement Team should scope in the relevant FRA for risk assessment against the relevant component within the Group Risk Assessment or (where multiple FRAs need to be risk assessed by the group auditor for a single component) in a separate Risk Assessment in Apex; or o the component auditor – the Group Engagement Team should instruct the component auditor to perform the relevant risk assessment (and associated responses where relevant) within the Group Audit Instructions. **Identifying and assessing the Risks of Material Misstatement – linking financial statements-level risks to assertion-level risks** Paragraph 30(a) of ISA (UK) 315 (Revised July 2020) requires that for identified risks of material misstatement at the financial statement level, the auditor shall assess the risks and determine whether such risks affect the assessment of risks at the assertion level. The Group Engagement Team should document such links between financial statements-level RoMMs and assertion-level RoMMs within the GARAST (tab 'A. FSRA Group Audit Approach'). The Group Engagement Team should review each identified financial statements-level RoMM and note any which have an impact on a Financial Reporting Activity (FRA) or class of transactions, account balance or disclosure (COTABD), and which components would be affected. These links should be factored into the assertion-level risk assessment as follows: • For components where the Group Engagement Team is performing the assertion-level risk assessment: The Group Engagement Team should

		either manually increase the Likelihood weighting of the relevant RoMMs or else justify why this is not required. • For components where the component auditor is performing the assertion-level risk assessment: The Group Engagement Team should request (via the Group Audit Instructions) that the component auditor considers the impact of the financial statement level risk assessment on their individual assertion-level risk assessment and provide the group auditor with an explanation of how this has been done. The Group Engagement Director should review the risk assessment activity performed by the component auditor and document this as set out in ***Table 25F*** above. **Identifying and assessing the Risks of Material Misstatement – Completeness and Estimates Standback** Having completed component-level scoping, the Group Engagement Team should undertake a stand-back assessment on estimates and completeness risks associated with elements of the group financial statements which are not scoped in through the above process. They should document this work within the GARAST (tab 'C2. FRA Level Standback'). If there are any individual components which contain material estimates or completeness risks to the group financial statements which have not been scoped in for risk assessment, they should be scoped in at the group level in respect of estimates or completeness risks only, as appropriate. The Group Engagement Team should then consider whether the total areas not scoped in for estimates and completeness risks contain estimates or completeness risks in aggregate which are material to the group financial statements – if so, then the Group Engagement Team should scope in further

		components for estimates and completeness purposes until the risk is reduced to an acceptable level. **Identifying and assessing the Risks of Material Misstatement – Component Standback** The Group Engagement Team should review the number of COTABDs scoped in against each component and consider whether this is appropriate based on their understanding of the component. They should document this work within the GARAST (tab 'C3. FRA Component Standback'). **Identifying and assessing the Risks of Material Misstatement – FRA-level Standback** The Group Engagement Team should consider the possibility of aggregation risk arising from multiple low-level risks aggregating to a significant risk at the group level. This should be documented in tab 'D2. FRA Group Standback' of the GARAST for each COTABD and component which has been scoped in for risk assessment purposes. The Group Engagement Team should consider the following in performing the FRA-level Standback: • whether any significant risks raised at a component level which are not individually a significant risk to the group constitute a significant risk to the group in aggregate when similar significant risks are raised in multiple components; • whether any matters not raised as a significant risk at individual components but occurring multiple times across the group aggregate into a significant risk at group level when considered in aggregate; and

		• whether the planned procedures across the group are sufficient and appropriate to support the group opinion as a whole for the COTABD or component. **Identifying and assessing the Risks of Material Misstatement – Aggregating components for risk assessment purposes** ***Consultation required*** As set out in the section earlier in this Chapter entitled 'Definition of a component', the approach of performing risk assessment procedures in aggregate for multiple components with a similar inherent risk profile should only be used in relatively limited circumstances where the inherent risk profile is consistent across the entities which are being aggregated for risk assessment purposes. Prior to adopting such an approach for the first time, the Group Engagement Team should consult FAPQ (if approved for one reporting period, there is no requirement to consult FAPQ in future periods). The Group Engagement Team should justify why the aggregated components have a materially similar inherent risk profile, with reference to their understanding of the group and its components. Factors which may indicate that it is not appropriate to aggregate components for risk assessment purposes may include: • significantly different approaches taking to valuing property estates; • pension schemes with different characteristics across different components; or • components operating in different jurisdictions. With appropriate justification, the Group Engagement Team may aggregate components for risk assessment purposes across the financial statements as a whole or across particular COTABDs or a combination of COTABDs.

		Identifying and assessing the Risks of Material Misstatement – Performing risk assessment procedures at the component level Where a COTABD or FSRA has been scoped in and the risk assessment is performed by the component auditor, the Group Engagement Team should review this risk assessment activity (see ***Table 25F*** above and ***Table 25N*** below). Where a COTABD or FSRA has been scoped in and the risk assessment is performed by the Group Engagement Team (appropriate for risks managed at the group level or for components where either there is no component auditor or where the Group Engagement Team has determined that they are unable to place reliance upon the work of component auditor), the Group Engagement Team should scope in the COTABD or FSRA to the Group Risk Assessment.

Materiality

Table 25J: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Materiality

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
35 to 36	In applying ISA (UK) 320 (Revised June 2016) (Updated May 2022) and ISA (UK) 450 (Revised June 2016) (Updated May 2022), when classes of transactions, account balances or disclosures in the group financial statements are disaggregated across components, for purposes of planning and performing audit procedures, the group auditor shall determine:	**Materiality and performance materiality** The Group Engagement Team should determine materiality and performance materiality for the group financial statements as a whole in accordance with ISA (UK) 320 (Revised June 2016) (Updated May 2022) and Chapter 16: Materiality, performance materiality and trivial threshold. **Component performance materiality**

	(a) component performance materiality. To address aggregation risk, such amount shall be lower than group performance materiality; and (b) the threshold above which misstatements identified in the component financial information are to be communicated to the group auditor. Such threshold shall not exceed the amount regarded as clearly trivial to the group financial statements. The group auditor shall communicate to the component auditor the amounts determined in accordance with the previous paragraph.	As defined in paragraph 14(e) of ISA (UK) 600 (Revised September 2022), component performance materiality is an amount set by the group auditor to reduce aggregation risk to an appropriately low level for purposes of planning and performing audit procedures in relation to a component. As defined in paragraph 14(a) of ISA (UK) 600 (Revised September 2022), aggregation risk is the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. As described in paragraph A118 of ISA (UK) 600 (Revised September 2022), the determination of component performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. Factors the group auditor may take into account in setting component performance materiality include the following: • The extent of disaggregation of the financial information across components (e.g., as the extent of disaggregation across components increases, a lower component performance materiality ordinarily would be appropriate to address aggregation risk). The relative significance of the component to the group may affect the extent of disaggregation (e.g., if a single component represents a large portion of the group, there likely may be less disaggregation across components). • Expectations about the nature, frequency, and magnitude of misstatements in the component financial information, for example: o Whether there are risks that are unique to the financial information of the component (e.g., industry-specific accounting matters, unusual or complex transactions). o The nature and extent of misstatements identified at the component in prior audits. Where performance materiality relating to the materiality levels determined for particular classes of transactions, account balance or disclosure differs from

		performance materiality for the group financial statements as a whole, the Group Engagement Team may correspondingly set additional specific levels of component performance materiality. The Group Engagement Team should document their consideration of aggregation risk and their determination of component performance materiality for each component within the GARAST ('B. Component PM' tab). **Determining aggregation risk and Component Performance Materiality Starting Point** The Group Engagement Team should document their consideration of the following factors affecting aggregation risk in tab 'B. Component PM' of the GARAST, including whether these factors are 'Low', 'Medium' or 'High' risk for the group: • Factor 1: Size of the group • Factor 2: Distribution of group balances between components • Factor 3: First year of audit • Factor 4: Material errors in the prior period • Factor 5: Significant deficiencies in group internal controls • Factor 6: Number of material COTABDs The GARAST will provide a suggested overall level of aggregation risk for the group as 'Low', 'Medium' or 'High', depending on the risk levels assigned to the individual factors considered above. The suggested overall aggregation risk is based on the aggregate of scores assigned to the risk levels set by the Group Engagement Team for individual factors ('Low' scores 1; 'Medium' scores 5; 'High' scores 10). If the aggregate score across all factors is 12 or less, overall suggested aggregation risk is 'Low'; between 13 and 17, 'Medium'; more than 18, 'High'.

		The Group Engagement Team should set a level of aggregation risk 'Low', 'Medium' or 'High', and may depart from the suggested aggregation risk with appropriate justification, which they should record in the GARAST. The GARAST will provide a suggested Component Performance Materiality Starting Point (the default Component Performance Materiality threshold for components where particular factors do not apply, expressed as a percentage of Group Performance Materiality). The suggested Component Performance Materiality Starting Point is based on the level of aggregation risk set by the Group Engagement Team. The Starting Point for 'Low' aggregation risk is 95%; for 'Medium', 80%; for 'High', 60%. These suggestions are the top of the allowable range for each aggregation risk level (see following paragraph). The Group Engagement Team should set a Component Performance Materiality Starting Point and may set a Starting Point lower than that suggested by the GARAST with appropriate justification, which they should record in the GARAST. ***Consultation required*** The Component Performance Materiality Starting Point should be set within the following ranges: for 'Low' aggregation risk, 80-95%; for 'Medium', 60-80%; for 'High', 40-60%. If the Group Engagement Team proposes to set Component Performance Materiality outside of these ranges, they should consult FAPQ. **Identifying components for which to set a lower Component Performance Materiality** The Group Engagement Team should consider whether any of the following factors are present for any individual components, and document this consideration in tab 'B. Component PM' of the GARAST: • Factor 1: First year of audit • Factor 2: Material errors in the prior period

		• Factor 3: Significant deficiencies in component internal controls • Factor 4: Industry specific accounting matters, unusual or complex transaction, or risks that are unique to the financial information of the component • Factor 5: Any other indicator that a component(s) is subject to higher aggregation risk For components where any of the above factors are present, this suggests an increased aggregation risk relevant to the specific component. The Group Engagement Team should use their professional judgement to determine an amount by which to reduce the Component Performance Materiality (as a percentage of Group Performance Materiality) to reflect each of these factors. **Calculating Component Performance Materiality by component** For each component, the Group Engagement Team should calculate Component Performance Materiality as follows, and document this within the appropriate table in the GARAST tab 'B. Component PM': • For components where no factors have been identified per the previous section entitled 'Identifying components for which to set a lower Component Performance Materiality', the GARAST will suggest a Component Performance Materiality calculated as the Component Performance Materiality Starting Point percentage multiplied by Group Performance Materiality. • For components where particular factors have been identified, the GARAST will suggest a Component Performance Materiality of the lower of: o the reduced Component Performance Materiality Starting Point percentage multiplied by Group Performance Materiality; and o the value of the highest-value COTABD in the component plus £1.

		• ***Consultation required*** The Group Engagement Team may depart from the suggested Component Performance Materiality with appropriate justification recorded in the GARAST, subject to the requirement to consult FAPQ outside of the following ranges: for 'Low' aggregation risk, 80-95%; for 'Medium', 60-80%; for 'High', 40-60%.

Responding to the assessed Risks of Material Misstatement

Table 25K: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Responding to the assessed Risks of Material Misstatement

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
37	In applying ISA (UK) 330 (Revised July 2017) (Updated May 2022), the group auditor shall take responsibility for the nature, timing and extent of further audit procedures to be performed, including determining the components at which to perform further audit procedures and the nature, timing and extent of the work to be performed at those components.	**Responding to the assessed Risks of Material Misstatement** In considering how to respond to risks of material misstatement in the context of a group audit, in addition to considering the nature and timing of the response, the Group Engagement Team should consider: • who performed the risk assessment relating to the risk • who will be performing the audit response • at which components the response be required (where relevant); and • how the responses and the response plan will be documented. The NAO has adopted a number of defined methods (Methods 1 to 5e as outlined below) for how to respond to the assessed Risks of Material Misstatement responses in the context of the audit of group financial statements, how they should be documented in respect of the audit plan and (where relevant) which components will be subject to the response. Which of these options is selected for which risk will depend largely upon the nature of the risk,

		who has performed the risk assessment activity associated with the risk and who will be performing the response. **Responding to the assessed Risks of Material Misstatement – Method 1: Direct reliance on component auditor risk assessments and responses** This method involves the Group Engagement Team reviewing the relevant risk assessment activity performed by the component auditor to confirm that it is appropriate and of sufficient quality to be relied upon for the purposes of the group audit, and also assessing the proposed responses to the risks identified by the component auditor. If the Group Engagement Team identifies that the proposed responses identified by the component auditor will not adequately address the associated risks, then they should select an alternative method from the options listed below. **Responding to the assessed Risks of Material Misstatement – Method 2: Component auditor performs risk assessment and group auditor performs response** ***Consultation required*** Where the component auditor has performed an adequate risk assessment but is unable to perform the responses on a sufficiently timely or appropriate basis to support the delivery of the group audit, the Group Engagement Team may directly perform the responses to the risk at a component level. In these circumstances, the Group Engagement Team should consult with FAPQ as a bespoke response group may be required. **Responding to the assessed Risks of Material Misstatement – Method 3: Group auditor performs risk assessment and response**

		It is expected that this method will be followed for central activities (such as the consolidation process) and also for Financial Reporting Activities (FRAs) at a component level where the Group Engagement Team is performing the work over component financial information directly. It is expected that the following FRAs will be assessed in aggregate by the Group Engagement Team using this method: • Charitable Funds • Charities Disclosures • Charity Income • Financial Instruments Disclosures and Completeness • Operating Segments • Assets Held for Sale and Discontinued Operations • Related Parties • Reserves • Losses and Special Payments (Disclosure only) **Responding to the assessed Risks of Material Misstatement – Method 4: Group auditor performs risk assessment and component auditor performs response on an individual component level** There may be some scenarios where the Group Engagement Team performs a detailed risk assessment over component financial information, but instead of directly performing the responses, the Group Engagement Team commissions the component auditor to perform the responses. **Responding to the assessed Risks of Material Misstatement – Method 5a: Group auditor performs risk assessment at an aggregated level and performs group substantive analytical procedures**

		Paragraph A129 of ISA (UK) 600 (Revised September 2022) envisages the group auditor performing substantive analytical procedures in accordance with ISA (UK) 520 (Updated May 2022). Depending on the circumstances of the engagement, the financial information of the components may be aggregated at appropriate levels for purposes of developing expectations and determining the amount of any difference of recorded amounts from expected values in performing the substantive analytical procedures. The use of automated tools and techniques may be helpful in these circumstances. **Responding to the assessed Risks of Material Misstatement – Method 5b: Group auditor performs risk assessment and response both at an aggregated level** As described in paragraph A129 of ISA (UK) 600 (Revised September 2022), in some cases, it may be possible to obtain sufficient appropriate audit evidence by performing further audit procedures centrally on these significant classes of transactions, account balances or disclosures (e.g., if they are homogeneous, subject to common controls and access to appropriate information can be obtained). **Responding to the assessed Risks of Material Misstatement – Method 5c: Group auditor performs risk assessment at an aggregated level and component auditors all perform response individually at individual component audit level** Under this method, the Group Engagement Team selects an appropriate response to address the associated risk and instructs relevant component auditors to perform the selected response through the Group Audit Instructions. **Responding to the assessed Risks of Material Misstatement – Method 5d: Group auditor performs risk assessment at an aggregated level and**

instructs a sample of component auditors to respond to the risk appropriately and the component auditor has the freedom to design the response

Paragraph A129 of ISA (UK) 600 (Revised September 2022) envisages the group auditor performing further audit procedures at selected components (whilst introducing an element of unpredictability in the components selected for testing) to address the risks of material misstatement of the group financial statements, with the determination of the components at which audit procedures are to be performed, and the nature, timing and extent of further audit procedures to be performed at the selected components, being matters of professional judgement.

Under this method, the Group Engagement Team should select components using the audit sampling principles in ISA (UK) 530 (Updated May 2022). In the NAO's methodology, the attribute substantive sampling frame is applicable to such selections:

Figure 25K(i): Attribute substantive sampling frame for use in selecting samples of component auditors

Material, key and anomalous items	Test 100% and treat any errors found as known	
Assurance required	**No strata present**	**Distinct strata present**
Low assurance	5% by volume (min 5 to max 10)	***Consultation required*** Where distinct audit strata of expected error rates exist in the data then a stratified approach should be adopted – confirm approach with AMT.
Medium assurance	10% by volume (min 10 to max 20)	
High assurance	15% by volume (min 15 to max 40)	

Expected error rate	Sample size per strata
Low	5% by volume (min 5 to max 10)
Medium	10% by volume (min 10 to max 20)
High	15% by volume (min 15 to max 40)

This approach is likely to amount to the Group Engagement Team placing reliance on the work performed by the sampled component auditor in their underlying statutory audit, as the request to be included within the Group Audit Instructions will not specify the procedures to be performed but instead will request assurance over the risks identified.

The Group Engagement Team does not need to plan to perform further work on the unsampled population. However, if errors are identified, it may be necessary to consider the implications across a wider population of components.

Responding to the assessed Risks of Material Misstatement – Method 5e: Group auditor performs risk assessment at an aggregated level and instructs a sample of component auditors to respond to the risk and group auditor directs the response

This method is identical to Method 5d except for instead of requesting the component auditor to perform procedures to address the identified risk of material misstatement, the Group Engagement Team specifies the procedures to be performed.

		This method is likely to be appropriate for highly disaggregated groups consisting of a large number of components. Under this method, the Group Engagement Team should select components using the audit sampling principles in ISA (UK) 530 (Updated May 2022). In the NAO's methodology, the attribute substantive sampling frame (***Figure 25K(i)*** above) is applicable to such selections. **Responding to the assessed Risks of Material Misstatement – IT-related risks** The Group Engagement Team should identify and assess IT-related risks of material misstatement in the same way as for other engagements and if they are planning to rely on group-wide controls, they should evaluate whether they are dependent upon general IT controls and test relevant IT controls as required. This may impact group audits where there are common control systems across the group, or automated reporting processes.
38 to 44	The group auditor shall take responsibility for designing and performing further audit procedures to respond to the assessed risks of material misstatement of the group financial statements arising from the consolidation process. This shall include: (a) evaluating whether all entities and business units have been included in the group financial statements as required by the applicable financial reporting framework and, if applicable, for designing and performing further audit procedures on sub-consolidations; (b) evaluating the appropriateness, completeness and accuracy of consolidation adjustments and reclassifications;	**Consolidation process** As part of the Group Engagement Team's risk assessment procedures, they should obtain an understanding of group-wide controls and the consolidation process, including the instructions issued by group management to components – in completing the Group Risk Assessment in Apex, the Group Engagement Team should scope in the 'Consolidation' Financial Statement Risk Area (FSRA) to assist with this risk assessment. If the Group Engagement Team plans to rely on group-wide controls, they, or a component auditor at their request, should test their operating effectiveness. The Group Engagement Team should design and perform controls and/or substantive procedures on the consolidation process to respond to the assessed

	(c) evaluating whether management's judgments made in the consolidation process give rise to indicators of possible management bias; and (d) responding to assessed risks of material misstatement due to fraud arising from the consolidation process. If the financial information of an entity or business unit has not been prepared in accordance with the same accounting policies applied to the group financial statements, the group auditor shall evaluate whether the financial information has been appropriately adjusted for purposes of preparing and presenting the group financial statements. If the group financial statements include the financial information of an entity or business unit with a financial reporting period-end that differs from that of the group, the group auditor shall take responsibility for evaluating whether appropriate adjustments have been made to that financial information in accordance with the applicable financial reporting framework. When the group auditor involves component auditors in the design or performance of further audit procedures, the group auditor shall communicate with the component auditor about matters that the group auditor or component auditor determine to be relevant to the design of responses to the assessed risks of material misstatement of the group financial statements.	risks of material misstatement of the group financial statements arising from the consolidation process. This should include: • evaluating whether all components have been included in the group financial statements; • checking whether the component financial information used in preparing the consolidation is the same as the financial information component auditors reported upon; • checking the arithmetic accuracy of the consolidation; • evaluating the appropriateness, completeness and accuracy of consolidation adjustments and reclassifications; • evaluating whether any fraud risk factors exist in respect of the consolidation process; and • evaluating whether any indicators of possible management bias exist. Where the group financial statements include the financial statements of a component with a financial reporting period-end that differs from that of the group, the Group Engagement Director determines the nature, timing and extent of the audit procedures required on any adjustments required. As set out in paragraph A141 of ISA (UK) 600 (Revised September 2022), The consolidation process may require adjustments and reclassifications to amounts reported in the group financial statements that do not pass through the usual IT applications, and may not be subject to the same controls to which other financial information is subject. The group auditor's evaluation of the appropriateness, completeness and accuracy of the adjustments and reclassifications may include: • evaluating whether significant adjustments appropriately reflect the events and transactions underlying them; • determining whether those entities or business units whose financial information has been included in the group financial statements were appropriately included;

	For areas of higher assessed Risks of Material Misstatement of the group financial statements, or significant risks identified in accordance with ISA (UK) 315 (Revised July 2020), on which a component auditor is determining the further audit procedures to be performed, the group auditor shall evaluate the appropriateness of the design and performance of those further audit procedures. When component auditors perform further audit procedures on the consolidation process, including on sub-consolidations, the group auditor shall determine the nature and extent of direction and supervision of component auditors and the review of their work. The group auditor shall determine whether the financial information identified in the component auditor's communication (see paragraph 45(a) of ISA (UK) 600 (Revised September 2022)) is the financial information that is incorporated in the group financial statements.	• determining whether significant adjustments have been correctly calculated, processed and authorized by group management and, when applicable, by component management; • determining whether significant adjustments are properly supported and sufficiently documented; and • evaluating the reconciliation and elimination of intra-group transactions, unrealized profits, and intra-group account balances.

Evaluating the component auditor's communications and the adequacy of their work

Table 25L: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Evaluating the component auditor's communications and the adequacy of their work

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
45 to 48	The group auditor shall request the component auditor to communicate matters relevant to the group auditor's	**Evaluating the component auditor's communications and the adequacy of their work**

	conclusion with regard to the group audit. Such communication shall include: (a) identification of the financial information on which the component auditor has been requested to perform audit procedures; (b) whether the component auditor has performed the work requested by the group auditor; (c) whether the component auditor has complied with the relevant ethical requirements, including those related to independence, that apply to the group audit engagement; (d) information about instances of non-compliance with laws or regulations; (e) corrected and uncorrected misstatements of the component financial information identified by the component auditor and that are above the threshold communicated by the group auditor in accordance with paragraph 36 of ISA (UK) 600 (Revised September 2022); (f) indicators of possible management bias; (g) description of any deficiencies in the system of internal control identified in connection with the audit procedures performed; (h) fraud or suspected fraud involving component management, employees who have significant roles in the group's system of internal control at the component or others where the fraud resulted in a material misstatement of the component financial information; (i) other significant matters that the component auditor communicated or expects to communicate to	If the Group Engagement Team concludes that communication with the component auditors has been inadequate, they should consider what further action could be taken to address this, including: • further discussions with the component auditor; • reviewing additional component auditor working papers, or more detail in their underlying risk assessment; • performing additional procedures or asking the component auditor to perform additional procedures; and • whether this indicates concerns around the component auditor's competence or capabilities which would lead the group auditor to reassess their evaluation of the component auditor.

	component management or those charged with governance of the component; (j) any other matters that may be relevant to the group audit, or that the component auditor determines are appropriate to draw to the attention of the group auditor, including exceptions noted in the written representations that the component auditor requested from component management; (k) the component auditor's overall findings or conclusions; and (l) any events or conditions identified by the component auditor that may cast significant doubt on the group's ability to continue as a going concern. The group auditor shall: (a) discuss significant matters arising from communications with the component auditor, including those in accordance with paragraph 45 of ISA (UK) 600 (Revised September 2022), with the component auditor, component management or group management, as appropriate; and (b) evaluate whether communications with the component auditor are adequate for the group auditor's purposes. If such communications are not adequate for the group auditor's purposes, the group auditor shall consider the implications for the group audit. The group auditor shall determine whether, and the extent to which, it is necessary to review additional component	

	auditor audit documentation. In making this determination, the group auditor shall consider: (a) the nature, timing and extent of the work performed by the component auditor; (b) the competence and capabilities of the component auditor as determined in accordance with paragraph 26(a) of ISA (UK) 600 (Revised September 2022); and (c) the direction and supervision of the component auditor and review of their work. If the group auditor concludes that the work of the component auditor is not adequate for the group auditor's purposes, the group auditor shall determine what additional audit procedures are to be performed, and whether they are to be performed by a component auditor or by the group auditor.	

Subsequent events

Table 25M: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Subsequent events

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
49	In applying ISA (UK) 560, the group auditor shall take responsibility for performing procedures, including, as appropriate, requesting component auditors to perform procedures, designed to identify events that may require	**Subsequent events** The Group Engagement Team should perform a subsequent events review. The work on component financial information should include consideration of subsequent events up to the date the group audit opinion is issued. The Group

	adjustment of, or disclosure in, the group financial statements.	Engagement Team therefore needs to consider whether there have been subsequent events since the preparation of the component financial information.
50	The group auditor shall request the component auditors to notify the group auditor if they become aware of subsequent events that may require adjustment of, or disclosure in, the group financial statements.	**Request for component auditors to notify the group auditor of subsequent events** A request for notification of relevant subsequent events is incorporated into the Group Audit Instructions Template. A specific confirmation over subsequent events which may require adjustment of, or disclosure in, the group financial statements is incorporated into the template for fieldwork returns made by component auditors. This confirmation provides the Group Engagement Team with some assurance over the completeness of identification of subsequent events material to the group at the relevant component up to the date of return by the component auditor. The Group Engagement Team should consider whether further subsequent events returns should be requested from component auditors, and document this consideration within the 'Events after the Reporting Date' Audit Response within the 'Conclusions' Audit Response Group. Such additional returns may be appropriate where there may be increased risk that subsequent events occur at the component level which may affect the group financial statements; for example, when: • there is a significant passage of time between the receipt of component fieldwork returns and certification; • there are known subsequent events which may crystalise at a component; or • there is significant uncertainty surrounding elements of the component's operations (including its going concern status).

Evaluating the sufficiency and appropriateness of audit evidence obtained

Table 25N: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Evaluating the sufficiency and appropriateness of audit evidence obtained

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
51 to 52	In applying ISA (UK) 330 (Revised July 2017) (Updated May 2022), the group auditor shall evaluate whether sufficient appropriate audit evidence has been obtained from the audit procedures performed, including from the work performed by component auditors, on which to base the group audit opinion. The group auditor shall: (a) evaluate and review the work performed by the component auditor for the purpose of the group audit; or (b) where the group auditor is unable to request or secure the agreement required by paragraph 29-1 of ISA (UK) 600 (Revised September 2022) (the group auditor shall request the agreement of the component auditor to the transfer of relevant documentation during the conduct of the group audit as a condition of the use by the group auditor of the work of the component auditor), take appropriate measures (including carrying out additional work, either directly or by outsourcing such tasks, in the relevant component) and inform the competent authority.	**Evaluating the sufficiency and appropriateness of audit evidence obtained** As explained in paragraph A149-1 of ISA (UK) 600 (Revised September 2022), the requirement to evaluate and review the work performed by component auditors for the purpose of the group audit is derived from Schedule 1 to the Statutory Auditors and Third Country Auditors Regulations 2016. 'Evaluate' is defined in the Financial Reporting Council's Glossary of terms – ethics and auditing (Updated December 2019) as "to identify and analyse the relevant issues, including performing further procedures as necessary, to come to a specific conclusion on a matter". 'Review' is defined in the Financial Reporting Council's Glossary of terms – ethics and auditing (Updated December 2019) as "appraising the quality of the work performed and conclusions reached by others". As described in paragraph A149-3 of ISA (UK) 600 (Revised September 2022), the nature, timing and extent of the review and evaluation required by paragraph 51-1 of ISA (UK) 600 (Revised September 2022) is a matter for professional judgement and may include consideration of such matters as: • The group auditor's previous experience with the component auditor, and the component. For example, if the work related to the component's information system is being performed by the same component auditor who performed the work in the prior period and there are no significant changes to the information system, the

	The group engagement partner shall evaluate the effect on the group audit opinion of any uncorrected misstatements (whether identified by the group auditor or communicated by component auditors) and any instances when there has been an inability to obtain sufficient appropriate audit evidence.	extent of the review of the related working papers may be less detailed. • The complexity of the component, including whether there are significant events that have occurred at the component or in the industry in which the component operates since the previous audit engagement or during the current engagement. • The assessed risks of material misstatement. For example, a higher assessed risk of material misstatement may require a more detailed review of the component auditor's work. Notwithstanding the factors above affecting the nature, timing and extent of the review and evaluation required, any work performed by component auditors for the purpose of the group audit (including risk assessment activity and responses to risks) must be subject to review by the Group Engagement Team).

Auditor's certificate or report

Table 25O: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Auditor's certificate or report

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
53	The auditor's report on the group financial statements shall not refer to a component auditor, unless required by law or regulation to include such reference. If such reference is required by law or regulation, the auditor's report shall indicate that the reference does not diminish the group engagement partner's or the group engagement partner's firm's responsibility for the group audit opinion.	**Auditor's certificate or report** The Group Engagement Team should follow the procedures set out in Section 13: Concluding and reporting when preparing the audit certificate or report on the group financial statements.

Communication with group management and those charged with governance of the group

Table 25P: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Communication with group management and those charged with governance of the group

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
54 to 55	The group auditor shall communicate with group management an overview of the planned scope and timing of the audit, including an overview of the work to be performed at components of the group. If fraud has been identified by the group auditor or brought to its attention by a component auditor (see paragraph 45(h) of ISA (UK) 600 (Revised September 2022)), or information indicates that a fraud may exist, the group auditor shall communicate this, unless prohibited by law or regulation, on a timely basis to the appropriate level of group management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities.	**Communication with group management** ***Consultation required*** If fraud has been identified or information indicates that a fraud may exist, the Group Engagement Team should report the fraud to the NAO's Money Laundering Reporting Officer – further guidance is provided in Chapter 30: Fraud responsibilities – and, subject to the requirements to avoid 'tipping off', communicate the fraud on a timely basis to the appropriate level of group management.
56	A component auditor may be required by statute, regulation or other reasons to express an audit opinion on the financial statements of an entity or business unit that forms part of the group. In that case, the group auditor shall request group management to inform management of the entity or business unit of any matter of which the group auditor becomes aware that may be significant to the financial statements of the entity or business unit, but	**A component auditor is required to express an audit opinion on the financial statements of an entity or business unit that forms part of the group, and the group auditor becomes aware that may be significant to the financial statements of the entity or business unit, but of which management of the entity or business unit may be unaware** ***Consultation required*** If the Group Engagement Team is required by paragraph 56 of ISA (UK) 600 (Revised September 2022) to consider whether to

	of which management of the entity or business unit may be unaware. If group management refuses to communicate the matter to management of the entity or business unit, the group auditor shall discuss the matter with those charged with governance of the group. If the matter remains unresolved, the group auditor, subject to legal and professional confidentiality considerations, shall consider whether to advise the component auditor not to issue the auditor's report on the financial statements of the entity or business unit until the matter is resolved.	advise the component auditor not to issue the auditor's report on the financial statements of the entity or business unit until the matter is resolved, the Group Engagement Team should consult FAPQ.
57 to 57-1	The group auditor shall communicate the following matters with those charged with governance of the group, in addition to those required by ISA (UK) 260 (Revised November 2019) (Updated May 2022) and other ISAs (UK): (a) an overview of the work to be performed at the components of the group and the nature of the group auditor's planned involvement in the work to be performed by component auditors. (b) instances when the group auditor's review of the work of a component auditor gave rise to a concern about the quality of that component auditor's work, and how the group auditor addressed the concern. (c) any limitations on the scope of the group audit, for example, significant matters related to restrictions on access to people or information. (d) fraud or suspected fraud involving group management, component management, employees who have significant roles in the group's system of internal control or others when	**Communication with those charged with governance of the group** The matters to be communicated to those charged with governance of the group are incorporated into the Audit Planning Report and Audit Completion Report templates, as well as the Additional Report to the Audit Committee of a PIE template, as appropriate.

	the fraud resulted in a material misstatement of the group financial statements. For audits of group financial statements of public interest entities, the group auditor shall bear overall responsibility for the additional report to the audit committee.	
58	In applying ISA (UK) 265 (Updated May 2022), the group auditor shall determine whether any identified deficiencies in the group's system of internal control are required to be communicated to those charged with governance of the group or group management. In making this determination, the group auditor shall consider deficiencies in internal control that have been identified by component auditors and communicated to the group auditor in accordance with paragraph 45(g) of ISA (UK) 600 (Revised September 2022).	**Communication of identified deficiencies in internal control** The Group Engagement Team should document their consideration of identified deficiencies in the group's system of internal control, including deficiencies in internal control that have been identified by component auditors and communicated to the group auditor, within the 'Significant Documentation and Deficiencies' Audit Response within the 'Conclusions' Audit Response Group.

Documentation

Table 25Q: Key policy choices used by the NAO in applying ISA (UK) 600 (Revised September 2022) – Documentation

ISA (UK) 600 (Revised September 2022) paragraph reference	Summary of requirements of the standard	NAO policies
59 to 59-1	In accordance with ISA (UK) 230 (Revised June 2016) (Updated May 2022), the audit documentation for a group audit engagement needs to be sufficient to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of	**Documentation of work performed by the component auditor** The Group Engagement Team should include in the audit documentation the reporting received from the component auditors or documentation of the communication with them (for example, through review of their files).

	audit procedures performed, the evidence obtained, and the conclusions reached with respect to significant matters arising during the group audit. In applying ISA (UK) 230 (Revised June 2016), the group auditor shall include in the audit documentation: • significant matters related to restrictions on access to people or information within the group that were considered before deciding to accept or continue the engagement, or that arose subsequent to acceptance or continuance, and how such matters were addressed; • the basis for the group auditor's determination of components for purposes of planning and performing the group audit; • the basis for the determination of component performance materiality, and the threshold for communicating misstatements in the component financial information to the group auditor; • the basis for the group auditor's determination that component auditors have the appropriate competence and capabilities, including sufficient time, to perform the assigned audit procedures at the components; • key elements of the understanding of the group's system of internal control in accordance with paragraph 30(c) of ISA (UK) 600 (Revised September 2022); • the nature, timing and extent of the group auditor's direction and supervision of component auditors and the review of their work, including, as applicable, the group auditor's review of	Where component auditors are performing risk assessment activity at the component level (see ***Table 25I*** above, section entitled 'Identifying and assessing the Risks of Material Misstatement – scoping the components at the assertion level'), the output of the component auditor's risk assessment should be reflected in tab 'D1. FRA Group Audit Approach' of the GARAST. As described in paragraph A176 of ISA (UK) 600 (Revised September 2022), component auditor audit documentation ordinarily need not be replicated in the group auditor's audit file. However, the group auditor may decide to summarise, replicate or retain copies of certain component auditor documentation in the group auditor's audit file to supplement the description of a particular matter in communications from the component auditor, including the matters required to be communicated by ISA (UK) 600 (Revised September 2022). Examples of such component auditor documentation may include: • a listing or summary of the significant judgments made by the component auditor, and the conclusions reached thereon, that are relevant to the group audit; • matters that may need to be communicated to those charged with governance of the group; or • matters that may be determined to be key audit matters to be communicated in the auditor's report on the group financial statements. **Documentation of work performed by the component auditor – NAO performs the component audit in-house and the Group Engagement Director is also the component Engagement Director** The Group Engagement Director should add a note to the group audit file to confirm that they have fulfilled their responsibilities under ISA (UK) 220 (Revised July 2021) to review work performed by the component auditor for the purpose

	additional component auditor audit documentation in accordance with paragraph 47 of ISA (UK) 600 (Revised September 2022); • matters related to communications with component auditors, including: o matters, if any, related to fraud, related parties or going concern communicated in accordance with paragraph 32 of ISA (UK) 600 (Revised September 2022); o matters relevant to the group auditor's conclusion with regard to the group audit, in accordance with paragraph 45 of ISA (UK) 600 (Revised September 2022), including how the group auditor has addressed significant matters discussed with component auditors, component management or group management; • the group auditor's evaluation of, and response to, findings or conclusions of the component auditors about matters that could have a material effect on the group financial statements. The group auditor shall include in the audit documentation the nature, timing and extent of the work performed by the component auditor, including, where applicable, the group auditor's review of relevant parts of the component auditor's audit documentation.	of the group audit whilst reviewing the component audit file as Engagement Director for the component. The Group Engagement Team should additionally include on the group audit file: • a high-level summary of the nature, timing and extent of the work performed by the component auditor for the purpose of the group audit (an optional template, the Component Auditor Summary Memo, is available to document this requirement); and • the Group Engagement Team's evaluation and review of the work performed at the component level for the purpose of the group audit (see ***Table 25N*** above) (an optional template, the Review of Component Auditor's Work template, is available to document this requirement). **Documentation of work performed by the component auditor – NAO performs the component audit in-house and the component Engagement Director is another NAO staff member; or a third party performs the group audit** The Group Engagement Director should use one of the following methods to document that they have fulfilled their responsibilities under ISA (UK) 220 (Revised July 2021) to review work performed by the component auditor for the purpose of the group audit: • Method 1: The Group Engagement Director brings copies of relevant component auditor working papers onto the group audit file and documents their review on those copies. This method is likely to be appropriate where the scope of the Group Engagement Director's review is restricted to small, discrete areas of the component audit file. It is less likely to be appropriate where multiple COTABDs or FSRAs have been scoped in for review.

		• Method 2: The Group Engagement Director reviews the working papers directly on the component auditor's file and adds a note of what they have reviewed to the group audit file. The Group Engagement Director then adds evidence (for example, an email trail or a calendar invitation) to the group audit file to demonstrate that they have carried out their review on the component audit file. The Group Engagement Team should additionally include on the group audit file: • a high-level summary of the nature, timing and extent of the work performed by the component auditor for the purpose of the group audit (an optional template, the Component Auditor Summary Memo, is available to document this requirement); and • the Group Engagement Team's evaluation and review of the work performed at the component level for the purpose of the group audit (see ***Table 25N*** above) (an optional template, the Review of Component Auditor's Work template, is available to document this requirement). **Documentation of work performed by the component auditor – NAO performs the component audit and the component audit is contracted out** The Group Engagement Director and Group Engagement Team should follow the relevant procedures outlined above for in-house audits depending on whether the Group Engagement Director is also the component Engagement Director, or not. On a contracted-out audit, the NAO Engagement Director is the engagement partner under ISA (UK) 220 (Revised July 2021). This means that any communications between the group auditor and the component auditor should be directed to the NAO Engagement Director and NAO engagement team for the component audit, rather than the contractor auditor of the component. The NAO

		Engagement Director for the component audit is responsible for facilitating access to the contractor auditor's file and the formal submission of any communications to the Group Engagement Team.
59-2 to 59-3	The group auditor shall retain sufficient and appropriate audit documentation to enable the competent authority to review the work of the auditor of the group financial statements. Where: • the group auditor is subject to a quality assurance review or an investigation concerning the group audit; and • the competent authority requests delivery of any additional documentation of the work performed by that component auditor for the purpose of the group audit (including the component auditor's working papers relevant to the group audit), the group auditor shall, in order to properly deliver such documentation in accordance with such request, either: • retain copies of the documentation of the work carried out by the relevant component auditor for the purpose of the group audit (including the component auditor's working papers relevant to the group audit); or • obtain the agreement of the relevant component auditor that the group auditor shall have unrestricted access to such documentation on request; or • retain documentation to show that the group auditor has undertaken the appropriate	**Reviews by the competent authority (Financial Reporting Council)** The Group Audit Instructions template incorporates a standard request for the component auditor to agree to provide the NAO and/or any regulatory authority access to component auditor documentation relevant to the group audit on request. ***Consultation required*** Where a component auditor does not agree to this requirement, the Group Engagement Team should either import all relevant component auditor documentation into the group audit file or consult FAPQ.

	procedures in order to gain access to the audit documentation, together with evidence supporting the existence of any impediments to such access; or • take any other appropriate action.	
A168	The audit documentation for the group audit comprises: • the documentation in the group auditor's file; and • the separate documentation in the respective component auditor files relating to the work performed by the component auditors for purposes of the group audit (i.e., component auditor audit documentation).	**Obtaining and retaining documentation held within component audit files which is performed by the component auditor and supports the group audit opinion** In relation to component audits where work is performed by the component auditor for the purpose of the group audit: • For component audits which are certified before or at the same time as the group audit, the file closure deadline and retention schedules will be aligned, so the Group Engagement Team is not required to undertake specific action to obtain and retain copies of separate documentation in the respective component auditor files. • ***Consultation required*** For component audits which are certified after the group audit, the Group Engagement Team should request a copy of the component auditor's audit file at the date of certification of the group financial statements and retain this within the group audit file on Apex for the standard retention period for an Apex audit file (six years). If a component auditor who has performed work for the purpose of the group audit does not agree to provide such a file copy, the Group Engagement Team should consult FAPQ.

Regularity for group audits – identifying the framework of authorities

25.9 As described in paragraph 2-63 of Practice Note 10 (Revised 2022), frameworks of authorities are specific to each entity and the fact that an entity is consolidated does not result in that entity having to apply their parent entity's framework of authorities. For example, a public sector body may not have a specific framework of authorities. Therefore, the component may not require the audit of regularity for the purpose of a group regularity opinion, except for fraud considerations. However, where a consolidated entity has a framework of authorities but was not subject to the audit of regularity, the group auditor may carry out audit procedures (or instruct a component auditor to do so) to obtain assurance over regularity of the component's transactions.

25.10 The Group Engagement Team should document the high-level framework of authorities applicable to the group using the Group Audit Risk Assessment Scoping Template (GARAST) (tab 'E. Group Regularity RA').

Regularity for group audits – communications with component auditors

25.11 The Group Engagement Team should identify which component auditors report on regularity as part of their work.

Regularity for group audits – materiality

25.12 The approach prescribed in the section of Chapter 16: Materiality, performance materiality and trivial threshold entitled 'Setting materiality for regularity' applies to the determination of materiality and performance materiality for the purpose of the regularity opinion on the group.

25.13 The Group Engagement Team is not required to determine component performance materiality for the purpose of the regularity opinion.

Regularity for group audits – risk assessment

25.14 Within the GARAST (tab 'E. Group Regularity RA'), the Group Engagement Team should make an assessment of the risks of material irregular transactions within the group financial statements associated with each aspect of the possible frameworks of authorities listed in the template, categorising these as follows:

- No risk: there is no risk of material irregular transactions, either because that aspect of the possible frameworks of authorities is not relevant to the audited entity or because the value of affected transactions is immaterial.
- Significant: there is a heightened risk of material irregular transactions
- Low: by exception, there is some risk of material irregular transactions, but the risk of their crystallising is very low due either to the nature of the risk or the counterparties involved.
- Medium: there is a risk of material irregular transactions, but this is not a heightened level of risk or a low level of risk (i.e., all other levels of risk).

Regularity for group audits – responses designed by the Group Engagement Team at an aggregated basis on a group level

25.15 For identified risks of material irregular transactions, the Group Engagement Team should document whether the responses to the risk will be determined by component auditors at component level or by the Group Engagement Team at an aggregated basis on a group level.

25.16 For risks to which the Group Engagement Team plans to design the responses at an aggregated basis on a group level, the Group Engagement Team should document the controls which address the risk of material irregular transactions and plan whether to seek to obtain assurance from the operating effectiveness of those controls. The Group Engagement Team should evaluate the design and implementation of any controls over which the Group Engagement Team seeks to obtain assurance from their operating effectiveness, as well as any controls addressing a risk of material irregular transactions which has been assessed as Significant.

25.17 Based on the level of risk and controls assurance to be obtained (see ***Table 25R*** below), the Group Engagement Team should design appropriate substantive responses and document these in the GARAST (tab 'E. Group Regularity RA').

Table 25R: Matrix for residual assurance required from substantive testing of risks of irregular transactions

Assessed level of risk of material irregular transactions	Planned controls assurance level		
	None	Low	Medium
Target	None	N/A	N/A
Low	Low	None	N/A
Medium	Medium	Low	N/A
Significant	High	Medium	Low

Regularity for group audits – scoping of components

25.18 For each relevant framework of authorities element affected by risks of material irregular transactions, the Group Engagement Team should compare the value affected to component performance materiality for each component. Where these values exceed component performance materiality, the relevant risk of material irregular transactions will be scoped-in to the group audit for risk assessment purposes, (and assurance will be required over the risk for the purposes of the group audit.

25.19 The Group Engagement Team may also judgementally scope in further risks of material irregular transactions. However, component scoping for regularity purposes should be primarily driven by quantitative considerations rather than qualitative factors. Matters which are considered qualitatively material at the component level should not be treated as qualitatively material to the group as whole, but should be considered by exception where appropriate for their potential impact on the group audit opinion.

25.20 This should be documented in the GARAST (tab 'F1. Regularity Component Scope').

25.21 The Group Engagement Team should determine whether the group auditor or the component auditor will be performing the risk assessment over the risk of material irregular transactions at the component level.

25.22 Where the component auditor is providing a regularity opinion, it will usually be sufficient to seek to use the work performed in support of the regularity opinion on that individual component to provide assurance to support the group regularity opinion. However, where the component auditor is

not providing a regularity opinion, the Group Engagement Team may wish to instruct the component auditor (through Group Audit Instructions) to perform specific procedures to address the risk of material irregular transactions.

25.23 Where the risk assessment is being performed by the component auditor, the Group Engagement Team should instruct the component auditor to perform the relevant risk assessment (and most likely the associated responses to assessed risk) within the Group Audit Instructions sent to that component auditor.

25.24 Where the risk assessment is being performed by the Group Engagement Team, the Group Engagement Team should ensure that they have performed a regularity risk assessment on the risk of material irregular transactions at the component level within a separate Regularity Risk Assessment template.

Regularity for group audits – regularity stand-back

25.25 The Group Engagement Team should consider whether the total scoped-in against all risks of material irregular transactions provide sufficient coverage to form a risk assessment over the transactions recorded in the group financial statements. If coverage is insufficient, the Group Engagement Team should judgementally scope in further components until the level of coverage is sufficient.

25.26 The Group Engagement Team should document why a component has not been scoped in for risk assessment on risk grounds where any of the following circumstances are applicable:

- the component auditor has qualified or is likely to qualify the regularity opinion;
- a significant risk in relation to regularity has been reported by the component auditor; or
- the component has an unusual or bespoke framework of authorities.

25.27 The Group Engagement Team should consider whether it is appropriate to recognise a significant risk of material irregular transactions in the circumstances where the same non-significant regularity risk arises in multiple components.

25.28 The Group Engagement Team should further document a final stand-back judgement on whether the totality of components scoped in against each risk of material irregular transactions is sufficient.

25.29 This should be documented in the GARAST (tab ‘F2. Regularity Standback’).

Chapter 26: Combined financial statements of components that have no parent

Relevant standards and guidance

26.1 ISA (UK) 600 (Revised September 2022) *Special considerations – audits of group financial statements (including the work of component auditors)* deals with special considerations that apply to group audits; in particular, those that involve component auditors.

26.2 Paragraphs 1-186 to 1-196 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying the principles of ISA (UK) 600 (Revised November 2019) (Updated May 2022) to combined financial statements of components that have no parent.

Parentless consolidations audited by the NAO

26.3 The NAO audits a number of accounts that consolidate financial information from a large number of components in a particular sector. These include:

- the Whole of Government Accounts prepared by HM Treasury; and
- the Consolidated NHS Provider Accounts.

26.4 These accounts differ from conventional group accounts, in that there is no parent entity, so the financial information includes only the results of the various components that are in scope.

26.5 These accounts are group financial statements as defined in of paragraphs 2 and 14(k) of ISA (UK) 600 (Revised September 2022). The audit approach for such engagements is discussed in Chapter 25: Group audit procedures.

Chapter 27: Going concern

Relevant standards and guidance

27.1 ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern* deals with the auditor's responsibilities in the audit of financial statements relating to going concern and the implications for the auditor's report.

27.2 Paragraphs 1-142 to 1-181 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provides guidance on applying ISA (UK) 570 (Revised September 2019) (Updated May 2022) in the public sector.

27.3 For the NAO's international audits, the requirements of ISA 570 (Revised) *Going concern* as issued by the International Auditing and Assurance Standards Board apply without the UK-specific adaptations in ISA (UK) 570 (Revised September 2019) (Updated May 2022) issued by the Financial Reporting Council. The differences between the international and UK versions of the ISAs are particularly significant for going concern. Some of the guidance in Practice Note 10 (Revised 2022) on going concern may also not be relevant for international audits, where it involves the application of the UK-adapted standard.

27.4 Paragraphs 14(a)(ii) and A35-5 of ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector* include requirements on the auditor to report promptly to the regulator a material threat or doubt concerning the continuous functioning of an audited entity that is a Public Interest Entity, which includes matters related to going concern.

Background to going concern in the public sector

27.5 Going concern issues arise in the public sector. They include, but are not limited to, situations where public sector entities operate on a for-profit basis, where government support may be reduced or withdrawn, or in the case of privatisation. Events or conditions that may cast significant doubt on an entity's ability to continue as a going concern in the public sector may include situations where the public sector entity lacks funding for its continued existence or when policy decisions are made that affect the services provided by the public sector entity.

27.6 The requirement to prepare financial statements under the going concern basis applies even when there are uncertainties about events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern in the future. Audited entities must disclose such uncertainties in the financial statements when they are material.

27.7 The term "ability to continue as a going concern" is equivalent to the term "ability to continue to adopt the going concern basis of accounting" in the future.

27.8 The FReM, IFRS and UK GAAP all include a requirement for management to make a specific assessment of the entity's ability to continue as a going concern and set standards to be considered and disclosures to be made in connection with going concern.

Determining the approach to going concern

27.9 In the first instance, the engagement team should consider the audited entity's circumstances and applicable financial reporting framework.

27.10 The engagement team should also consider the applicable auditing standards, in particular whether the international (rather than the UK-specific) version of ISA 570 (Revised) applies (i.e. for international audits). Where this is the case, as part of the risk assessment carried out as per Chapter 17: Risk assessment and response planning, the engagement team should ensure the relevant Financial Reporting Sub-Activity for going concern for international audits is scoped into the risk assessment in the Risk Assessment in Apex.

27.11 The engagement team should identify whether the primary financial reporting framework provides that the anticipated continuation of the provision of a service in the future will be presumed to provide sufficient evidence to prepare the financial statements on a going concern basis.

27.12 The FReM includes such a provision for non-trading entities. The interpretation of IAS 1 *Presentation of financial statements* in the FReM provides that the anticipated continuation of the provision of a service in the future will be presumed to provide sufficient evidence to prepare the financial statements on a going concern basis for non-trading entities. Therefore, the 'continued provision of service' approach would not be appropriate for trading entities that follow the FReM. Trading entities are entities that operate on a commercial or quasi-commercial basis or generate the majority of their income through sales of goods or services. They include, but are not limited to, trading funds as some executive agencies or NDPBs may operate on this basis. Entities funded primarily by the Estimates process, grant-in-aid, statutory levies, fees or taxes are not trading entities.

27.13 If appropriate, based on the considerations above, the engagement team should apply the 'continued provision of service' approach in accordance with Practice Note 10 (Revised 2022), which provides guidance on when such an approach may be applied. Further guidance is provided under the headings below on 'Risk assessment' and 'Evaluating management's assessment'.

Additional considerations for entities which are required to or choose voluntarily to report on compliance with the UK Corporate Governance Code

27.14 The engagement team should establish whether the entity is required or chooses voluntarily, to report on compliance with the UK Corporate Governance Code (not to be confused with HM Treasury's Corporate governance for central government departments: code of good practice). Where this applies to the entity, the engagement team should follow the specific additional procedures for these UK Corporate Governance Code bodies set out in paragraphs 16-1, 21-1(c), 21-1(d), 22(c), 24-1 and 24-2 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) and paragraph 1-170 of Practice Note 10 (Revised 2022).

27.15 Determining the nature and extent of procedures to address the specific requirements for these bodies is a matter of the engagement team's professional judgment. Examples of such procedures include:

- Obtaining an understanding of the management's method to assess the entity's viability.
- Obtaining and considering management's assessment of the entity's viability and the underlying supporting documents.
- Considering the appropriateness of the assessment period used by management over which viability is assessed.
- Considering the extent to which management has stress tested their forecasts, including any reverse stress testing.

- Where management has prepared cash flow forecasts:
    - Checking whether the calculations within the cash flow forecasts are arithmetically accurate.
    - Considering whether there are inconsistencies between the cash flow forecasts prepared to support the viability assessment and those prepared for other purposes (e.g., for going concern, impairment, deferred taxation). In most cases, the auditor would expect the underlying data generated to prepare the forecasts to be the same, whilst recognising there may be permissible differences between certain items in the individual forecasts (e.g., remedial actions).
- Where management have considered a range of alternative outcomes by, for example, performing a sensitivity analysis to determine the effect of changes in the significant assumptions or the data used in assessing the entity's viability, considering the appropriateness of the outcomes.
- Considering whether the statements and disclosures made in the annual report comply with the relevant provisions of the UK Corporate Governance Code and are consistent with:
    - management's assessment of the audited entity's viability and the underlying supporting documents; and
    - management's assessment of the audited entity's ability to continue as a going concern, including all relevant information of which the engagement team are aware as a result of the audit.

Risk assessment

27.16 In performing the risk assessment procedures for going concern, the engagement team should (as required by paragraphs 10-2(a) to 10-2(c) of ISA (UK) 570 (Revised September 2019) (Updated May 2022)) obtain an understanding of the audited entity and its environment consisting of:

- The audited entity's business model, objectives, strategies and related business risks;
- The nature of the audited entity, including its operations, the types of investments or disposals, if any, the audited entity is making and plans to make, and how the audited entity is structured and financed; and
- The measurement and review of the audited entity's financial performance, including forecasts, future cash flows, and management's budgeting processes.

27.17 The engagement team should also (as required by paragraph 10-2(d) of ISA (UK) 570 (Revised September 2019) (Updated May 2022)) obtain an understanding of the requirements of the applicable financial reporting framework relating to going concern, and the related disclosures that the audited entity should include in their financial statements.

27.18 The engagement team should also (as required by paragraphs 10-2(e) to 10-2(h) of ISA (UK) 570 (Revised September 2019) (Updated May 2022)) obtain an understanding of the audited entity’s system of internal control consisting of:

- The nature and extent of oversight and governance that the audited entity has in place over management's assessment of the audited entity's ability to continue as a going concern;
- How the audited entity’s risk assessment process:
    - Identifies business risks relating to events or conditions that, individually or collectively, may cast significant doubt on the audited entity's ability to continue as a going concern;
    - Assesses the significance of those risks, including the likelihood of their occurrence and their potential impact; and
    - Addresses those risks;
- The results of the audited entity's risk assessment process; and
- The audited entity's information system, and related business processes, as it relates to going concern, including:

- How the information system identifies and captures events or conditions that, individually or collectively, may cast significant doubt on the audited entity's ability to continue as a going concern;
- How management identifies the relevant method, assumptions and data that are appropriate in assessing the audited entity's ability to continue as a going concern; and
- How the financial reporting process used to prepare the audited entity's financial statements captures disclosures related to the audited entity's ability to continue as a going concern.

27.19 The engagement team should obtain an understanding of the legislative framework of the entity. This should include, as a minimum:

- whether the audited entity is established in statute and whether it would require an Act of Parliament and/or a Ministerial Order to dissolve or abolish the audited entity; and
- whether there is a statutory mechanism under which funding is required to be provided to the audited entity. This could either be through a statutory provision for funding by Ministers or a mechanism for raising fees.

27.20 Where either:

- the engagement team assesses that both criteria in the previous paragraph are met; or
- the engagement team is applying the 'continued provision of service approach; or
- the audited entity is a smaller entity that may not have an independent governance structure, and the role of governance may be undertaken directly by one or a small number of individuals, meaning some considerations about the nature and extent of oversight and governance the audited entity has in place may be less relevant or not applicable,

the engagement team is likely to be able to undertake less extensive risk assessment procedures on the basis provided for in paragraph A4-1 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) and paragraph 1-158 of Practice Note 10 (Revised 2022). However, the fact that the entity is funded wholly or partly through grant-in-aid is not in itself sufficient justification for the application of this approach.

27.21 Throughout the audit, the engagement team should document their consideration of whether there are any changes in the understanding of the audited entity and its environment, its financial reporting framework or the system of internal control relevant to going concern and consider the impact on the risk assessment and the scope of planned work.

27.22 Where the engagement team considers that events or conditions that may cast significant doubt on the audited entity's ability to continue as a going concern give risk to a risk of management bias in the preparation of the financial statements, the engagement team must factor this risk in to their work to respond to the significant risk of fraud through management override of controls. This includes the assessment of significant estimates or journals impacting key balances upon which management's assessment of going concern is based. In practice, this will be done through revisiting the Risk Assessment in Apex and ensuring that the going concern financial statements level risk is mapped as affecting any relevant FRAs, which may be impacted.

Risk assessment – continued provision of service approach

27.23 The engagement team should (in accordance with paragraph 1-155 of Practice Note 10 (Revised 2022) and paragraphs 10-1 to 10-2 of ISA (UK) 570 (Revised September 2019) (Updated May 2022)) obtain an understanding with respect to going concern of the entity and its environment, applicable financial reporting framework and audited entity's system of internal control sufficient to conclude that:

- the nature of the entity means that, notwithstanding any intention to liquidate the entity or cease its operations in their current form, it will continue to be appropriate to adopt the going concern basis of accounting because, in such an event, the services it performs can be expected to continue to be delivered by related public authorities and preparing the financial statements on a going concern basis will still provide a faithful representation of the items in the financial statements;
- the financial reporting framework permits the entity to prepare its financial statements on the basis of the presumption of the anticipated continuation of the provision of a service in the future. This may include assessing whether the entity is a trading entity as some financial reporting frameworks do not allow trading entities to apply this presumption; and
- the entity's system of internal control to identify events or conditions relevant to going concern is proportionate to the low risk that a material uncertainty related to going concern exists.

27.24 The engagement team should perform procedures to ascertain whether Parliament has a known intention to abolish, transfer or privatise the activities of the entity (in accordance with paragraph 1-166 of Practice Note 10 (Revised 2022)). Where the engagement team considers this to be the case, they should first establish whether the audited entity's operational activities are likely to be transferred elsewhere in the public sector. Where they are, irrespective of whether the audited entity will continue to operate, the going concern basis of preparation of the financial statements is likely to remain appropriate. Where they are not, the continued provision of service approach will not be appropriate.

27.25 Where a government policy decision has been taken which affects the going concern status of an audited entity it will be necessary to consider the specific wording of the relevant legislation. In some cases, the Secretary of State may have the authority to discontinue substantially all the functions of the body without recourse to Parliament. In other cases, the functions of the body will continue until the authorising legislation is repealed.

27.26 Where legislation is required for the cessation of a body, it will usually remain appropriate to prepare the financial statements on a going concern basis until such time as the legislation is passed, as the requirement to pass legislation makes the cessation contingent on a future event and therefore uncertain. However, the intention to bring legislation before the Houses may give rise to a material uncertainty over going concern.

27.27 The situation in the public sector is further complicated by the possibility of the transfer of functions or operations to another part of the public sector. Where an entity itself will cease to exist, the going concern basis may remain an appropriate basis for the preparation of financial statements where the majority of functions or operations (together with the assets used to deliver them) will be transferred. Consideration needs to be given as to whether the services will continue to be provided using the same assets but through another public sector entity before confirming whether the going concern or an alternative basis of accounting should be used to prepare the accounts.

27.28 Following the risk assessment, the engagement team should conclude whether it is appropriate to assume that the services being performed by the audited entity will continue to be performed for the foreseeable future. If this conclusion is inappropriate, the engagement team should cease to follow the continued provision of service approach (in accordance with paragraph 1-156 of Practice Note 10 (Revised 2022)). Re-visit this assessment, including consideration of any changes in the audited entity's financial reporting framework, prior to commencing the evaluation of management's assessment and again prior to certification to ensure the approach remains appropriate.

Period of assessment

27.29 In the UK, the period used by those charged with governance in making their assessment is usually at least one year from the date of approval of the financial statements, including for those entities reporting under the FReM.

27.30 While the minimum period to be covered by management's assessment is one year from the date of approval of the financial statements, management should also consider events or conditions within the foreseeable future where these fall outside of this period. Specific guidance on directors' responsibilities which apply for companies or charities is provided in Chapter 42: Companies and Chapter 43: Charities.

27.31 For the purpose of applying paragraph 14-1 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) (management's assessment of the entity's ability to continue as a going concern covers less than twelve months from the date of approval of the financial statements), the date of approval of the financial statements is usually the certification date.

27.32 A small number of financial reporting frameworks or laws or other regulations may require an assessment for a period longer than twelve months. If this is the case, the engagement team should request management extend its assessment period to cover the period required if it does not already.

Evaluating management's assessment

27.33 The engagement team should ensure the Apex audit file contains a copy of management's assessment of the entity's ability to continue as a going concern and, where management has not yet performed an assessment, the auditor's request for this as required by paragraph 10-3 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) and paragraph 1-160 of Practice Note 10 (Revised 2022).

27.34 Where the engagement team is applying the 'continued provision of service' approach or has established that both the following criteria are met:

- the audited entity is established in statute and would it require an Act of Parliament and/ or Ministerial Order to dissolve or abolish the entity; and
- there is a statutory mechanism under which funding is required to be provided to the audited entity, which could either be through a statutory provision for funding by Ministers or a mechanism for raising fees,

the engagement team's evaluation of the appropriateness of management's assessment may be made without performing further procedures where the engagement team's other audit procedures are sufficient to enable the team to conclude whether management's use of the going concern basis of accounting in the preparation of the financial statements is appropriate in the circumstances. However, the fact that the entity is funded wholly or partly through grant-in-aid is not in itself sufficient justification for the application of this approach.

27.35 Where the engagement team assess that further procedures are required to evaluate the appropriateness of management's assessment, they should document management's method to assess the entity's ability to continue as a going concern on the Apex audit file.

27.36 ***Consultation required*** Where management is unwilling to make an assessment or extend its assessment when requested to do so by the engagement team, the Engagement Director should discuss the matter with management, and where appropriate, those charged with governance. Where management or those charged with governance do not provide sufficient information about

the audited entity's ability to continue as a going concern, the engagement team should consult FAPQ on how to apply paragraph 15-1 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) (management is unwilling to make or extend its assessment when requested to do so by the auditor).

27.37 Determining whether a material uncertainty related to going concern exists involves management's assessment of:

- the likelihood of events or conditions occurring; and
- their potential impact.

27.38 Uncertainties relating to such events or conditions are considered material if their disclosure could reasonably be expected to affect the economic decisions of users of the financial statements.

27.39 When evaluating management's method to assess the audited entity's ability to continue as a going concern, the engagement team may conduct a review of the outcome of previous forecasts (retrospective review) as this may provide information regarding the effectiveness of management's review. Further guidance is provided in paragraph A8-3 of ISA (UK) 570 (Revised September 2019) (Updated May 2022).

Evaluating management's assessment – continued provision of service approach

27.40 Management's method for assessment of going concern may be proportionate to the low risk to the entity, where the continued provision of service approach applies. The lack of detailed analysis by management to support its assessment should not prevent the engagement team from concluding whether management's use of the going concern basis of accounting is appropriate in the circumstances. Nevertheless, where management has not yet performed an assessment, the engagement team should request the management perform an assessment (in accordance with paragraph 10-3 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) and paragraph 1-163 of Practice Note 10 (Revised 2022)) and ensure such a request is included within the audit documentation.

27.41 The engagement team should evaluate management's method to assess the audited entity's ability to continue as a going concern to conclude that either (in accordance with paragraph 1-161(a) of Practice Note 10 (Revised 2022)):

- where management has made a simple assessment of the audited entity's ability to continue as a going concern, management's assessment is clearly appropriate in the circumstances; or
- where management has made no assessment despite the engagement team making an explicit request for them to do so, the engagement team is able to conclude that management's use of the going concern basis is appropriate in the absence of detailed analysis by management.

27.42 The engagement team should obtain sufficient evidence to conclude that either (in accordance with paragraph 1-161(b) of Practice Note 10 (Revised 2022)):

- where management has made a simple assessment of the entity's ability to continue as a going concern, no underlying data exists because management's assessment is not based on quantitative factors; or
- where management has made no assessment despite the engagement team making an explicit request for them to do so, there are no underlying data or assumptions to assess because management has not made its own assessment.

27.43 The engagement team should evaluate and conclude (in accordance with paragraph 1-161(c) of Practice Note 10 (Revised 2022)) whether an appropriate underlying assumption is made

that, because of the nature of the entity, the services the entity performs can be expected to continue to be delivered by related public authorities and preparing the financial statements on a going concern basis will still provide a faithful representation of the items in the financial statements.

27.44 The engagement team should confirm (in accordance with paragraph 1-161(d) of Practice Note 10 (Revised 2022)) that the financial reporting framework permits the entity to prepare its financial statements on the going concern basis of accounting on the basis of the anticipated continuation of the provision of a service in the future.

27.45 The engagement team should consider whether any additional facts or information have become available since the date on which management made its assessment (as required by paragraph 12-2(e) of ISA (UK) 570 (Revised September 2019) (Updated May 2022)), including whether Parliament has made, or plans to make, a decision which is likely to impact the audited entity's continued operational existence.

Guarantees and support from third parties

27.46 As part of the evaluation of whether management's plans for future actions are feasible and likely to improve the situation required by paragraph 12-2(d) of ISA (UK) 570 (Revised September 2019) (Updated May 2022), the engagement team should assess whether:

- management's plans for future actions are based on continued support by third parties whether through loans, grant-in-aid or other funding; and
- such support is important to the audited entity's ability to continue as a going concern.

27.47 Where the third party is a central government entity including, but not limited to, the audited entity's sponsor department, the engagement team should enquire of management whether the audited entity has received any letter of comfort or guarantee from that third party and ensure any such letter of comfort or guarantee is stored in the audit documentation.

27.48 The fact that an audited entity is wholly or mostly funded by grant in aid is not in itself normally sufficient evidence that the funding will continue to be provided in the future if there is no statutory provision requiring such funding to be provided.

27.49 Some central government entities may be reluctant to provide such guarantees or letters of comfort because of the annual nature of the Parliamentary estimates process and the requirements of Box A2.2A in Annex 2.2 of Managing Public Money requiring entities to seek HM Treasury approval before entering in to guarantees, indemnities or letters of comfort creating contingent liabilities.

27.50 However, the lack of a positive confirmation from the central government third party does not in and of itself provide evidence of a material uncertainty related to going concern. The audited entity may, for example, provide evidence of clear Parliamentary intention for the body to continue its operations. The guidance in paragraph A8-15 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) applies to this situation.

27.51 Paragraph 1-175 of Practice Note 10 (Revised 2022) provides further guidance on guarantees given by statutory bodies.

27.52 ***Consultation required*** Where the engagement team judges that the going concern basis is appropriate for the preparation of a public sector entity's financial statements substantially on the basis of third-party confirmations received from the department or executive body responsible for

providing financial backing, the engagement team should consider whether this is a matter of such significance that the confirmations are referred to in the financial statements and in the audit certificate or report as being relevant to a proper understanding of the basis of the opinion. If the team consider this to be the case, they should consult FAPQ.

27.53 Where the audited entity receives a guarantee, indemnity or letter of comfort from a central government entity, the engagement team should inform the Engagement Director of that central government entity. The engagement team of the provider will need to assess the regularity of such a commitment. However, an assessment that it may be irregular for the provider does not mean that it is not sufficient evidence of continued support that demonstrates the plans of management of the recipient are feasible and, therefore, there is no material uncertainty related to the recipient's ability to continue as a going concern.

27.54 Where the entity has not obtained such evidence of continued support from the third party or parties upon whose continued support management has based its plans for future actions, the engagement team should consider whether it is necessary that management obtains such evidence from the relevant central government entity or entities. This will not be necessary if the engagement team is following the 'continued provision of service' approach.

27.55 The engagement team should evaluate any guarantees or letters of comfort to assess whether they provide sufficient evidence of adequate continued support to assess that management's plans for future actions are feasible.

27.56 The engagement team's assessment of whether the guarantees or letters of comfort provide sufficient evidence is a matter of professional judgment for the engagement team, but relevant considerations include:

- whether the entity providing the confirmation of support has the ability and resources to provide such support;
- whether the requirements of the letter are consistent with the general strategy of the entity;
- whether the letter was signed by someone with sufficient authority;
- whether the support guaranteed is sufficient for the plans;
- whether there are any terms or conditions that would restrict the audited entity's ability to carry out management's plans for future actions or which the audited entity is likely to breach; and
- whether the support covers a sufficient length of time to conclude there are no material uncertainties related to going concern for a period of at least twelve months or longer if required by the applicable financial reporting framework or law or regulation.

27.57 ***Consultation required*** If the third party is external to government, such as a finance provider, the engagement team may need to consider requesting an external confirmation (including of terms and conditions) from those third parties and to obtain evidence of their ability to provide such support. If the engagement team considers this is necessary, they should consult with FAPQ before requesting such third party confirmations.

Reporting to regulators on going concern

27.58 If the auditor is required under paragraph 25-1 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) (the auditor considers that it may be necessary to include a "Material Uncertainty Related to Going Concern" paragraph in the auditor's report or issue a qualified, adverse or disclaimer of opinion in respect of matters related to going concern) to determine whether law, regulation or relevant ethical requirements require the auditor to report to an appropriate authority outside the entity or establish responsibilities under which reporting to an appropriate authority

outside the entity may be appropriate in the circumstance, the engagement team should follow the protocol for reporting to regulators in Chapter 31: Consideration of laws and regulations and reporting to regulators. This applies to Public Interest Entities and other regulated entities, including charities regulated by the Charity Commission.

Disclosure of material uncertainty

27.59 Engagement teams should consider disclosure of any material uncertainty over the status of the body, such as because a government announcement has been made but legislation not yet passed. This is the case even where teams expect that the majority of functions and assets of the body will continue in another body.

27.60 The disclosures should be clearly tailored to the individual circumstances of the audited entity in order to draw the reader's attention to the potential impact arising from the uncertainty. For public sector bodies, a common cause of material uncertainty is government policy proposals.

Audited entities ceasing to exist

27.61 Where an audited entity is ceasing to exist there may be increased risks of irregularity as a result of:

- redundancy arrangements requiring approval within the framework of delegated authorities;
- disillusionment of staff leading to a breakdown in controls over use of funds and safeguarding of assets; and
- misuse or misappropriation of assets where they are not transferred to another body within central government.

27.62 ***Consultation required*** The engagement team should consider the impact of the closure on the assessment of audit risk within the Risk Assessment in Apex. When an audited entity ceases to exist and prepares its final set of financial statements, the C&AG may report to Parliament on the distribution of assets and liabilities. In all cases where a C&AG's Report is considered necessary, the engagement team should consult FAPQ.

Management representations

27.63 The audit documentation should include the representations received from management and, where relevant, the sponsoring body.

27.64 Knowledge of events or conditions affecting the going concern assumption is often restricted to senior management within an audited entity. When considering the applicability of the going concern assumption, the engagement team should, therefore, make enquiries and seek representations from the appropriate level within the organisation

Post-reporting period events

27.65 The risks to the C&AG's opinion related to going concern considerations typically arise from events or conditions existing at the date of the authorisation for issue of the financial statements of which the engagement team are not fully aware, and which may lead to an:

- inappropriate conclusion on the applicability of the going concern assumption; and/or
- incorrect or incomplete disclosure of events or conditions relevant to the use of the going concern assumption.

27.66 Engagement teams should therefore ensure that they consider events and conditions affecting the going concern status of the audited entity as part of their post reporting events procedures.

Concluding and reporting – use of the going concern basis is appropriate

27.67 Where the engagement team concludes that management's use of the going concern assumption is appropriate in the circumstances and no material uncertainty related to going concern exists, no modification to the opinion or the certificate is required.

27.68 In addition to the statements required by paragraph 21-1 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) to be included in the 'Conclusions relating to going concern' section of the auditor's report, where the conclusion is based on the fact the financial reporting framework provides that anticipated continuation of the provision of a service in the future will be presumed to provide sufficient evidence to prepare the financial statements on a going concern basis, the auditor's report should include an articulation of this and an explanation that the conclusions given do not amount to assurance regarding the entity's current or future financial sustainability.

Concluding and reporting – modified opinions

27.69 ***Consultation required*** In all cases where a modified audit opinion is considered the engagement teams must consult with FAPQ. This includes the cases described below.

Concluding and reporting – unable to obtain sufficient appropriate evidence

27.70 ***Consultation required*** If the auditor is required under paragraph 17-2 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) to consider the implications for the opinion of being unable to obtain sufficient appropriate evidence regarding going concern, the engagement team should consult FAPQ.

27.71 ***Consultation required*** If the audited entity's going concern status is complex or there are significant concerns with respect to the financial sustainability of the services being delivered, the engagement team should consult with FAPQ and set out their consideration of the need for a report on accounts as per paragraph 1-179 of Practice Note 10 (Revised 2022).

Concluding and reporting – material uncertainty related to going concern exists

27.72 ***Consultation required*** Where a material uncertainty related to going concern exists and appropriate disclosure about the material uncertainty related to going concern is made in the financial statements, the engagement team should consult FAPQ with their proposals to include in the auditor's report a 'Material uncertainty related to going concern paragraph' as per paragraph 22 of ISA (UK) 570 (Revised September 2019) (Updated May 2022).

27.73 ***Consultation required*** Where a material uncertainty related to going concern exists and appropriate disclosure about the material uncertainty related to going concern is not made in the financial statements, the engagement team should consult FAPQ with their proposals to express a qualified or adverse opinion, as appropriate, and in the 'Basis for Qualified (Adverse) Opinion' section of the auditor's report, state that a material uncertainty exists that may cast significant doubt on the entity's ability to continue as a going concern and that the financial statements do not

appropriately disclose this matter, as per paragraph 23 of ISA (UK) 570 (Revised September 2019) (Updated May 2022).

Concluding and reporting – inappropriate basis used in preparing the financial statements

27.74 ***Consultation required*** Where the financial statements have been prepared using the going concern basis of accounting but, in the auditor's judgment, management's use of the going concern basis of accounting in the preparation of the financial statements is inappropriate, the engagement team should consult FAPQ with their proposals to express an adverse opinion as per paragraph 21 of ISA (UK) 570 (Revised September 2019) (Updated May 2022).

Concluding and reporting – financial statements prepared on a basis other than going concern

27.75 Where management concludes that the going concern basis is no longer appropriate, they will need to prepare the financial statements on an appropriate alternative basis.

27.76 ***Consultation required*** In such circumstances, the engagement team should consult with FAPQ and consider the appropriateness of the basis of preparation with particular reference to the valuation of assets, completeness of recognised liabilities and the completeness of disclosures.

27.77 ***Consultation required*** Where the financial statements are prepared on a basis other than going concern, it is NAO policy to draw attention to this within the audit certificate/report. In these circumstances, the engagement team should consult FAPQ on the form of reporting.

Chapter 28: Related parties

Relevant standards and guidance

28.1 ISA (UK) 550 (Updated May 2022) *Related parties* deals with the auditor's responsibilities relating to related party relationships and transactions in an audit of financial statements.

28.2 Paragraphs 1-116 to 1-119 of Practice Note 10 *Audit of financial statements and regularity of public sector bodies in the United Kingdom* (Revised 2022) provide guidance on applying ISA (UK) 550 (Updated May 2022) in the public sector.

Background

28.3 As with other audit areas, the approach to auditing transactions with related parties should be risk-focused.

28.4 Risks of material misstatement can arise in a number of ways:

- related party transactions may be less well documented than other transactions, and so it may be more difficult to determine their substance and appropriate accounting and disclosure;
- related party transactions may be structured in complex ways, possibly involving several other bodies;
- transactions with key management, or related parties connected to key management, may give rise to issues of irregularity or impropriety, particularly if not conducted under normal market terms and conditions;
- the nature of some related party transactions mean that audited entity's information systems may not appropriately capture transactions or balances;
- audited entities may rely on information supplied by related parties without checking or assessing that information themselves; or
- related party transactions may not be subject to the same types of transactional controls in place around other types of income and expenditure.

28.5 The engagement team has a responsibility to:

- obtain an understanding of the entity's related party relationships and transactions;
- assess whether there is a risk of fraud in relation to related party transactions;
- assess whether there are other risks of material misstatement related to related party transactions;
- perform audit procedures to assess the completeness and accuracy of the financial statement disclosures; and
- perform audit procedures to respond to any identified risks of material misstatement.

28.6 Professional scepticism is particularly important in the audit of related parties, as there are inherent limitations on our ability to detect misstatements. Examples include:

- management may be unaware of the existence of all related party relationships and transactions; or
- related party relationships may present a greater opportunity for collusion, concealment or manipulation by management.

28.7 In the context of audits of bodies where a "true and fair" audit opinion is given under the FReM, IFRS or the UK GAAP, the objectives of the engagement team are:

- to obtain a sufficient understanding of related party relationships and transactions:

- to recognise fraud risk factors, if any, arising from related party relationships and transactions that are relevant to the identification and assessment of the risks of material misstatement due to fraud;
- to conclude, based on the audit evidence obtained, whether the financial statements, insofar as they are affected by those relationships and transactions achieve fair presentation; and
- to obtain sufficient appropriate audit evidence about whether related party relationships and transactions have been appropriately identified, accounted for and disclosed in the financial statements in accordance with the applicable financial reporting framework.

28.8 Where audits are performed under other accounting frameworks, or for audits where there is not a "true and fair" audit opinion (i.e. those conducted under a compliance framework with a "properly prepared" opinion, such as cash accounts), the objectives of the engagement team are:

- irrespective of whether the applicable financial reporting framework establishes related party requirements, to obtain an understanding of related party relationships and transactions sufficient to be able:
  - to recognise fraud risk factors, if any, arising from related party relationships and transactions that are relevant to the identification and assessment of the risks of material misstatement due to fraud;
  - to conclude, based on the audit evidence obtained, whether the financial statements, insofar as they are affected by those relationships and transactions achieve fair presentation (for fair presentation frameworks) or are not misleading (for compliance frameworks); and
- where the applicable financial reporting framework establishes related party requirements, to obtain sufficient appropriate audit evidence about whether related party relationships and transactions have been appropriately identified, accounted for and disclosed in the financial statements in accordance with the framework.

Related party disclosure requirements in the public sector

28.9 The FReM interprets IAS 24 *Related party disclosures* in a public sector context. The disclosure requirements for public bodies are a combination of those required under IFRS and specific additional disclosures for public accountability. Related parties in the public sector might include the following:

- sponsoring bodies or departments;
- subsidiary bodies;
- other public sector bodies; and/or
- Ministers, members of the management board, trustees, key management personnel and their close family members and connected businesses.

28.10 The relationship between a Government Department and its sponsored bodies is not exactly the same as that between a parent company and its subsidiaries, but HM Treasury has stipulated that the principles of IAS 24 *Related party disclosures* should apply to transactions between Government Departments and their sponsored bodies.

28.11 The definition of related parties includes any entities that members of key management or their close family members control, jointly control, significantly influence, or directly or indirectly have significant voting power over. For entities who follow the FReM, further guidance and interpretations on the definition of a related party can be found chapter 5 of the FReM.

28.12 Close members of the family of a person are defined in paragraph 9 of IAS 24 as those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity, which include:

- the individual's domestic partner and children;
- children of the individual's domestic partner; and
- dependants of the individual or the individual's domestic partner.

Other reporting frameworks (such as the Charities SORP – see the definition of 'Related parties' in Appendix 1: Glossary of terms) may adopt different definitions from that in IAS 24.

28.13 The disclosure requirements can be summarised as:

- entities should disclose their parent department (if any);
- for transactions with other government bodies, central government entities do not need to detail each transaction – they should disclose the main entities within government with which the entity has had dealings;
- the compensation paid to management, expense allowances and similar items paid in the ordinary course of an entity's operations should be disclosed in the notes to the accounts or in the Remuneration Report as appropriate (note that where disclosure requirements of International Accounting Standards are satisfied via the disclosures given in the Remuneration Report, the Related Party note to the accounts should include cross reference to the Remuneration Report); and
- details of material transactions between the entity and individuals or non-governmental bodies who are regarded as related parties should be disclosed.

28.14 These disclosures, together with other disclosures requirements in the FReM (for example, about the funding of the entity, which demonstrates its dependence on related parties), will usually suffice to give a true and fair view.

28.15 However, teams should remain alert to the possibility that additional disclosures may be required to provide a fair presentation of particular transactions.

28.16 The materiality of related party transactions should be considered from the perspective of each party involved, so relatively low value transactions with individuals or companies could be material, based on the significance to the other party.

28.17 Teams should be alert to circumstances where someone who has control or significant influence over an entity, or a close member of their family also has control or significant influence over a company. Where this is the case, that company would be a related party.

Risk assessment procedures

28.18 The engagement team should ensure related parties are scoped in as a Financial Statement Risk Area (FSRA) within the Risk Assessment in Apex. The default placement on the spectrum of inherent risk of RoMMs associated with related parties should not be manually overridden into the Target position – this ensures compliance with the risk assessment requirements in ISA (UK) 550 (Updated May 2022) and that mandatory procedures are included in the engagement team's response to related parties risks.

28.19 Where the engagement team considers that controls over related party relationships and transactions are relevant to the audit (either because there is a RoMM over related parties where either or both of the Financial Statement Impact (magnitude) and Likelihood placements are High or

because the engagement team plans to obtain assurance from the operating effectiveness of such controls) they should evaluate the design and implementation of these controls.

28.20 The NAO's audited entities are expected to, at least:

- maintain a comprehensive list of related parties;
- have policies and procedures for open and timely disclosure of the interests that management and those charged with governance have in related party transactions;
- have clear guidelines for the approval of related party transactions involving actual or perceived conflicts of interest, such as approval by a subcommittee of those charged with governance comprising individuals independent of management; and
- put in place whistle-blowing policies and procedures.

28.21 If these processes and controls are not in place, the engagement team should consider whether this represents a control deficiency and whether this gives rise to a significant risk or otherwise affects our audit approach. Paragraphs 9, A12 to A18 and A27 of ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* include requirements to communicate in writing significant deficiencies in internal control identified during the audit to those charged with governance on a timely basis; paragraphs 11 and A28 to A30 set out matters required to be included in this written communication.

28.22 The engagement team discussion on risk and fraud will include a specific consideration of how related parties may be involved in fraud. For example, how transactions between the entity and a known business partner of a key member of management could be arranged to facilitate misappropriation of the entity's assets.

28.23 Even in the case of transactions wholly within the public sector it is possible that related party transactions could be used in fraudulent financial reporting. For example, transactions between government bodies could be structured in a way that did not reflect the substance of transactions.

28.24 Other individuals the engagement team may wish to inquire of include:

- those charged with governance;
- internal audit;
- in-house legal counsel; and
- personnel in a position to initiate, process, or record transactions that are both significant and outside the entity's normal course of business, and those who supervise or monitor such personnel.

28.25 Where applicable, the engagement team would also ordinarily:

- review invoices and correspondence from lawyers for indications of the existence of related parties or related party transactions;
- inquire of the names of all pension and other trusts established for the benefit of employees and the names of their management; and
- review the entity's income tax returns and other information supplied to its sponsoring body or regulatory agencies.

28.26 Examples of other documents which may provide information about related party relationships or transactions include:

- other third-party confirmations;
- statements of conflicts of interest from management and those charged with governance;
- records of the entity's investments and those of its pension plans;
- contracts and agreements with key management or those charged with governance;

- significant contracts and agreements not in the entity's ordinary course of business;
- specific invoices and correspondence from the entity's professional advisors;
- significant contracts re-negotiated by the entity during the period; and
- internal auditors' reports.

28.27 Information would usually be shared as part of the Engagement Team discussion and then team members updated as additional information comes to light.

28.28 Matters to share information about include:

- the identity of the entity's related parties;
- the nature of the related party relationships and transactions; and
- significant or complex related party relationships or transactions that may require special audit consideration, in particular transactions in which management or those charged with governance are financially involved.

Identifying and responding to risks of material misstatement associated with related parties

28.29 The following may be RoMMs associated with related party relationships and transactions:

- the related parties listing is incomplete;
- the related parties listing includes incorrect entries;
- related party transactions did not occur or have been incorrectly calculated;
- transactions or balances with related parties are incorrectly disclosed as having been conducted at arm's length;
- transactions or balances with related parties are incorrectly disclosed as not having been conducted at arm's length;
- transactions and bad debt balances with related parties are not disclosed; or
- the audited entity incorrectly applies exemptions from disclosure of related party relationships or transactions.

28.30 Risks of material irregular transactions may also arise where related party transactions are not in accordance with the framework of authorities.

28.31 If any significant related party transactions outside the entity's normal course of business have been identified, paragraph 18 of ISA (UK) 550 (Updated May 2022) requires this to be treated as giving rise to a significant risk. requires this to be treated as giving rise to a significant risk.

28.32 Entities are required to disclose their ultimate controlling party within the financial statements. For the majority of the NAO's audit portfolio, this is likely to be the entity's sponsor department. The engagement team is required to document the identity of the entity's ultimate controlling party.

28.33 Examples of indicators of outside the normal course of business may include the following:

- abnormal terms of business;
- no logical business reason for their occurrence;
- high volume or high value transactions with certain organisations or individuals when compared to others;
- substance differs from form; or
- unusual manner of processing.

28.34 Audit procedures to obtain assurance that there are not unidentified related party transactions could include one or more of:

- detailed tests of transactions and balances;
- reviewing minutes of meetings of management and those charged with governance;
- analysing registers of interests;
- reviewing accounting records for large or unusual transactions, and transactions with senior management and/or trustees paying particular attention to the beginning and the end of the reporting period;
- reviewing bank letters, loan confirmations and any other third party confirmations received, as these may indicate a guarantor relationship or other related party transactions; or
- reviewing investment transactions, such as the purchase or sale of an interest in a joint venture or other entity.

28.35 Audit procedures to obtain assurance about the substance of the transaction (to enable the engagement team to conclude on the appropriateness of the accounting and disclosure) could include one or more of:

- discussions of the purpose of the transaction with management or those charged with governance;
- confirmation of the transaction, including the terms and the amount with the related party;
- reviewing information held by the related party;
- confirming the explanation of the purpose of the transaction in question with the related party; or
- confirming or discussing the information with others involved in the transaction, such as lawyers, banks, guarantors and agents.

28.36 Examples of possible responses to significant risks around related party transactions include:

- confirming or discussing specific aspects of the transactions with intermediaries such as banks, law firms, guarantors or agents where practicable and not prohibited by law, regulation or ethical rules;
- confirming the purposes, specific terms or amounts of the transactions with the related party (this audit procedure may be less effective where engagement teams judge that the entity is likely to influence the related party in their responses); or
- where applicable, reading the financial statements or other available relevant financial information of the related parties for evidence of the accounting of the transactions in the related parties' accounting records.

28.37 In practice, it may be difficult for management to evidence a statement a transaction is on arms-length terms given the nature of public body's activities. To make the assertion, management should have evidence available to support the statement, which may include:

- a comparison of the terms of the related party transaction to those of an identical or similar transaction with one or more unrelated parties;
- having engaged an external expert to determine a market value and to confirm market terms and conditions for the transaction; or
- a comparison the terms of the transaction to known market terms for broadly similar transactions on an open market.

Evaluating and concluding

28.38 For audits where there is not a "true and fair" audit opinion (i.e. those conducted under a compliance framework with a "properly prepared" opinion, such as cash accounts), engagement teams would evaluate whether they cause the financial statements to be misleading rather than prevent fair presentation.

28.39 Some of the specific considerations around regularity in respect of related parties and related party transactions include:

- a public sector organisation entering into a contract on non-’rm's length terms with a related party;
- the write-off of related party receivables;
- failure to obtain approval for novel and contentious payments, including ex gratia severance; and/or
- expenditure to related parties in excess of Cabinet Office limits

28.40 Where an irregular related party transaction is identified the decision to qualify the audit opinion should consider materiality based on the significance of the transaction. Further guidance on evaluation of materiality in the context of the regularity opinion can be found in paragraphs 2-33 to 2-37 of Practice Note 10 (Revised 2022).

28.41 Examples of significant related party matters include:

- non-disclosure (whether intentional or not) by management to the team of related parties or significant related party transactions, which may alert those charged with governance to significant related party relationships and transactions of which they may not have been previously aware;
- the identification of significant related parties that have not been appropriately authorised and approved, which may give rise to suspected fraud;
- disagreement with management regarding the accounting for and disclosure of significant related party transactions in accordance with the financial reporting framework; and/or
- non-compliance with applicable law or regulations prohibiting or restricting specific types of related party transactions.

28.42 Significant related party issues, in particular significant related party transactions outside the ordinary course of business, may be significant documentation matters. For significant documentation matters our documentation should be sufficient to enable an experienced auditor, having no previous connection with the audit, to:

- understand the issue;
- understand the conclusions reached; and
- understand any significant professional judgments made in reaching those conclusions.

28.43 Documentation of the professional judgments made, where significant, serves to explain our conclusions and to reinforce the quality of the judgment in the file.

Chapter 29: Comparative information

Relevant standards and guidance

29.1 ISA (UK) 710 *Comparative information – corresponding figures and comparative financial statements* deals with the auditor's responsibilities relating to comparative information in an audit of financial statements.

29.2 ISA (UK) 510 (Revised June 2016) *Initial audit engagements – opening balances* deals with auditor's responsibilities relating to opening balances in an initial audit engagement.

29.3 Paragraphs 1-97 to 1-107 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 510 (Revised June 2016) in the public sector.

Background

29.4 The FReM requires audited entities to include comparative information in the financial statements. UK GAAP has similar reporting requirements.

29.5 The information included is referred to by the ISAs (UK) as "corresponding figures", as amounts and other disclosures for the prior period are included as an integral part of the current period financial statements, and are intended to be read only in relation to the amounts and other disclosures relating to the current period (referred to as "current period figures"). The level of detail presented in the corresponding amounts and disclosures is dictated primarily by its relevance to the current period figures.

29.6 Although the engagement team have responsibilities in respect of the comparative information, the C&AG's opinion refers only to the current period.

29.7 This Chapter also deals with opening balances in an initial audit engagement. An initial audit engagement is defined in paragraph 4(a) of ISA (UK) 510 (Revised June 2016) as an engagement in which either the financial statements for the prior period were not audited or the financial statements for the prior period were audited by a predecessor auditor. In addition to financial statement amounts, opening balances include disclosures relating to the prior year-end, such as contingencies and commitments.

29.8 As set out in paragraph 5 of ISA (UK) 710 and paragraph 3 of ISA (UK) 510 (Revised June 2016), the objectives of the engagement team are:

- to obtain sufficient appropriate audit evidence about whether:
    - the comparative information included in the financial statements has been presented, in all material respects, in accordance with the requirements for comparative information in the applicable financial reporting framework;
    - opening balances contain misstatements that materially affect the current period's financial statements; and
    - appropriate accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, or changes thereto are appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework; and
- to report in accordance with the auditor's reporting responsibilities.

29.9 The extent of procedures required to obtain evidence over opening balances is a matter of professional judgement. Accordingly, the Engagement Director should decide as part of establishing the overall audit strategy the planned approach to obtaining assurance.

Effect of prior period misstatements on current period financial statements

29.10 Where a misstatement in the prior year is corrected through an adjustment in the current year, the engagement team should consider whether that adjustment constitutes a misstatement in the current year financial statements due to the transaction or balance being recognised in an incorrect accounting period. Paragraph A3-1 of ISA (UK) 710 sets out that this may lead to a qualified opinion on the current period financial statements in some circumstances.

Prior period financial statements audited by the NAO

29.11 ***Consultation required*** If the engagement team becomes aware of a possible material misstatement in the comparative information, and the NAO audited the prior period's financial statements, they must consult with FAPQ about whether the requirements of paragraphs 14 to 17 of ISA (UK) 560 *Subsequent events* (facts which become known to the auditor after the financial statements have been issued) apply. If, following these requirements, the prior period financial statements are amended, the engagement team should determine whether the comparative information agrees with the amended financial statements.

Initial audit engagements – opening balances

29.12 The considerations set out in this Chapter regarding initial audit engagements do not apply:

- when contracted out audits of central government bodies are brought back within the NAO; or
- when engagement teams are changed within the NAO.

29.13 The considerations set out in this Chapter regarding initial audit engagements will usually only apply to charity or company audits where an entity has existed for a number of years and either has not been audited or has been audited by another auditor.

29.14 When considering opening balances which were not audited by the NAO, the engagement team should consider where issues might arise. These will usually either be:

- items such as intangible assets, PPE, or slow-moving inventories which are also reflected in the closing balance sheet; or
- items such as debtors or creditors where errors in the opening balance sheet would be expected to be reverse through the income statement in the year.
- In general, risks may arise in the comparative information/opening balances for entities that have transferred into the public sector or entities audited by members of firms not otherwise familiar with the public sector.

29.15 The Engagement Director should decide as part of establishing the overall audit strategy the planned approach to obtaining assurance over opening balances for initial audit engagements. This should take into account any assurance obtained from review of predecessor auditor's working papers as part of engagement acceptance.

29.16 Section 5: New engagements and standing information includes additional requirements and guidance regarding activities prior to starting an initial audit.

29.17 As required by paragraph 5 of ISA (UK) 510 (Revised June 2016), the engagement team should read the most recent financial statements, if any, and the predecessor auditor's report thereon, if any, for information relevant to opening balances, including disclosures.

29.18 As required by paragraph 6 of ISA (UK) 510 (Revised June 2016), the engagement team should obtain sufficient appropriate audit evidence about whether the opening balances contain misstatements that materially affect the current period's financial statements by:

- determining whether the prior period's closing balances have been correctly brought forward to the current period or, when appropriate, have been restated;
- determining whether the opening balances reflect the application of appropriate accounting policies; and
- performing one or more of the following:
    - where the prior year financial statements were audited, reviewing the predecessor auditor's working papers to obtain evidence regarding the opening balances;
    - evaluating whether audit procedures performed in the current period provide evidence relevant to the opening balances; or
    - performing specific audit procedures to obtain evidence regarding the opening balances.

29.19 As per paragraph A3 of ISA (UK) 510 (Revised June 2016), the nature and extent of audit procedures necessary to obtain sufficient appropriate audit evidence regarding opening balances is a matter of professional judgement and depends on considerations such as:

- the accounting policies followed by the entity;
- the nature of the classes of transactions, account balances and disclosures (COTABDs) and RoMMs in the current period's financial statements;
- the significance of the opening balances relative to the current period's financial statements; and
- whether the prior period's financial statements were audited and, if so, whether the predecessor auditor's opinion was modified.

29.20 As required by paragraph 7 of ISA (UK) 510 (Revised June 2016), if the engagement team obtains audit evidence that the opening balances contain misstatements that could materially affect the current period's financial statements, they should perform such additional audit procedures as are appropriate in the circumstances to determine the effect on the current period's financial statements. If the engagement team concludes that such misstatements exist in the current period's financial statements, they should communicate the misstatements with the appropriate level of management and those charged with governance in accordance with ISA (UK) 450 (Revised June 2016) (Updated May 2022) *Evaluation of misstatements identified during the audit*.

29.21 The engagement team should obtain written representations in respect of the opening balances as part of an initial audit.

29.22 As required by paragraph 8 of ISA (UK) 510 (Revised June 2016), the engagement team should obtain sufficient appropriate audit evidence about whether the accounting policies reflected in the opening balances have been consistently applied in the current period's financial statements, and whether changes in the accounting policies have been appropriately accounted for and adequately presented and disclosed in accordance with the applicable financial reporting framework.

29.23 Paragraph 8R-1 of ISA (UK) 510 (Revised June 2016) includes additional requirements relating to initial audits of Public Interest Entities.

29.24 As required by paragraph 9 of ISA (UK) 510 (Revised June 2016), if the prior period's financial statements were audited by a predecessor auditor and there was a modification to the

opinion, the engagement team should evaluate the effect of the matter giving rise to the modification in assessing the risks of material misstatement in the current period's financial statements in accordance with ISA (UK) 315 (Revised June 2016).

29.25 The engagement team should express a qualified opinion, express an adverse opinion or disclaim an opinion on the financial statements, as appropriate, if:

- the engagement team are unable to obtain sufficient appropriate audit evidence regarding the opening balances (as required by paragraph 10 of ISA (UK) 510 (Revised June 2016));
- the engagement team conclude that the opening balances contain a misstatement that materially affects the current period's financial statements, and the effect of the misstatement is not appropriately accounted for or not adequately presented or disclosed (as required by paragraph 11 of ISA (UK) 510 (Revised June 2016));
- the engagement team conclude that the current period's accounting policies are not consistently applied in relation to opening balances in accordance with the applicable financial reporting framework (as required by paragraph 12(a) of ISA (UK) 510 (Revised June 2016));
- the engagement team conclude that a change in accounting policies is not appropriately accounted for or not adequately presented or disclosed in accordance with the other applicable financial reporting framework (as required by paragraph 12(b) of ISA (UK) 510 (Revised June 2016)); or
- the predecessor auditor's opinion regarding the prior period's financial statements included a modification to the auditor's opinion that remains relevant and material to the current period's financial statements (as required by paragraph 13 of ISA (UK) 510 (Revised June 2016)).

Initial audit engagements – considerations for particular categories of opening balances

29.26 For items which will be reflected in the year-end balance sheet, the engagement team should consider how to obtain sufficient appropriate audit evidence about the opening values of the items.

29.27 For balances where errors in the opening balance sheet would be expected to reverse to give a correct closing position (such as an unaccrued expense), the engagement team should consider whether it is appropriate to review for unexpected costs or income in the current period.

29.28 For current assets and liabilities, some audit evidence about opening balances may be obtained as part of the current period's audit procedures. For example, the collection (payment) of opening accounts receivable (accounts payable) during the current period will provide some audit evidence of their existence, rights and obligations, completeness and valuation at the beginning of the period.

29.29 In the case of inventories, however, the current period's audit procedures on the closing inventory balance provide little audit evidence regarding inventory on hand at the beginning of the period. Therefore, additional audit procedures may be necessary, and one or more of the following may provide sufficient appropriate audit evidence:

- observing a current physical inventory count and reconciling it to the opening inventory quantities;
- performing audit procedures on the valuation of the opening inventory items; and/or
- performing audit procedures on, for example, gross margins and cut-off.

29.30 For non-current assets and liabilities, such as property plant and equipment, investments and long-term debt, some audit evidence may be obtained by examining the accounting records and other information underlying the opening balances. In certain cases, it may be possible to obtain some audit evidence regarding opening balances through confirmation with third parties, for

example, for long- term debt and investments. In other cases, the engagement team may need to carry out additional audit procedures.

Initial audit engagements – prior period financial statements audited by another auditor

29.31 For UK audits, auditors do not refer to the predecessor auditor's report on the corresponding figures in their audit reports. The C&AG assumes responsibility for the corresponding figures, although only in the context of the financial statements as a whole.

29.32 If the prior period's financial statements were audited by a predecessor auditor, it may not be possible to obtain sufficient appropriate audit evidence regarding the opening balances by reviewing the predecessor auditor's working papers.

29.33 When evaluating the professional competence and independence of a predecessor auditor to determine whether a review of their working papers provides sufficient appropriate audit evidence in accordance with paragraph A4 of ISA (UK) 510 (Revised June 2016), the engagement team should apply the principles set out in ISA (UK) 600 (Revised September 2022) *Special considerations – audits of group financial statements (including the work of component auditors*, regarding the professional competence and independence of component auditors, for these purposes.

29.34 The engagement team should read the preceding period's financial statements and, using the knowledge gained during the current audit, consider whether they have been properly reflected as corresponding figures in the current period's financial statements.

29.35 Although not required to re-audit the financial statements of the preceding period, the engagement team may become aware of a possible material misstatement of corresponding figures.

29.36 ***Consultation required*** For other audits, the engagement team may be able to refer to a predecessor auditor's report in our opinion. If the engagement team are not prohibited by law or regulation from doing so, they should consider whether it is appropriate to do so in consultation with FAPQ. If the engagement team decides to refer to the predecessor auditor, they should refer to paragraph 13 of ISA (UK) 710.

29.37 If the engagement team becomes aware of a possible material misstatement in the comparative information while performing the current period audit, they should perform such additional audit procedures as are necessary in the circumstances to obtain sufficient appropriate audit evidence to determine whether a material misstatement exists.

Written representations

29.38 The request for written representations for all periods referred to in the audit opinion required by paragraph 9 of ISA (UK) 710 and paragraph 14 of ISA (UK) 580 (Updated May 2022) *Written representations* will usually consist of a request for representations on the current period financial statements only, as they include the corresponding figures.

Chapter 30: Fraud responsibilities

Relevant standards and guidance

30.1 ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* deals with the auditor's responsibilities relating to fraud in an audit of financial statements. Specifically, it expands on how ISA (UK) 315 (Revised July 2020) and ISA (UK) 330 (Revised July 2017) (Updated May 2022) are to be applied in relation to risks of material misstatement due to fraud. The objectives of the auditor under ISA (UK) 240 (Revised May 2021) (Updated May 2022) are:

- to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement due to fraud, including:
    - identifying and assessing the risks of material misstatement of the financial statements due to fraud;
    - obtaining sufficient appropriate audit evidence regarding the assessed risks of material misstatement due to fraud, through designing and implementing appropriate responses; and
- to respond appropriately to fraud or suspected fraud identified during the audit.

30.2 Paragraphs 1-38 to 1-51 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 240 (Revised May 2021) (Updated May 2022) in the public sector.

The nature of fraud

30.3 Financial statements can be misstated due to either fraud or error. What distinguishes instances of fraud is that they are intentional. Two types of intentional misstatements are relevant to NAO audits:

- misstatements resulting from fraudulent financial reporting; and
- misstatements resulting from misappropriation of assets.

30.4 Although the NAO's responsibilities under ISAs (UK) are focussed upon the risk of material misstatement through fraud by management, the risk of irregularity arising due to external fraud is also considered. Irregular transactions arising from external fraud may be of particular interest to users of the financial statements.

30.5 The risk of external fraud may be particularly high where a body is involved in issuing grants or benefits to the public or collecting tax revenues as there is an increased risk of fraudulent activity by individuals or groups outside of the immediate control of the audited entity, for example fraudulent benefit or prescription claims.

Definition of fraud

30.6 Fraud is defined in a legal sense in the Fraud Act 2006. 'Fraud' involves the use of deception to obtain an unjust or illegal financial advantage as well as intentional misstatements in, or omissions of amounts or disclosures from, an entity's accounting records or financial statements. It includes acts of bribery, forgery, extortion, corruption, theft, conspiracy, embezzlement, misappropriation, false representation, concealment of material facts and collusion. 'Fraud' involves the use of deception to obtain an unjust or illegal financial advantage as well as intentional misstatements in, or omissions of amounts or disclosures from, an entity's accounting records or financial statements. It

includes acts of bribery, forgery, extortion, corruption, theft, conspiracy, embezzlement, misappropriation, false representation, concealment of material facts and collusion.

30.7 Fraud includes both dishonest acts committed by employees or management of the audited entity ('internal Fraud') and dishonest acts perpetrated against the audited entity by outside individuals or group‘ ('external Fraud'). Internal fraud may result in benefits being obtained either from the organisation (for example, theft of cash/assets, falsification of payroll data), or from a third party (for example, the theft of patient's property). The latter may not result in immediate loss to the audited entity, but it may result in a liability for compensation where positions of trust have been abused. Examples of external fraud include making fraudulent claims for benefits or suppliers issuing false or duplicate invoices.

Responsibilities of those charged with governance and management in respect of fraud

30.8 The primary responsibility for the detection of fraud rests with those charged with governance and with management. Their role in the detection of fraud is an extension of their role in preventing fraudulent activity.

30.9 The Accounting Officer is responsible for establishing a sound system of internal control designed to support the achievement of departmental policies, aims and objectives and to manage the risks facing the organisation; this includes the risk of fraud. The responsibilities of the Accounting Officer and senior management of an entity are defined in chapter 3 of Managing Public Money.

30.10 The Accounting Officer is also responsible for ensuring that the financial statements are prepared and give a true and fair view of the state of affairs of the entity and its transactions in the course of a financial year. The Accounting Officer therefore has a duty, where material fraud or error has occurred, to ensure that the matter is appropriately reflected and/or disclosed in the financial statements.

30.11 Departments are required to formulate a fraud policy and communicate this to all staff. This should be supported by a fraud response plan which is designed to ensure that timely and effective action can be taken if a fraud is identified. The department must undertake an investigation when fraud is identified or suspected and take the appropriate legal and/or disciplinary action in proven cases.

Responsibilities of the auditor in respect of fraud

30.12 An audit of financial statements is designed to provide reasonable assurance that the financial statements (as a whole) are free from material misstatement, whether caused by fraud or error. The auditor is not responsible for preventing fraud or corruption from occurring, although an audit may serve to act as a deterrent.

30.13 ISAs (UK) and, in particular, ISA (UK) 240 (Revised May 2021) (Updated May 2022) require the engagement team to consider fraud at all stages in the audit process. require the engagement team to consider fraud at all stages in the audit process.

30.14 The audit documentation should reflect the engagement team’s attitude of professional scepticism, which is required by paragraph 13 of ISA (UK) 240 (Revised May 2021) (Updated May 2022).

30.15 ***Consultation required*** Where the engagement team has identified or suspects a fraud, the Engagement Director should, as required by paragraph 44 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), determine whether law, regulation or relevant ethical requirements:

- Require the auditor to report to an appropriate authority outside the entity. Any reports to an appropriate external authority must be approved by the Director, Financial Audit, Practice and Quality.
- Establish responsibilities under which reporting to an appropriate authority outside the entity may be appropriate in the circumstances. Where the responsibilities for reporting to appropriate authorities outside of the entity are unclear, the engagement team may consult with FAPQ and obtain external legal advice.

30.16 As noted in paragraph A6 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), law, regulation or relevant ethical requirements may require the engagement team to perform additional procedures and take further actions. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements., law, regulation or relevant ethical requirements may require the engagement team to perform additional procedures and take further actions. Such steps may include the communication of identified or suspected non-compliance with laws and regulations to other auditors within a group, including a group engagement partner, component auditors or other auditors performing work at components of a group for purposes other than the audit of the group financial statements.

Fraud risk assessment – inquiries of management and those charged with governance

30.17 The engagement team should make inquiries of the following in order to obtain information for use in identifying the risks of material misstatement due to fraud:

- management (as required by paragraphs 18 to 19 and A13 to A18-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022));
- others within the entity, as appropriate to address RoMMs resulting from management fraud (examples given in paragraph A17 of ISA (UK) 240 (Revised May 2021) (Updated May 2022));
- those charged with governance (as required by paragraphs 21 to 22-1 and A20 to A20 of ISA (UK) 240 (Revised May 2021) (Updated May 2022));
- if separate from management, those who deal with allegations, if any, of fraud raised by employees or other parties (as required by paragraphs 19-1 and A17-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022)); and
- internal audit (as required by paragraphs 20 and A19 of ISA (UK) 240 (Revised May 2021) (Updated May 2022)).

30.18 The mandated inquiries of management and those charged with governance in respect of fraud (as required by paragraphs 18 to 22-2 of ISA (UK) 240 (Revised May 2021) (Updated May 2022)) are often made during the initial planning meeting(s) as part of establishing the Overall Audit Strategy, but may be conducted later in planning. See Chapter 15: Gathering entity initial information for further guidance on making planning inquiries. for further guidance on making planning inquiries.

30.19 In accordance with paragraphs 22-1 and A21-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team should discuss with those charged with governance the risks of fraud in the entity, including those that are specific to the entity's business sector. The discussion with those charged with governance should also cover how these fraud risk factors may impact the financial statements and areas of the financial statements that may be susceptible to fraud. The discussion with those charged with governance should also cover how these fraud risk

factors may impact the financial statements and areas of the financial statements that may be susceptible to fraud.

30.20 Inconsistencies may arise in responses to inquiries between those from those charged with governance, management and others within the entity. Paragraph 22-2 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires the engagement team to determine the implications for the audit of any such inconsistencies. requires the engagement team to determine the implications for the audit of any such inconsistencies.

30.21 The engagement team should reconfirm the inquiries at a later stage in the audit, where appropriate.

30.22 The procedures specified in paragraphs 21 to 22-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) will usually be relevant to NAO audits, notwithstanding that they do not apply where all of those charged with governance are involved in managing the entity, since public sector bodies should have independent members of the audit committee. will usually be relevant to NAO audits, notwithstanding that they do not apply where all of those charged with governance are involved in managing the entity, since public sector bodies should have independent members of the audit committee.

Fraud risk assessment – analytical procedures

30.23 In accordance with paragraph 23 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team should evaluate whether unusual or unexpected relationships that have been identified in performing analytical procedures, including those related to revenue accounts, may indicate fraud-related RoMMs.

Fraud risk assessment – engagement team discussions

30.24 The engagement team should hold a discussion on risk and fraud. Paragraph 17 of ISA (UK) 315 (Revised July 2020) requires the engagement team to discuss the application of the applicable financial reporting framework and the susceptibility of the entity's financial statements to material misstatement. As per paragraph A42 of ISA (UK) 315 (Revised July 2020), paragraph 16 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires this discussion to place particular emphasis on how and where the entity's financial statements (including the disclosures) may be susceptible to material misstatement due to fraud, including how fraud might occur. requires this discussion to place particular emphasis on how and where the entity's financial statements (including the disclosures) may be susceptible to material misstatement due to fraud, including how fraud might occur.

30.25 The discussion should be led by the Engagement Director and attended by the whole engagement team (including specialists). In accordance with paragraph 18 of ISA (UK) 315 (Revised July 2020), the Engagement Director should ensure the Apex audit file includes documentation of how any members of the engagement team who could not attend the discussion will be:, the Engagement Director should ensure the Apex audit file includes documentation of how any members of the engagement team who could not attend the discussion will be:

- made aware of the content of the discussion and its outcomes for the audit and
- given the opportunity to feed into the ongoing risk assessment regarding risk and fraud throughout the audit.

30.26 The discussion should be documented in the Engagement Team Discussion on Risk and Fraud template.

30.27 The discussion should be focused on the fraud risk factors listed in the 'Discussion fraud risk factors' tab in the template. These fraud risk factors are all Generic Inherent Risk Factors (GIRFs) within the Risk Assessment in Apex. The engagement team should discuss these fraud risk factors and consider for each:

- whether the GIRF is present for the audited entity;
- for those that are present, whether the GIRF could have a material impact on the financial statements, either individually or in combination with other risk factors; and
- for those that are present and could have a material impact, which Financial Reporting Activities may be impacted by the GIRF.

30.28 In discussing fraud risk factors, the engagement team may find it helpful to first consider whether or not they are present before holding a more holistic discussion around which fraud risk factors either individually or in combination with other fraud risk factors may lead to a material fraud. This holistic discussion should consider whether all elements of the fraud triangle would need to be present for there to be a material fraud in practice.

30.29 The engagement team should ensure the outcome of this discussion is reflected within the scoping of the audit carried out in the Risk Assessment in Apex per Chapter 17: Risk assessment and response planning.

30.30 In accordance with paragraphs 16-4 and A12-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the discussion should be revisited during the audit if there are indicators that fraud risk (covering both RoMMs due to fraud and fraud risk factors) may have changed or indications of actual or suspected fraud. Additional discussions of this nature should be documented in the 'Further team discussions' tab of the Engagement Team Discussion on Risk and Fraud template.

30.31 As part of the stand-back assessment, the engagement team should hold a second discussion on risk and fraud. This should be documented in the 'Fraud discussion stand back' tab in the Engagement Team Discussion on Risk and Fraud template and address the following requirements:

- The engagement team should consider whether the primary driver of any of the identified RoMMs in the Risk Assessment in Apex is fraud. Any RoMMs whose primary driver is determined to be fraud should be assessed as a significant risk, as required by paragraph 28 of ISA (UK) 240 (Revised May 2021) (Updated May 2022). This should be reflected in the Risk Assessment in Apex (overriding the original risk placement) and, for group audits, in the Group Audit Plan.
- The engagement team should also consider the appropriateness of the planned responses to identified RoMMs in light of identified RoMMs which are due to fraud. This should include consideration of how an element of unpredictability will be incorporated into the nature, timing and extent of the audit procedures to be performed, as well as whether certain types of audit procedure are more effective than others.

Fraud risk assessment – presumed significant RoMMs

30.32 As set out in Chapter 17: Risk assessment and response planning, every engagement will have a significant risk of fraud through management override of controls. Engagement teams should identify the nature of the risk of management override in the context of the entity, using the Risk Assessment in Apex.

30.33 There is a presumption in paragraph 27 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) that there are risks of fraud in revenue recognition. This presumption may be rebutted as described in Chapter 17: Risk assessment and response planning. If the Engagement Director concludes that the presumed risk is not applicable in the circumstances of the engagement (i.e. wishes to rebut it), the engagement team should document the reasons that revenue recognition is not a risk of material misstatement due to fraud. For example, it may be that income arises entirely from grant-in-aid or is highly immaterial.

30.34 The team should consider the presumed risk of fraud in revenue recognition as part of the engagement team discussion on fraud discussed above. The outcome of this discussion should be recorded within the Engagement Team Discussion on Fraud template, including the documenting the rationale for rebutting this risk where appropriate. Where this risk is not rebutted, the engagement team should ensure that the Risk Assessment in Apex appropriately reflects the outcome of the discussion as documented within the Engagement Team Discussion on Fraud template.

Additional procedures responsive to risks related to management override of controls

30.35 The Engagement Director and Engagement Manager should determine whether, in order to respond to the identified risks of management override of controls, the engagement team needs to perform other audit procedures in addition to those specifically required by the standard (that is, where there are specific additional risks of management override that are not covered as part of the procedures required for every audit engagement). The engagement team should follow the requirements of Chapter 17: Risk assessment and response planning in respect of these further procedures.

Evaluation of audit evidence

30.36 In concluding upon our audit procedures, the Engagement Director and Engagement Manager should evaluate whether the assessments of fraud risk (covering both RoMMs due to fraud and fraud risk factors) remain appropriate.

30.37 This evaluation may indicate that there are additional risks of material misstatement due to fraud, further fraud risk factors, or that there is a need to perform additional or different audit procedures. If such additional RoMMs, fraud risk factors or different procedures are identified, the engagement team should revisit the Engagement Team Discussion on Risk and Fraud template and document their response in the 'Further team discussions' tab. Appendix 3 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) provides examples of circumstances which may indicate the possibility of fraud. provides examples of circumstances which may indicate the possibility of fraud.

30.38 In accordance with paragraph 36 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), for any misstatements identified, the engagement team should obtain an understanding of how the misstatement arose and evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the engagement team should evaluate the implications of the misstatement in relation to other aspects of the audit, particularly the reliability of management representations, recognising that an instance of fraud is unlikely to be an isolated occurrence.

30.39 In accordance with paragraph 37 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) If the engagement team identifies a misstatement, whether material or not, and has reason to believe that it is or may be the result of fraud and that management (in particular, senior management) is involved, they should re-evaluate the assessment of fraud risk (covering both

RoMMs due to fraud and fraud risk factors) and its resulting impact on the nature, timing and extent of audit procedures to respond to the assessed risks. The engagement team should also consider whether circumstances or conditions indicate possible collusion involving employees, management or third parties when reconsidering the reliability of evidence previously obtained.

30.40 In the circumstances envisaged by paragraph 38 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) (the auditor confirms that, or is unable to conclude whether, the financial statements are materially misstated as a result of fraud), the engagement team's evaluation of the implications for the audit should cover in particular the implications for the regularity opinion.

Impact of identified fraud on the financial statements

30.41 If a significant fraud is identified, the engagement team need to evaluate the possible effect, both in quantitative and qualitative terms, on the financial statements, taking into account whether:

- the crime itself has a material effect on the financial statements;
- the consequences of the crime have a material effect on the financial statements; or
- the outcome of any subsequent investigation by the police or other investigatory body may have a material effect on the financial statements.

Regularity considerations

30.42 All fraud is by definition without proper authority and therefore irregular and where material fraud (either by value or context) is discovered the C&AG will qualify his opinion on regularity. If the details of the fraud or suspected fraud are properly disclosed in the financial statements an unqualified opinion on the 'true and fair' presentation in the financial statements can be given. What constitutes proper disclosure will depend upon the circumstances of each case but the engagement team should have regard to the requirements of Managing Public Money and the Government Financial Reporting Manual (FReM). If fraud is identified which is considered to be immaterial the Engagement Director should consider whether it is appropriate to report to Parliament on the fraud.

30.43 Circumstances may arise where engagement teams have insufficient evidence to give an opinion on whether or not material fraud has occurred. This may be the case where the audited entity's procedures are not sufficiently robust to support a reasonable assessment of the level of fraud and where alternative audit procedures are not available; for example, missing documents supporting the application for benefit payments or where the only evidence available is from previous years and there is no evidence that the position has changed. In such cases the regularity opinion will be qualified and an explanation of the factors leading up to the limitation in scope will be included in the basis of opinion. Such circumstances are expected to be rare and restricted to external fraud and engagement teams should encourage audited entities to undertake an exercise to attempt to quantify the levels of fraud, wherever possible.

30.44 Where it has been concluded that there is a limitation on the scope of the C&AG's regularity opinion, the engagement team should consider the implications for the presentation of true and fair opinion. Whether a similar limitation applies will depend on the nature and extent of our concerns and the disclosure requirements relevant to the particular financial statements.

30.45 ***Consultation required*** All qualifications and potential qualifications must be referred to FAPQ for advice. All qualified accounts require a minute from the Director, Audit Quality or a named deputy to be included on the Certification Journal.

Ability to continue the engagement

30.46 ***Consultation required*** If the circumstances envisaged in paragraph 39 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) apply (as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit), the Engagement Director should consult FAPQ. This consultation should include consideration of:

- what the NAO's reporting requirements are; and
- whether the NAO is able to withdraw from the engagement.

30.47 ***Consultation required*** The NAO usually cannot withdraw from an engagement as statutory auditor. Where appropriate, the engagement team should consider, as part of their consultation with FAPQ per the previous paragraph, whether the NAO would do so if it were able to. Paragraphs 1-5 and 1-6 of Practice Note 10 (Revised 2022) provide guidance on interpreting the requirement to withdraw from an engagement where the appointment is made in statute. Relevant responses include:

- reflecting the circumstances in the engagement team's risk assessment and
- reporting publicly (for example, using the C&AG's powers to report to Parliament) such matters that may otherwise have caused withdrawal or resignation from the engagement.

Reporting to a third party

30.48 If the engagement team identifies or suspects a fraud, the Engagement Director should determine whether to report the occurrence or suspicion to a party outside the entity.

30.49 This may be one or more of: a money laundering report; a report to Parliament; and/or a report to another body. Any report to Parliament should be drafted in such a way as to not run a risk of prejudicing any on-going investigation which might result in a court hearing or appeal hearing.

30.50 Although our professional duty to maintain the confidentiality of audited entity information may preclude such reporting, our legal responsibilities or duty to Parliament and other parties external to the audited entity, such as regulators, may override the duty of confidentiality in some circumstances.

30.51 ***Consultation required*** Any reports to an appropriate authority outside the audited entity under paragraph 44(a) of ISA (UK) 240 (Revised May 2021) (Updated May 2022) must be approved by the Director, Financial Audit, Practice and Quality. Where the responsibilities for reporting to appropriate authorities outside of the entity are unclear, the engagement team should consult with FAPQ and may obtain external legal advice.

The effect of IT controls upon the risk of fraud

30.52 The existence of a satisfactory control environment, including appropriate IT controls, can reduce the risks of material misstatement through fraud or error. However, although it may help reduce the risk of fraud, a satisfactory control environment is not an absolute deterrent to fraud.

30.53 Conversely, deficiencies in the control environment may undermine the effectiveness of controls, in particular in relation to fraud. For example, management's failure to commit sufficient resources to address IT security risks may adversely affect internal control by allowing improper changes to be made to computer programs or to data, or unauthorised transactions to be processed.

30.54 Generally, IT benefits an entity's internal control by enabling an entity to:

- consistently apply predefined business rules and perform complex calculations in processing large volumes of transactions or data;
- enhance the timeliness, availability, and accuracy of information;
- facilitate the additional analysis of information;
- enhance the ability to monitor the performance of the entity's activities and its policies and procedures;
- reduce the risk that controls will be circumvented; and
- enhance the ability to achieve effective segregation of duties by implementing security controls in applications, databases, and operating systems.

30.55 IT can, however, give rise to risks of material misstatement due to fraud or error, including, for example:

- Systems or programs that are inaccurately processing data, processing inaccurate data, or both.
- Unauthorised access to data that may result in destruction of data or improper changes to data, including the recording of unauthorised or non-existent transactions, or inaccurate recording of transactions. Particular risks may arise where multiple users access a common database.
- IT personnel abusing administrative access privileges to amend system logic, standing data or change transactional data.

The use of digital audit or data analytics in the detection of fraud

30.56 Data analytics, or digital audit techniques can offer an effective and efficient response to significant risks of fraud.

30.57 In responding to the significant risk of fraud through management override of controls, which is present on all audits, engagement teams may:

- use tools (such as IDEA or Microsoft Excel) to identify journals for testing with characteristics that suggest that they present a greater fraud risk, as discussed above;
- use the AIMS Journals App for the same purpose; and/or
- use tools to identify unusual transactions.

30.58 Engagement teams may use data analytics in responding to significant risks of fraud by:

- identifying duplicate payments;
- checking numeric/date sequences for gaps;
- comparing addresses or other information to identify employees that are also suppliers;
- comparing addresses or other information to identify possible ghost employees;
- identifying suppliers with only PO Boxes as addresses (PTP);
- sorting payments by value to identify transactions that fall just under authorisation limits;
- identifying unusual items, such as:
    - employees working unusually high hours or at unusual rates;
    - unusually high or frequent expense claims;
    - unusual patterns in the level of usage of suppliers;
    - large round-sum items;
- checking data logs for modifications to master files; and/or
- checking for slow-moving inventory.

Quality and reviewing guidance

30.59 Audited entities should have strong controls in place to prevent fraud by benefit or grant recipients. It is often effective and efficient to work with the audited entity to obtain assurance over the existence or level of such external fraud.

30.60 This will usually not be appropriate in the case of "internal fraud", except where management have already identified a risk or incidents.

30.61 The main focus of ISA (UK) 240 (Revised May 2021) (Updated May 2022) is on fraudulent financial reporting. Although the standard sets out procedures to be performed on each audit to respond to the significant risk of fraud through management override of controls, these will only be effective where the engagement team plans tests that reflect the particular risks on an individual engagement and performs other relevant tests if required.

30.62 The incentives and pressures on public sector managers and employees differ from those in the private sector, so understanding the reasons why frauds might be committed helps the engagement team to understand what the risks to the entity are.

30.63 The opportunities to commit frauds will differ between entities. However, identifying the possible ways that misstatement or misappropriation might occur in the context of the particular audited entity will enable the engagement team to tailor tests appropriately.

30.64 Employees who commit a fraud are often able to rationalise their actions as acceptable. For example, a department head might justify understating a provision to allow more spending on delivery of services.

Written representations

30.65 The engagement team should obtain written representations from the Accounting Officer (or, where there is no Accounting Officer, other appropriate member of management/those charged with governance where there is no Accounting Officer) to cover the requirements of paragraph 40 of ISA (UK) 240 (Revised May 2021) (Updated May 2022).

Communications to management and with those charged with governance

30.66 If a fraud is identified or information obtained that indicates that a fraud may exist, the engagement team should first comply with their money laundering responsibilities.

30.67 Having done so, and considered the risk of tipping off, in accordance with paragraph 41 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team should communicate these matters on a timely basis to the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities, unless prohibited from doing so by law or regulations., the engagement team should communicate these matters on a timely basis to the appropriate level of management in order to inform those with primary responsibility for the prevention and detection of fraud of matters relevant to their responsibilities, unless prohibited from doing so by law or regulations.

30.68 In accordance with paragraph 42 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), unless all of those charged with governance are involved in managing the entity, if the engagement team has identified or suspects fraud involving:

- management;
- employees who have significant roles in internal control; or

- others where the fraud results in a material misstatement in the financial statements,

they should communicate these matters with those charged with governance on a timely basis. If the auditor suspects fraud involving management, the auditor shall communicate these suspicions with those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit. Such communications with those charged with governance are required unless the communication is prohibited by law or regulation.

30.69 Where the audited entity is a Public Interest Entity, the engagement team should comply with the requirements of paragraph 42-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022). Further guidance may be found in Chapter 45: Public Interest Entities.

30.70 In accordance with paragraph 43 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team should communicate with those charged with governance any other matters related to fraud that are, in our judgement, relevant to their responsibilities, unless prohibited from doing so by laws or regulation. In doing so, the engagement team should consider the matters, if any, to communicate regarding management's process for identifying and responding to the risks of fraud in the entity and the auditor's assessment of the risks of material misstatement due to fraud. consider the matters, if any, to communicate regarding management's process for identifying and responding to the risks of fraud in the entity and the auditor's assessment of the risks of material misstatement due to fraud.

Documentation requirements

30.71 The engagement team should include in the audit file:

- the significant decisions reached during the discussion among the engagement team regarding the susceptibility of the entity's financial statements to material misstatement due to fraud;
- the identified and assessed Financial Statements-level RoMMs and Assertion-level RoMMs due to fraud;
- detail of the overall responses to RoMMs which are driven by or primarily due to fraud;
- detail of the nature, timing and extent of audit procedures in response to significant risks of fraud and the linkage of those procedures to the assessed risk; and
- the results of the audit procedures, including those designed to address the risk of fraud through management override of controls.

30.72 The documentation requirements above will normally be captured within the Engagement Team Discussion on Risk and Fraud template, the Risk Assessment in Apex and our documentation of the associated audit procedures within the Apex audit file.

30.73 The engagement team should include in the Apex audit file documentation of communications about fraud made to management, those charged with governance, regulators and others. For oral communications, minute these appropriately in the file.

30.74 As noted in Chapter 17: Risk assessment and response planning, if the Engagement Director has concluded that the presumed significant risk of fraud in revenue recognition is not applicable in the circumstances of the engagement, the engagement team should include in the audit documentation the reasons for that conclusion.

30.75 Fraud risks (which are significant risks) and identified or suspected fraud will be a significant documentation matter. Documentation relating to these matters should comply with paragraphs 8(c) and A8 to A11 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation*.

30.76 Documentation of the professional judgements made, where significant, serves to explain our conclusions and to reinforce the quality of the judgement in the file.

Money laundering

30.77 Guidance on anti-money laundering requirements is available on Sharepoint and linked in the bullet points below. This includes:

- the NAO's anti-money laundering policy; and
- anti-money laundering internal process guidance.

30.78 Full compliance with the policy and guidance linked above is required for all those involved in carrying out NAO financial audit engagements.

30.79 Anyone involved in a financial audit engagement can obtain advice in relation to a money laundering matter by contacting the Anti-Money Laundering Team via the MLRO inbox (MLRO@nao.org.uk) or by speaking directly to a member of the team (a current list of AMLT team members can be found on Sharepoint here).

Money laundering - due diligence procedures during audited entity acceptance

30.80 The C&AG's acceptance of new public sector bodies as audited entities is exempt from the requirements of the Money Laundering Regulations.

30.81 The NAO has made a policy decision to disapply the C&AG's exemptions from the Money Laundering, Terrorist Financing and Transfer of Funds Regulations 2017 for any audits undertaken by agreement (i.e. "non-statutory" audits). This includes profit-making companies audited under the Companies Act 2006. These regulations require the NAO to undertake due diligence procedures for all new audited entities before accepting appointment, and to monitor the relationship on an on-going basis. These processes are similar to those required as part of our wider audited entity acceptance procedures detailed in Chapter 9: Engagement acceptance (statutory and non-statutory).

30.82 Audited entity due diligence procedures must be carried out on a risk-sensitive basis.

30.83 Standard due diligence procedures should be completed for all new audited entities. Before entering an agreement, the Engagement Director must:

- identify and verify the audited entity's identity using documents or information from reliable or independent sources;
- identify the beneficial owner of the audited entity, where required, including understanding the ownership and control structure of the audited entity and verifying, according to risk, the identity of the beneficial owner(s); and
- obtain information on the purpose and intended nature of the business relationship.

30.84 ***Consultation required*** Simplified due diligence procedures can be adopted in certain circumstances. However, these are unlikely to apply to any audited entities gained under the Companies Act 2006. Further details are provided in Regulation 37 of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017. If an Engagement Director intends to apply simplified due diligence procedures, they should consult FAPQ as part of the audited entity acceptance and approval process.

30.85 Enhanced due diligence procedures should be adopted when circumstances imply that there is a higher risk of money laundering or terrorist financing. Indications of heightened risk might include

audited entity business in a high-risk sector or high-risk jurisdiction. Careful consideration, in the context of general business risk management, should be given to whether the engagement should be accepted if an entity falls into this category. Engagement Directors may consult the MLRO and FAPQ in such circumstances.

30.86 On-going monitoring of the business relationship with audited entities should be undertaken, revisiting the due diligence procedures at least annually and whenever audited entity circumstances change, including changes in ownership or control, to the level, type or conduct of business, or specific causes for concern or suspicion arise.

30.87 The initial engagement team should assemble records of the audited entity's identity and the supporting evidence of verification of identity. Such records should be retained for five years after the end of the client relationship. These may be stored in an appropriate folder on Sharepoint.

30.88 The following enquiries are suggested as part of audited entity due diligence processes:

- What are the entity's main trading and registered office addresses?
- What are its business activities or purposes and sector?
- Who controls and manages the entity (i.e. has executive power over the entity – this may be directors, shadow directors or others depending on the circumstances)
- Name and check that the person(s) purporting to represent the entity is/are who they say they are.
- Who owns the entity – ultimate beneficiary owners and steps in between?
- What is its business model/intended business model?
- What are the key sources of income and capital?
- The history and current scale of the entity's earnings and net assets
- The entity's geographical connections, such that unusual transfers of assets and economic benefits can be identified.

30.89 Potential sources of evidence for the above enquiries include a full company search from a national companies registry (such as Companies House) or certified copies of original documents evidencing details of incorporation or registration, registered office and list of directors and shareholders/members.

Money laundering – when does a MLRO report need to be submitted?

30.90 All members of NAO staff have a personal legal obligation to report any case that they come across during the course of their normal work, where objective evidence is gained leading to reasonable grounds for knowledge or suspicion that someone has obtained a benefit from the proceeds of any crime. Failing to incur an expense through a criminal act, such as a deliberate breach of health and safety law to save money, would be reportable under the Proceeds of Crime Act 2002. Further guidance may be found in the linked anti-money laundering internal process guidance on Sharepoint.

30.91 Knowledge means that engagement team members know an incident has taken place, this incident is a criminal offence and that someone has obtained a benefit from it. Suspicion is not defined in law but will generally involve uncertainty as to one of these conditions.

30.92 It is important to note that reporting is case based. If at the planning stage staff consider the risk of fraud to be high or even know that a number of frauds have occurred, but don't have any details of any specific cases there is no need to make a report. If testing uncovers specific cases where someone has obtained a benefit from the proceeds of crime then make a report for each case, where there is sufficient information to report.

30.93 There is no de minims limit for reporting. The view of Parliament is that intelligence about comparatively small amounts could prompt investigations leading to the termination of significant criminal operations and the recovery of criminal property.

30.94 Staff need to record what they have done with the information or suspicion for their own benefit, either reporting to the MLRO or not reporting, with appropriate justification.

30.95 The most common type of incident that engagement teams are likely to come across is where the audited entity has detected a fraud and informs either the engagement team or the audit committee. In these cases, the fact that the audited entity may have reported the incident to the police does not absolve the engagement team of the responsibility to report.

30.96 There is no requirement to make a report where the engagement team identifies a case but does not have any information that would aid an investigating authority in identifying either the suspect or the criminal property. An example of this is where assets are stolen by unknown persons.

Money laundering – submitting a report

30.97 Money laundering reports should be submitted by email to the MLRO. Initial consultations with the MLRO team can be conducted by phone, but a formal report will not be recorded until an email is received. The report should be made using the template on Sharepoint stating the audited entity, a summary of the incident, reference to supporting evidence where appropriate and the grounds for knowledge and suspicion. Providing a fraud report or audit committee minute with no assessment of why this gives grounds for knowledge or suspicion does not fulfil an individual's reporting responsibility.

30.98 Where multiple members of the engagement team have access to the same evidence, the team should submit only one report per incident, listing all team members with knowledge of the matter in the report.

Money laundering – conducting further work

30.99 It is possible that the evidence available will leave engagement teams unsure as to whether they have sufficient evidence to make a report. In these cases, team members should use their judgement and act appropriately. It is important that where an individual’s professional scepticism has caused them to consider whether or not a money laundering offence has been committed, that this is documented on the audit file (or in a confidential folder). In appropriate circumstances, and while taking into account the risk of tipping off, the engagement team should ask their audited entity for an explanation of facts or matters that could have alternative answers and explanations). Nobody can be expected to make the right judgement call in every instance, but in case their judgement is called into question subsequently they should have available to them an aide memoire of their thought process and evaluation of circumstances.

30.100 There is no need to do further work to firm up whether there is a reportable offence and in fact, further work should not be performed unless it is required for audit purposes.

Money laundering – discharging ongoing audit responsibilities and obtaining appropriate consent

30.101 ***Consultation required*** Following the submission of a report to the MLRO, the engagement team should be aware of the risk that further actions which they take in discharging their

responsibilities under ISAs or ISAs (UK) could generate a risk of committing a principal money laundering offence, particularly tipping off. Where engagement teams consider that the actions they plan to take, or may be asked to take, will result in themselves committing a principal money laundering offence, they must consult with the MLRO. The MLRO may decide to consult further with the National Crime Agency (NCA) to seek a defence:

- to a principal money laundering offence under Section 335 and Section 336 of the Proceeds of Crime Act 2002; and/or; and/or
- to a terrorist financing offence under Section 21ZA of the Terrorism Act 2000.

30.102 Engagement team members could also commit a principal offence through acts of omission.

30.103 ***Consultation required*** In the circumstances where money laundering has been reported to the NCA and the engagement team considers that making the audit report may generate a risk of committing a principal money laundering offence, the engagement team must obtain consent from the MLRO, prior to making the audit report.

30.104 ***Consultation required*** The engagement team also needs to consider whether continuing to act for the entity could itself constitute money laundering; for example, if it amounted to aiding or abetting the commission of one of the principal money laundering offences, or if it amounted to one of the principal money laundering offences itself, in particular the offence of becoming involved in an arrangement under the Anti-Money Laundering Legislation. In those circumstances, the engagement team may want to consider whether to resign, but should firstly contact the MLRO, both to report the suspicions and to seek guidance in respect of 'tipping off'. If the engagement team wishes to continue the engagement the auditor may need to seek NCA consent for such an action to be taken.

30.105 ***Consultation required*** Appropriate consent from the NCA will protect the auditor from committing a principal money laundering offence but will not relieve the auditor from any civil liability or other professional, legal or ethical obligations. As an alternative to seeking appropriate consent, the Engagement Director may consider resignation from the audit but, in such circumstances, is still required to disclose suspicions to the MLRO.

30.106 ***Consultation required*** The Engagement Director must consult with FAPQ in circumstances where it has been determined that it is necessary to withdraw from the engagement, especially in circumstances where it is not possible to do so.

Money laundering – considerations for the auditor's report

30.107 ***Consultation required*** In circumstances where it is known that money laundering has occurred and that management or those charged with governance were involved, the Engagement Director should consider whether it is necessary to modify the audit report or include an emphasis of matter paragraph. In such circumstances, all modifications and potential modifications of the audit report must be referred to FAPQ for advice.

30.108 ***Consultation required*** The engagement team also needs to consider whether including information in the auditor's report about any identified or suspected money laundering activities, for example, through modifying the auditor's opinion or communicating key audit matters, could alert a money launderer. The engagement team must consult with FAPQ and the MLRO before including such information in an audit report.

30.109 ***Consultation required*** Where issuing an audit report in circumstances where money laundering has occurred, timing may be the crucial factor. Any delay in issuing the auditor's report

pending the outcome of an investigation is likely to be impracticable and could in itself alert a money launderer. The engagement team should seek advice from the MLRO who acts as the main source of guidance and if necessary is the liaison point for communication with external legal counsel, the NCA and the relevant law enforcement agency.

Money laundering – responsibilities for providing access to working papers to successor auditors and regulatory authorities for quality monitoring purposes

30.110 ***Consultation required*** In circumstances where a money laundering offence has been committed and information relevant to that offence is required to be shared with third parties to fulfil our regulatory responsibilities (for example, successor auditors or as part of the external monitoring regime), the engagement team in consultation with the MLRO considers whether the disclosure of that information would constitute a 'tipping off' offence under the Anti-Money Laundering Legislation as it may prejudice an investigation.

30.111 If the engagement team and the MLRO considers a 'tipping off' offence might be committed, the MLRO speaks to the National Crime Agency to see if they are content that disclosure in those circumstances would not prejudice any investigation. The MLRO may, as a last resort, need to apply to the Court for directions as to what is disclosed to the successor auditor or relevant third party.

Money laundering – reporting to regulators

30.112 The identification and reporting of money laundering to the MLRO does not relieve the engagement team from other responsibilities which they may have for reporting to appropriate authorities and regulators under ISA (UK) 250A (Revised November 2019) (Updated May 2022) and ISA (UK) 250B (Revised November 2019). Chapter 31: Consideration of laws and regulations and reporting to regulators provides more guidance in respect of these responsibilities.

30.113 ***Consultation required*** A 'tipping off' offence is not committed when a report is made to the entity's supervisory authority and where a disclosure is not likely to prejudice an investigation. Where the engagement team is considering making such a report, they must consult with both the MLRO and FAPQ.

Tax evasion

30.114 Sections 45 and 46 of the Criminal Finances Act 2017 create criminal offences for failing to prevent the facilitation of tax evasion. These offences apply to Companies, Partnerships and Limited Liability Partnerships (LLPs) where: create criminal offences for failing to prevent the facilitation of tax evasion. These offences apply to Companies, Partnerships and Limited Liability Partnerships (LLPs) where:

- Criminal tax evasion takes place under UK or foreign law;
- It is facilitated by the business' employee, agent or those performing services for the business; and
- The business, by virtue of failing to put in place reasonable prevention methods, has failed to prevent that person from enabling the crime

30.115 Any instances of actual or suspected tax evasion identified during the course of the audit must be reported to the MLRO. In these circumstances consideration should also be given as to whether a report should be made to HMRC, or the relevant tax authority, as an appropriate authority under ISA (UK) 250A (Revised November 2019) (Updated May 2022). Chapter 31: Consideration of laws and regulations and reporting to regulators provides further guidance on reporting to the

appropriate authority in the public interest. provides further guidance on reporting to the appropriate authority in the public interest.

Chapter 31: Consideration of laws and regulations and reporting to regulators

Relevant standards and guidance

31.1 ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements* deals with the auditor's responsibility to consider laws and regulations in an audit of financial statements. The objectives of the auditor under ISA (UK) 250A (Revised November 2019) (Updated May 2022) are:

- to obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements;
- to perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements; and
- to respond appropriately to identified or suspected non-compliance with laws and regulations identified during the audit.

31.2 Paragraphs 1-52 to 1-60 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 250A (Revised November 2019) (Updated May 2022) in the public sector.

31.3 Paragraphs 36 to 62 of Practice Note 11 (PN 11) (Revised 2017) *The audit of charities in the United Kingdom* provide guidance on applying ISA (UK) 250A (Revised November 2019) (Updated May 2022) to the audit of charities.

31.4 ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector* deals with the circumstances in which the auditor of an entity subject to statutory regulation (a "regulated entity") is required to report direct to a regulator information which comes to the auditor's attention in the course of the work undertaken in the auditor's capacity as auditor of the regulated entity. This may include work undertaken to express an opinion on the entity's financial statements, other financial information or on other matters specified by legislation or by a regulator. The objective of the auditor of a regulated entity under ISA (UK) 250B (Revised November 2019) is to bring information of which the auditor has become aware in the ordinary course of performing work undertaken to fulfil the auditor's audit responsibilities to the attention of the appropriate regulator as soon as practicable when:

- the auditor concludes that it is relevant to the regulator's functions having regard to such matters as may be specified in statute or any related regulations; and
- in the auditor's opinion there is reasonable cause to believe it is or may be of material significance to the regulator.

Background

31.5 Laws and regulations can have a material impact upon an entity's results and financial position, either by directly determining amounts presented (such as payroll taxes) or through the potential impact of non-compliance (such as environmental regulations).

31.6 Non-compliance with laws and regulations may result in fines, litigation or other consequences for the entity that may have a material effect on the financial statements. ISAs (UK)

therefore require the engagement team to consider and respond to the risks that laws and regulations may impact upon the financial statements.

31.7 The Accounting Officer is responsible for ensuring the entity's operations are conducted in accordance with the provisions of laws and regulations, under the oversight of those charged with governance. Typically, they would implement policies and procedures to prevent and detect non-compliance with laws and regulations, such as:

- those listed in paragraph A2 of ISA (UK) 250A (Revised November 2019) (Updated May 2022);
- implementation of an internal audit function (required for public sector bodies); and
- establishment of an audit and risk committee.

31.8 Where possible non- compliance with law or regulations has occurred, which may result in a material misstatement in the financial statements, the accounting officer should ensure that the matter is appropriately reflected and/or disclosed in the financial statements. The NAO is not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

31.9 Although there are overlaps between the work performed on general laws and regulations under ISAs and the work performed on regularity, the two are distinct. For example, a breach of health and safety legislation may not be irregular, whereas an ex-gratia redundancy payment may be irregular, but permitted under laws and regulations.

31.10 Although breaches of general law and regulations may put a statutory duty on the auditor to report, they are not irregular on their own. For example, if an audited entity breaches general legislation such as employment, environmental, health and safety or tax law, this is not irregular. Engagement teams should consider the impact on the true and fair opinion in line with ISA (UK) 250A (Revised November 2019) (Updated May 2022) (for example, there may be associated provisions missing from the accounts). (for example, there may be associated provisions missing from the accounts).

31.11 The objectives of the engagement team (as set out in paragraph 11 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) and paragraph 8 of ISA (UK) 250B (Revised November 2019)) are:

- to obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements;
- to perform specified audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements;
- to respond appropriately to non-compliance or suspected non-compliance with laws and regulations identified during the audit; and
- (for a regulated entity) to bring information of which the engagement team has become aware in the ordinary course of performing work undertaken to fulfil the engagement team's audit responsibilities to the attention of the appropriate regulator as soon as practicable when:
    - the engagement team concludes that it is relevant to the regulator's functions having regard to such matters as may be specified in statute or any related regulations; and
    - in the engagement team's opinion there is reasonable cause to believe it is or may be of material significance to the regulator.

31.12 When obtaining audit evidence to understand how the entity is complying with the legal and regulatory framework applicable to the entity, the engagement team may obtain that understanding

through a combination of inquiries and other risk assessment procedures (i.e., corroborating inquiries through observation or inspection of documents).

31.13 'Non-compliance' consists of acts of omission or commission by the entity, either intentional or unintentional, which are contrary to the prevailing laws or regulations. Such acts include transactions entered into by, or in the name of, the entity, or on its behalf, by those charged with governance, management or other individuals working for or under the direction of the entity. Non-compliance does not include personal misconduct unrelated to the business activities of the entity by those charged with governance, management or employees of the entity. However, the engagement team should be aware of the risk that personal misconduct may be indicative of non-compliance corporately or weaknesses in the system of control to ensure compliance which may need to be brought to the attention of the regulator for regulated entities.

31.14 The term 'material significance' (to the regulator of a regulated entity) will depend on the context of the specific legislation applicable to the regulated entity. A matter or group of matters is normally of material significance to a regulator's functions when, due either to its nature or its potential financial impact, it is likely of itself to require investigation by the regulator.

Inquiries of management and those charged with governance

31.15 As part of the process of gathering entity initial information set out in Chapter 15: Gathering entity initial information, the engagement team should inquire of management specifically as to the nature of the legal and regulatory framework and how the entity complies with that framework, including:

- laws and regulations that directly determine the reported amounts and disclosures in the financial statements (or changes thereto);
- laws or regulations other than those which directly determine the reported amounts and disclosures in the financial statements that may be expected to have a fundamental effect on the operations of the entity;
- the entity's policies and procedures regarding compliance with laws and regulations; and
- the policies or procedures adopted for identifying, evaluating and accounting for litigation claims.

31.16 The engagement team should also inquire of management and those charged with governance as to whether the entity is in compliance with laws and regulations that may be expected to have a fundamental effect on the operations of the entity. In addition, they should inspect correspondence, if any, with relevant licensing or regulatory authorities.

Consideration of compliance with laws and regulations

31.17 The engagement team should ensure that compliance with laws and regulations is scoped in as a Financial Statement Risk Area (FSRA) within the Risk Assessment in Apex. The default placement on the spectrum of inherent risk of the RoMM associated with compliance with laws and regulations should not be manually overridden into the Target position – this ensures compliance with the requirements to consider compliance with laws and regulations in ISA (UK) 250A (Revised November 2019) (Updated May 2022).

31.18 ISA (UK) 250A (Revised November 2019) (Updated May 2022) distinguishes between:

- those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements; and
- other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the

operating aspects of the business, to an entity's ability to continue its business, or to avoid material penalties; non-compliance with such laws and regulations may therefore have a material effect on the financial statements.

31.19 As required by paragraph 14 of ISA (UK) 250A (Revised November 2019) (Updated May 2022), for laws and regulations that have a direct effect on the determination of material amounts and disclosures in the financial statements (such as tax and pension laws and regulations), the engagement team should obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations.

31.20 By contrast, for laws and regulations that do not directly affect the financial statements, but compliance with which may be fundamental to the operating aspects of the entity, to an entity's ability to operate, or to avoid material penalties (for example, compliance with environmental regulations), the engagement team's responsibility is limited to undertaking specified audit procedures to help identify non-compliance with those laws and regulations that may have a material effect on the financial statements.

31.21 Although the extent of the required procedures to assess non-compliance with laws and regulations that do not directly affect the financial statements is limited, the engagement team should remain alert throughout the audit to indications of possible non-compliance, and teams should maintain professional scepticism when considering the entity's compliance.

31.22 In the absence of identified or suspected non-compliance, the engagement team are required to perform the following audit procedures regarding the entity's compliance with laws and regulations but are not required to perform additional procedures to evidence compliance with laws and regulations that do not directly affect the financial statements.

31.23 The planned procedures may relate to individual Financial Reporting Activities or be part of the procedures performed in auditing the preparation of the financial statements. Examples of laws and regulations directly affecting the financial statements include those governing:

- the accrual or recognition of expenses for payroll taxes or pension costs;
- the form and content of financial statements;
- sector specific financial reporting requirements such as those in the FReM or Charities SORP.

31.24 These laws and regulations may be directly relevant to specific risks of material misstatement (such as completeness of accruals for national insurance), or to the financial statements as a whole (such as the requirements for the content of the financial statements).

31.25 Possible non-compliance may be detected through a variety of audit procedures performed for other reasons, including:

- reading minutes;
- inquiring of the entity's management and in-house legal counsel or external legal counsel concerning litigation, claims and assessments; or
- performing tests of detail.

31.26 The engagement team may seek legal advice from the entity's legal counsel, or, if this is inappropriate, from the NAO's own legal counsel. If it is necessary to consult the NAO's legal counsel, this should be arranged through the Legal and Policy team.

31.27 In some situations, the entity may have obtained legal advice to the effect that certain actions or circumstances do not give rise to criminal conduct and therefore cannot give rise to criminal property.

31.28 Whether an act constitutes non-compliance with laws and regulations may involve consideration of matters beyond the auditor's professional competence to determine. Provided that the auditor considers that the advice has been obtained from a suitably qualified and independent solicitor and that the solicitor was made aware of all relevant circumstances known to the auditor, the auditor may rely on such advice, provided the auditor has complied with the requirements of ISA (UK) 500 (Updated May 2022) and ISA (UK) 620 (Revised November 2019) (Updated May 2022). Further guidance on obtaining assurance from the work of others may be found in Section 12: Use of experts.

31.29 The implications of particular instances of non-compliance identified will depend on the relationship of the perpetration and concealment, if any, of the act to specific control activities and the level of management or employees involved, especially implications arising from the involvement of the highest authority within the entity.

31.30 ***Consultation required*** In exceptional cases, the engagement team may consider withdrawal from the engagement, or, if not possible, reporting to those charged with governance and/or Parliament that the C&AG would withdraw from the engagement if he were able to do so. In such cases, the engagement team must consult with FAPQ and obtain legal advice as to the best course of action, noting that withdrawing from the engagement does not remove the auditor's responsibility for reporting the non-compliance with laws and regulations under ISA (UK) 250A (Revised November 2019) (Updated May 2022).

31.31 Non-compliance with laws and regulations can have a fundamental effect upon the financial statements. It is therefore important that:

- engagement teams consider compliance with laws and regulations at the planning stage of the audit and build appropriate procedures into our approach, through considering the laws and regulations Financial Statements Risk Area within the Risk Assessment in Apex;
- engagement team members testing compliance with laws and regulations (including in the form of reporting for the entity) are familiar with the relevant requirements;
- the engagement team remains alert throughout the engagement to possible indications of non-compliance with laws and regulations; and
- careful consideration is given to how laws and regulations interact with our work on regularity to take an effective and efficient approach to testing these areas.

31.32 Particular areas to consider during the course of the audit are:

- considering the possibility of non-compliance with legislation around redundancy where there are restructurings;
- thinking carefully about the impact of issues noted in review of the entity's minutes;
- considering if legal expenses are indicative of issues the engagement team are unaware of;
- remaining alert to matters which arise where there may be a need to make a report to a proper authority in the public interest; and
- (for regulated entities) considering whether any instances of actual or suspected non-compliance with laws and regulations are sufficiently significant to be of material significance to a regulator and therefore require reporting to the regulator.

Audit procedures when non-compliance is identified or suspected

31.33 Where non-compliance with laws and regulations is identified or suspected, the engagement team should consider whether there are obligations relating to money laundering (an act which conceals, disguises, converts, transfers, removes, uses, acquires or possesses property resulting from criminal conduct) which should be complied with before proceeding further (such as avoiding tipping off). Requirements under money laundering legislation are discussed in the NAO's policy and guidance on money laundering – links to these documents are included in Chapter 30: Fraud responsibilities.

31.34 If management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations, then the engagement team should evaluate:

- the potential financial consequences of non-compliance with laws and regulations on the financial statements including, for example, the imposition of fines, penalties, damages, threat of expropriation of assets, enforced discontinuation of operations, and litigation
- whether the potential financial consequences require disclosure; and
- whether the potential financial consequences are so serious as to call into question the fair presentation of the financial statements, or otherwise make the financial statements misleading

31.35 ***Consultation required*** If the engagement team is required to consider the need to obtain legal advice, as for instance in the circumstances set out in paragraph 20 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) (management or, as appropriate, those charged with governance do not provide sufficient information that supports that the entity is in compliance with laws and regulations and, in the auditor's judgment, the effect of the suspected non-compliance may be material to the financial statements either quantitatively or qualitatively, and where there is more than one occurrence both individually and in aggregate), they should consult FAPQ.

31.36 Instances of non-compliance or suspected non-compliance with laws and regulations may be significant documentation matters.

Potential implications of identified or suspected non-compliance for the auditor's report

31.37 When considering whether the financial statements reflect the possible consequences of any suspected or actual non-compliance, the engagement team should consider the requirements of applicable accounting standards. Non-compliance with laws or regulations may require disclosure in the financial statements because, although the immediate financial effect on the entity may not be material, there could be future material consequences such as fines or litigation.

31.38 ***Consultation required*** Law or regulation may preclude public disclosure by either management, those charged with governance or the auditor about a specific matter. When the engagement team intends to communicate identified or suspected non-compliance in the auditor's report, such law or regulation may have implications for the engagement team's ability to describe the matter in the auditor's report, or in some circumstances to issue the auditor's report. In such cases, the engagement team must consult with FAPQ and consider obtaining legal advice to determine the appropriate course of action.

31.39 ***Consultation required*** For all circumstances where the engagement team proposes to report on instances of identified or suspected non-compliance with laws and regulations in the auditor's report, approval of the modified report must be obtained from the Director, Audit Quality.

Communicating identified or suspected non-compliance with those charged with governance

31.40 In the circumstances envisaged by paragraph 25 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) (the auditor suspects that management or those charged with governance are involved in non-compliance and either no higher authority exists or the auditor believes that the communication may not be acted upon or is unsure as to the person to whom to report), it may be appropriate for the C&AG to report to Parliament, or to the audited entity's sponsor department (if applicable).

31.41 Written representations do not provide sufficient appropriate audit evidence about compliance with laws and regulations on their own and, accordingly, do not affect the nature and extent of other audit evidence that is to be obtained by our audit procedures.

31.42 The engagement team should communicate with those charged with governance matters involving non-compliance with laws and regulations that come to our attention during the course of the audit, other than when the matters are clearly inconsequential or where prohibited from doing so by law or regulation (subject to compliance with the "tipping off" provisions of money laundering legislation).

31.43 This would not be necessary if all those charged with governance were also involved in the management of the entity, and therefore are aware of matters involving identified or suspected non-compliance already communicated by the engagement team. However, this is unlikely to be the case in the public sector.

31.44 ***Consultation required*** Engagement teams should also not report any instances of non-compliance with laws and regulations which they are considering reporting to a regulatory or enforcement authority where they no longer have confidence in the integrity of those charged with governance or where they are prohibited from doing so by law or regulation. Instead, such matters may be required to be reported directly to the relevant authority following consultation with FAPQ. Examples of such situations include the circumstances described in paragraph A24 of ISA (UK) 250A (Revised November 2019) (Updated May 2022).

Reporting in the public interest

31.45 ***Consultation required*** Where the engagement team identifies matters which may be required to be reported to a relevant authority in the public interest (as per paragraphs A28(d) and A33-1 to A33-8 of ISA (UK) 250A (Revised November 2019) (Updated May 2022)), they must consult FAPQ on these matters prior to discussing them with those charged with governance.

31.46 ***Consultation required*** All reports made to the proper authorities in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022) must be approved by the Director, Audit Quality. The Director, Financial Audit, Practice and Quality may decide to consult with the Legal and Policy and obtain external legal advice prior to making any such report.

31.47 In making a judgement regarding whether or not to report any actual or suspected non-compliance with laws and regulations to a proper authority in the public interest, the engagement team should be mindful that decision as to whether to report, and if so to whom, may be called into question at a future date, for example on the basis of:

- what the engagement team knew at the time;
- what the engagement team ought to have known in the course of the audit;
- what the engagement team ought to have concluded; and
- what the engagement team ought to have done.

Reporting identified or suspected non-compliance to regulatory or enforcement authorities

31.48 The auditor of entities subject to statutory regulation (such as charities and pension schemes), has separate responsibilities to report certain information direct to the relevant regulator. Standards and guidance on these responsibilities is given in ISA (UK) 250B (Revised November 2019), as well as relevant FRC Practice Notes (such as Practice Note 11 (Revised 2017)). (Revised 2017)).

31.49 Where there is a suspected or actual instance of non-compliance with law or regulations which does not give rise to a statutory duty to report to an appropriate authority, there may still be an obligation to make a report to an appropriate authority where it is in the public interest to do so. Similarly, the relevant law, regulation or ethical requirement may provide the engagement team with a right to make a report to an appropriate authority even where there is no obligation to do so.

31.50 In the circumstances envisaged by paragraph 29 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) (the auditor has identified or suspects non-compliance with laws and regulations), in determining reporting responsibilities to an appropriate authority, the Engagement Director should consider whether Parliament is an appropriate authority to report to. should consider whether Parliament is an appropriate authority to report to.

31.51 The auditor's professional duty to maintain the confidentiality of audited entity information may preclude reporting identified or suspected non-compliance with laws and regulations to a party outside the entity. However, the auditor's legal responsibilities vary by jurisdiction and, in certain circumstances, the duty of confidentiality may be overridden by statute, the law or courts of law. The C&AG's unique role and function usually means that his responsibilities for reporting to Parliament will override any duty of confidentiality to the entity. Where concerns are identified surrounding audited entity confidentiality surrounding reporting matters to Parliament, these may be discussed with FAPQ and the Legal and Policy team as appropriate.

31.52 For some entities, such as Public Interest Entities and charities, the auditor has a statutory duty to report the occurrence, or suspected occurrence, of non-compliance with laws and regulations to supervisory authorities. In some jurisdictions, the auditor also has a duty to report misstatements to authorities in those cases where management and, where applicable, those charged with governance fail to take corrective action.

31.53 Where the engagement team is uncertain as to their reporting responsibilities, they may consult with FAPQ and the Legal and Policy team, who may also obtain external legal advice where appropriate.

31.54 It may be that the NAO is the most appropriate authority and it would be necessary to consider whether the matter should be subject to further investigative work (separate from our financial audit) and/or reported to Parliament.

31.55 The consideration of whether to report any identified or suspected instances of non-compliance with laws and regulations to the relevant regulatory or enforcement authorities should be clearly documented on the audit file. Such documentation should include:

- the facts of the matter,
- evidence to support the non-compliance
- any further investigatory work which the team have undertaken to support the decision to report or not report,
- any communications with management concerning the matter

- any communications with those charged with governance concerning the matter
- evidence that those charged with governance have reported the matter to the relevant authority
- evidence of consultation with PQ and others as appropriate
- the report submitted to the relevant authority
- any relevant other correspondence with the relevant authority together with evidence that the report has been submitted to the relevant authority where relevant.

31.56 The engagement team should ensure any additional documentation requirements regarding identified or suspected non-compliance with laws and regulations set out in law, regulation or relevant ethical requirements (as per paragraph A36 of ISA (UK) 250A (Revised November 2019) (Updated May 2022)) are met within their Apex audit file.

31.57 ***Consultation required*** Content is available within Apex to document these considerations. This content will be released to the engagement team upon request to FAPQ.

31.58 The engagement team should consider the implications for the audit and the financial statements more general of matters which have led to them making a report to an appropriate authority.

Reporting to a regulator for a regulated entity – wider applicability of ISA (UK) 250B

31.59 ISA (UK) 250B (Revised November 2019) deals with the case where the auditor of a regulated entity has either: deals with the case where the auditor of a regulated entity has either:

- a responsibility to provide a report on matters specified in legislation or by a regulator; or
- a statutory duty to report certain information, relevant to the regulators' functions, that come to the auditor's attention in the course of the audit work.

31.60 The procedures and guidance in ISA (UK) 250B (Revised November 2019) should be adapted to circumstances in which the auditor of other types of entity (i.e. other than those in the financial services sector) becomes aware of a suspected instance of non-compliance with laws or regulations which the auditor is under a statutory duty to report. This may be particularly relevant to charities. Further guidance on reporting to the Charity Commission may be found in Chapter 43: Charities.

Reporting to a regulator for a regulated entity – understanding the regulatory environment

31.61 In the circumstances envisaged by paragraph A13 of ISA (UK) 250B (Revised November 2019) (the engagement team's review of the reporting entity's activities indicates that published guidance by the regulator may not be sufficiently precise to enable the team to identify circumstances in which it is necessary to initiate a report), the engagement team may discuss any such matters with FAPQ prior to contacting the relevant regulator. prior to contacting the relevant regulator.

Reporting to a regulator for a regulated entity – matters which may give rise to a need to report

31.62 ***Consultation required*** In addition to the types of matter listed in paragraph A24 of ISA (UK) 250B (Revised November 2019) that give rise to a statutory duty on auditors to make a report to a regulator, additional matters may be specified within the legislation or regulations which the particular entity applies. Engagement teams must consult with FAPQ if they consider that a matter may give rise to the need to report to the regulator.

31.63 When a matter does not give rise to a statutory duty to report, it may nevertheless be a relevant matter to report under the appropriate legal provisions. If the matter should be reported, the engagement team should advise those charged with governance to do so, except in the circumstances in which the engagement team does not have confidence in the integrity of those charged with governance or where prohibited from doing so by law or regulation. In such circumstances, a direct report to the regulator should be made.

31.64 If, within a reasonable period, the engagement team cannot confirm that those charged with governance have properly informed the regulator of the matter, they should report directly to the regulator as soon as practicable.

31.65 ***Consultation required*** All investigations undertaken in order to determine whether or not a matter is of sufficient material significance to the regulator should be documented on Apex. Content is available upon request from FAPQ to document this testing and includes as a minimum:

- details of the matter which may give rise to a duty to report to the regulator;
- details of any investigation under taken by the engagement team to ascertain the significance of that matter;
- the engagement team's judgement on whether that matter is of material significance to the regulator.
- documentation of the discussions with management and those charged with governance on the matter (where applicable) including actions taken by those charged with governance in response to those discussions;
- evidence that those charged with governance have reported the matter to the relevant authority;
- evidence of consultation with FAPQ and others as appropriate;
- the report submitted to the relevant authority; and
- any relevant other correspondence with the relevant authority together with evidence that the report has been submitted to the relevant authority where relevant.

Reporting to a regulator for a regulated entity – issuing the report

31.66 When issuing a report expressing an opinion on a regulated entity's financial statements or on other matters specified by legislation or a regulator, the engagement team should consider whether they are any:

- consequential reporting issues affecting the auditor's opinion which arise from any report previously made direct to the regulator in the course of the auditor's appointment
- matters encountered in the course of the audit indicating a need for a further direct report

31.67 When making or confirming in writing a report direct to a regulator, in addition to the items required to be included by paragraph 17 of ISA (UK) 250B (Revised November 2019), the report should also state::

- the engagement being performed when the matter came to the engagement team's attention;
- the applicable legislative requirements and interpretations of those requirements which have informed the engagement team's judgment;
- the extent to which the engagement team has investigated the circumstances giving rise to the matter reported;
- whether the matter has been reported to and discussed with those charged with governance; and
- what steps management have taken to rectify the issue.

31.68 Where the engagement team chooses not to send a copy of the auditor's written report to those charged with governance in the circumstances envisaged by paragraphs 14 and A32 of ISA (UK) 250B (Revised November 2019), as such circumstances are unusual, the engagement team

may consult with FAPQ regarding such a decision, who may wish to consult with the Legal and Policy team and external legal counsel., who may wish to consult with the Legal and Policy team and external legal counsel.

31.69 As noted in paragraph A33 of ISA (UK) 250B (Revised November 2019), in normal circumstances, the engagement team would wish to communicate with the regulator with the knowledge and agreement of those charged with governance of the regulated entity. However, in some circumstances immediate notification of the discovery of a matter giving reasonable grounds to believe that a reportable matter exists will be necessary – for example, a phone call to alert the regulator followed by a meeting to discuss the circumstances.

31.70 ***Consultation required*** Where engagement teams identify the need to make a report to the regulator of a regulated entity, they must consult with FAPQ and approval of the report to the regulator should be obtained from the Director, Audit Quality.

31.71 The engagement team should consider the implications for the audit and the financial statements more general of matters which have led to them making a report to a regulator.

31.72 ***Consultation required*** In circumstances where an oral report has been made to the regulator, the engagement team should follow it up with a formal written report which has been approved by the Director, Audit Quality.

31.73 As noted in paragraph A34 of ISA (UK) 250B (Revised November 2019), speed of reporting is essential where the circumstances cause the engagement team to no longer have confidence in the integrity of those charged with governance. In such circumstances, there may be a serious and immediate threat to the interests of depositors or other persons for whose protection the regulator is required to act; for example where the engagement team believes that a fraud or other irregularity may have been committed by, or with the knowledge of, those charged with governance, or have evidence of the intention of those charged with governance to commit or condone a suspected fraud or other irregularity. peed of reporting is essential where the circumstances cause the engagement team to no longer have confidence in the integrity of those charged with governance. In such circumstances, there may be a serious and immediate threat to the interests of depositors or other persons for whose protection the regulator is required to act; for example where the engagement team believes that a fraud or other irregularity may have been committed by, or with the knowledge of, those charged with governance, or have evidence of the intention of those charged with governance to commit or condone a suspected fraud or other irregularity.

31.74 There may be occasions where there is no readily identifiable regulator to which the engagement team can make a report, or the matter to be reported would not be of interest or relevance to the UK Listing Authority (UKLA). In that case, the engagement team considers whether to make a report to the NAO's competent authority (the Financial Reporting Council).

Reporting to a regulator for a regulated entity – communications with the regulator

31.75 Auditors of regulated entities are expected to establish regular channels of communication with regulators. These communication channels will be setup and managed through FAPQ. Where engagement teams consider that they have identified a new regulator where a regular channel of communication has yet to be established, they may contact FAPQ.

31.76 Any confidential information received from a regulator in accordance with paragraph A44 of ISA (UK) 250B (Revised November 2019) must be handled in accordance with the NAO's Information Management Policies and Procedures.

31.77 Where legislation permits, regulators have confirmed that they will consider taking the initiative in bringing a matter to the attention of the auditor of a regulated entity in circumstances where:

- they believe the matter is of such importance that the auditor's knowledge of it could significantly affect the form of the auditor's report on the entity's financial statements or other matters on which the auditor is required to report, or the way in which the auditor discharges the auditor's reporting responsibilities; or
- the disclosure is for the purpose of the regulator in discharging its own statutory functions.

Distributions

31.78 The Companies Act 2006 determines the circumstances under which companies are permitted to make distributions to their members and shareholders and also which profits may be available for distribution. Where a company makes an unlawful distribution, this is legally reclaimable by the company and should be disclosed as a Receivable within its financial statements. determines the circumstances under which companies are permitted to make distributions to their members and shareholders and also which profits may be available for distribution. Where a company makes an unlawful distribution, this is legally reclaimable by the company and should be disclosed as a Receivable within its financial statements.

31.79 ***Consultation required*** Where unlawful distributions are made by companies, the engagement team should consider whether this should be reported to the relevant authority in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022) (see the section above on 'Reporting in the public interest). In this context, the relevant authority may include HM Revenue & Customs (HMRC), where such distributions have led to underpayment of tax, or the entity's sponsor department, if applicable. Teams must consult FAPQ prior to making any such report which must be approved by the Director, Audit Quality.

31.80 In circumstances where a regularity opinion is provided on the company's financial statements, the engagement team should consider the implications for that opinion of any unlawful distributions made by the company.

Taxation

31.81 Crown bodies are liable to incur penalties resulting from VAT or Customs infringements just as any other taxpayer.

31.82 The engagement team's responsibilities for the audit of the financial statements do not extend to obtaining assurance that the entity has complied with every aspect of tax legislation. Instead, the engagement team should perform procedures to obtain sufficient appropriate evidence to give reasonable assurance that the amounts included in the financial statements in respect of taxation are not materially misstated. Further guidance on such procedures can be found in Chapter 42: Companies.

31.83 Engagement teams should not be drawn into advising audited entities on the calculation of their tax liabilities and associated penalties and interest. There are appropriate channels for departments and other public sector bodies to consult with HMRC. Engagement teams should still

consider such matters and the robustness of the relevant underlying systems and records as part of their risk assessment for the audited entity and carry out appropriate testing on any tax charges and balances keeping in mind the potential for penalties

31.84 ***Consultation required*** However, if the engagement team identifies instances of non-compliance with tax legislation, consideration should be given to reporting this to HMRC or other relevant authorities in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022) (see the section above on 'Reporting in the public interest) .Teams must consult FAPQ prior to making any such report, which must be approved by the Director, Audit Quality.

31.85 In circumstances, where a non-compliance with tax legislation is identified relating to an entity where a regularity opinion is provided, the engagement team should consider the implications for that opinion.

Chapter 32: Other information and other reporting responsibilities

Relevant standards and guidance

32.1 Paragraphs 43 and A58 to A60 of ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* set out how the auditor should address other reporting responsibilities in the auditor's report on the financial statements that are in addition to the auditor's responsibilities under the ISAs (UK).

32.2 ISA (UK) 720 (Revised November 2019) (Updated May 2022) sets out the auditor's responsibilities with respect to other information, whether financial or non-financial information (other than financial statements and the auditor's report thereon), included in an entity's annual report.

32.3 Paragraphs 1-221 to 1-228 of Practice Note 10 *Audit of financial statements and regularity of public sector bodies in the United Kingdom* (Revised 2022) provide guidance on applying ISA (UK) 720 (Revised November 2019) (Updated May 2022) in the public sector.

Positive and negative consistency opinions

32.4 The other information comprises information included in the Annual Report, but does not include:

- the parts of the Accountability Report or Remuneration Report (as appropriate) described in that report as having been audited:
    - for FReM accounts, this is the items listed in paragraph 6.2.1 of the 2021-22 FReM, including regularity, Parliamentary accountability and remuneration disclosures;
    - for Companies Act accounts, this is specific parts of the Directors' Remuneration Report listed in Part 3 of Schedule 8 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008, including directors' emoluments and compensation, share options and pensions disclosures);
- the financial statements; or
- the audit certificate or report.

32.5 The annual report and accounts for an entity reporting under the FReM will normally include the following:

- Annual Report, including:
    - Performance Report
    - Accountability Report (audited and unaudited parts), including
        - Remuneration and Staff Report
        - Statement of Accounting Officer's responsibilities;
        - Governance Statement;
- Audit certificate and/or report; and
- Primary financial statements and notes.

32.6 The engagement team should read the other financial and non-financial information and, in doing so, consider whether the Other Information is materially inconsistent with the financial statements or the engagement team's knowledge obtained in the audit or otherwise appears to be materially misstated – the negative consistency opinion. The negative consistency opinion is

included in the section of the C&AG's certificate on 'Other information', which is required by paragraphs 21 and 22 of ISA (UK) 720 (Revised November 2019) (Updated May 2022).

32.7 The engagement team should read:

- for FReM accounts, the Performance Report and Accountability Report; or
- for company accounts, the Strategic Report and Directors' Report; or
- for charity accounts, the Trustees' Report,

and determine whether the information given in those Reports is materially consistent with the financial statements – the positive consistency opinion. The positive consistency opinion is given in the 'Opinion on other matters' section of the C&AG's certificate, which is included as an "other reporting responsibility" under paragraph 43 of ISA (UK) 700 (Revised November 2019) (Updated May 2022).

32.8 The information and disclosures within the Accountability Report that are subject to audit are listed in paragraph 6.2.1 of the FReM (2021-22 version). These are required to be clearly identified as audited within the Accountability Report and the C&AG's certificate accordingly describes them as "the parts of the Accountability Report described in that report as having been audited".

32.9 The nature and scope of the reviews for the two consistency opinions are the same. No additional work is required to reach a positive consistency opinion.

32.10 In reviewing the Other Information prepared alongside the financial statements, the engagement team should seek to identify any material misstatements.

32.11 In accordance with paragraph 12(b) of ISA (UK) 720 (Revised November 2019) (Updated May 2022), in the context of the Other Information, misstatements are defined as instances where the Other Information has not been prepared in accordance with the legal and regulatory requirements applicable to that information. Misstatements on this Other Information may also occur where the information disclosed is either not consistent with the information disclosed in the financial statements or the engagement team's knowledge and understanding of the entity based upon the findings of the audit.

32.12 In accordance with paragraph 12(b) of ISA (UK) 720 (Revised November 2019) (Updated May 2022), where information which is required to be included within the Statutory Other Information by law or regulation is omitted from the Statutory Other Information, this is also considered to be a misstatement of the Statutory Other Information.

32.13 ***Consultation required*** Where an engagement team identifies a misstatement in the Other Information, they should assess whether it is material in a similar manner to which misstatements in the financial statements are identified. Where a material misstatement in the Other Information is identified and management does not propose to correct the misstatement, the engagement team must consult with FAPQ.

32.14 Where an engagement team identifies a material misstatement in the financial statements as a result of their review of Other Information or information which indicates that the auditor's understanding of the entity and its environment should be updated, this should be responded to in accordance with the relevant ISAs (UK). The engagement team should refer to the requirements of Chapter 19: Continuous risk assessment.

Statutory other information

32.15 In accordance with paragraph 14-1 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), for entities that are required to prepare Statutory Other Information, which in the NAO context are considered to be those bodies who are required to prepare their financial statements under the Companies Act 2006 and those bodies which are required to prepare a Performance Report and Accountability Report in accordance with the FReM, the engagement team should read the Statutory Other Information and perform any other procedures which may be necessary in their professional judgment to determine whether the statutory other information appears to be materially misstated in the context of the engagement team's understanding of the legal and regulatory requirements applicable to the statutory other information.

32.16 In the context of the majority of the NAO's audit portfolio (i.e. those entities that are required to prepare their financial statements under the FReM), the Statutory Other Information is interpreted to include the Governance Statement, the Performance Report and the Accountability Report.

32.17 In the context of entities that are required to prepare their financial statements under the Companies Act 2006, paragraph A10-1 of ISA (UK) 720 (Revised November 2019) (Updated May 2022) defines the Statutory Other Information to mean the separate Corporate Governance Statement, the Strategic Report and the Director's Report.

32.18 As required by paragraph 14-2 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), the engagement team should also perform such procedures that may be necessary in their professional judgement to identify:

- any material inconsistencies between the other information and the financial statements;
- any material inconsistencies between the other information and the auditor's knowledge obtained in the audit, in the context of audit evidence obtained and conclusions reached in the audit; and
- whether the statutory other information appears to be materially misstated in the context of the auditor's understanding of the legal and regulatory requirements applicable to the statutory other information.

32.19 For audited entities that either are required to apply or voluntarily apply the UK Corporate Governance Code, the engagement team's responsibilities are explained in the section below entitled 'Responsibilities in respect of the UK Corporate Governance Code'.

32.20 There is no requirement to report on other information included in the financial statements for the majority of public sector bodies, with the exception of certain items in the remuneration report. There are additional requirements relating to the audit of statutory other information for companies. These are set out in Chapter 42: Companies.

32.21 The Engagement Manager and Engagement Director should be involved in reviewing the Other Information included in the annual report.

32.22 In order to comply with paragraph 25 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), the Apex audit file must include:

- the completed disclosure checklist covering the Other Information;
- the results and conclusion of those procedures performed to assess whether the information in the annual report is materially consistent with the financial statements, including details of any material inconsistencies identified and how they were resolved; and
- the final version of the Other Information upon which the engagement team have performed this work.

32.23 In accordance with paragraph A10-3 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), where any of the information required to be included within the Statutory Other Information is included in cross-referenced documents rather than within the Statutory Other Information itself, the relevant sections of the cross-referenced documents will also be included in the C&AG's opinion on the Statutory Other Information. This information must therefore be reviewed by the engagement team in the same manner as the Statutory Other Information included within the main Annual Report document.

32.24 Where the engagement team identifies a material misstatement in the Statutory Other Information which they are unable to resolve through discussion with management or those charged with governance, they should recommend that those charged with governance seek legal advice to resolve the matter and consider any such advice obtained.

Guidance on other information included in the Annual Report

32.25 The engagement team should use the relevant NAO disclosure guides to confirm the Other Information is in line with the requirements of the FReM (or other applicable financial reporting framework).

32.26 ***Consultation required*** If inconsistencies between other information in the annual report and the financial statements, or material misstatements of fact, are identified, the engagement team should discuss these with management and those charged with governance to resolve the issue. If revision of the other information is necessary and management refuses, the engagement team should consult FAPQ and, following this consultation, should communicate this matter to those charged with governance, unless all of those charged with governance are involved in managing the entity.

Remuneration and Staff Report

32.27 For entities reporting under the FReM which are required to prepare a Remuneration and Staff Report, the engagement team should consider whether all senior managers, Board members, trustees and ministers (as appropriate) have been identified in the Remuneration and Staff Report. Possible procedures over completeness include:

- establishing all ministers have been included from a Parliamentary search or the entity's website;
- review of Board, Senior Management, Oversight Board or trustee minutes to identify missing individuals; and
- discussions with management and knowledge of the business.

32.28 The engagement team should ensure that the Remuneration and Staff Report has been prepared in line with the FReM and Section 13 of the Employer Pension Guide (updated with an annual Employer Pension Notice) as published by the Cabinet Office. This can be completed using the relevant disclosure checklist.

32.29 The engagement team should agree all salary, bonuses, performance pay and benefits in kind to supporting documentation (payslips/P60s, agreements with the remuneration committee, contracts and P11Ds).

32.30 The remainder of the Remuneration and Staff Report is subject to our negative consistency statement. An actuarial expert has been appointed to provide assurance over the CETV disclosures provided by MyCSP through their central review of the Government Actuaries Department (GAD).

The engagement teams should review these disclosures for any unusual movements and ask the individuals concerned to confirm their accuracy for any unusual movements or new disclosures.

32.31 It should not be necessary for teams to obtain the MyCSP calculator to re-perform the calculations. The work of the actuarial expert provides sufficient assurance over the operation of the model and teams will be able to confirm the inputs used by MyCSP by reference to the inputs and outputs pdf file generated by the model.

Fees and charges

32.32 The Government Financial Reporting Manual (FReM) drafted by HM Treasury sets out the guidance on what needs to be disclosed for fees and charges raised under legislation enacted by the UK Parliament.

32.33 Disclosures of the outturn costs and incomes for services within the remit of fees and charges are covered by our audit opinion. The engagement team should obtain assurance that the expenditure and income disclosed are:

- free from material misstatement;
- in accordance with the governing legislation and Managing Public Money; and
- that the disclosures meet the requirements of the FReM.

Statement of losses and special payments

32.34 Losses and special payments are all are items that Parliament would not have contemplated when it agreed funds for departments or passed legislation. They are, by their nature, events or payments that ideally should not arise and are subject to special control procedures, including approval by HM Treasury either through the framework of delegated authorities or on a case-by-case basis.

32.35 The definitions of, and categories applied to, losses and special payments are set out in Annexes 4.10 and 4.13 of Managing Public Money.

32.36 The engagement team should perform procedures over losses and special payments, including completeness, following the requirements set out in the 'Regularity' Audit Response Group in Apex.

32.37 Departments should always consult HM Treasury (in advance) about special payments unless there are specific agreed delegation arrangements in place. Therefore, a department should seek Treasury approval, in advance, for any special payment for which it has no delegated authority, or which exceeds its authority. Departments have delegated authority to deal with all losses, unless there are specific delegations put in place.

32.38 Departments should consult the Treasury (in advance) on losses and special payments, irrespective of the amount of money concerned, if they:

- involve important questions of principle;
- raise doubts about the effectiveness of existing systems;
- contain lessons which might be of wider interest;
- are novel or contentious;
- might create a precedent for other departments in similar circumstances; and/or
- arise because of obscure or ambiguous instructions issued centrally.

Contingent liabilities and remote contingent liabilities

32.39 The engagement team should pay particular attention to the completeness of contingent liability disclosures and the adequacy of the presentation and disclosure in explaining the liability. Contingent liabilities may or may not have a value.

32.40 Procedures may include reviewing the processes in place at the audited entity to identify liabilities entered into and consideration of business information including Board and Audit Committee minutes for any indication of new liabilities.

32.41 In addition to contingent liabilities which departments are required to disclose under IAS 37 *Provisions, contingent liabilities and contingent assets*, there may be further contingent liabilities which departments are required to report to Parliament for accountability reasons in accordance with Managing Public Money ("remote contingent liabilities). Such contingent liabilities should be reported on in the Accountability Report and the engagement team should review these in a similar manner to those contingent liabilities that have been disclosed under IAS 37.

32.42 Engagement teams should carefully review any contingent liabilities disclosed under IAS 37 or remote contingent liabilities disclosed within the Accountability Report to ensure that they meet the definition and do not indicate the presence of a financial instrument (for example, a guarantee or derivative instrument).

32.43 As with provisions, there may be valid reasons for not providing a more detailed explanation; for example, disclosure may influence the outcome of a court case or be commercial in confidence. Engagement teams may consult FAPQ if they consider that the audited entity has legal or other reasons for not disclosing a contingent liability.

The Governance Statement

32.44 All central government bodies covered by the FReM are required to produce a Governance Statement for inclusion in their annual report and accounts.

32.45 The Governance Statement is a comprehensive explanation of organisational governance. It brings together in one place all disclosures about matters relating to corporate governance, risk management, and in the case of some departments, oversight of certain local responsibilities. In addition, HM Treasury's Corporate governance in central government departments: code of good practice ("the Code") was re-issued by Treasury in April 2017 and includes provision for a "comply or explain" approach whereby departures from the Code should be explained in the Governance Statement.

The Governance Statement – engagement team's review responsibilities

32.46 In accordance with an agreement between HM Treasury and the C&AG, the engagement team is required to review the Governance Statement to confirm that:

- it is in accordance with Treasury requirements, including the requirement for departments to explain significant departures from HM Treasury's Corporate governance in central government departments: code of good practice; and
- the disclosures are consistent with our understanding of the organisation based on the information that the engagement team are aware of from their work on the financial statements and other work.

32.47 As per paragraph 1-224 of Practice Note 10 (Revised 2022), the engagement team's responsibility in respect of the Governance Statement is to consider the statement. This review is not to provide assurance on the statement, but to:

- consider the completeness of the disclosures in meeting the reporting requirements;
- identify whether the disclosures are misleading; and
- identify any inconsistencies between the disclosures and the information that the auditor is aware of from audit work.

32.48 The extent of review procedures will vary according to the nature and content of our work. For a standard certification engagement, review procedures should include consideration of whether the Accounting Officer's review of the effectiveness of the system of internal control supports the disclosures made, and whether the disclosures are consistent with our understanding derived from our audit work.

32.49 The engagement team should consider at the planning stage what additional procedures to undertake to support a review of the Governance Statement. During the review, the engagement team should have regard to the knowledge of the entity obtained from audit work performed on the financial statements.

32.50 For departments, the engagement team should review the assurance provided to the Board over compliance with HM Treasury's Corporate governance in central government departments: code of good practice and ensure that this supports the disclosures made. The engagement team should consider whether they have become aware of any undisclosed non-compliance with the Code.

32.51 The engagement team should consider whether the Governance Statement covers the year under review and whether there are any material developments between the reporting date and the date the accounts are signed which should properly be included.

32.52 Appropriate evidence regarding the disclosures in the Governance Statement will usually be obtained by:

- considering whether the disclosures are consistent with our review of management board and committee minutes;
- reviewing supporting documents prepared for the board that are relevant to disclosures made in the Governance Statement. In doing this the engagement team should pay particular attention to the documentation prepared for Accounting Officers to support the statement made in connection with their effectiveness review and assess whether or not it provides sound support for that statement;
- gaining an understanding of the process defined by the Accounting Officer for their review of the effectiveness of internal control through enquiry of the senior management and comparing their understanding to the statement made by the Accounting Officer in the Governance Statement
- attending Audit Committee meetings at which corporate governance, internal control and risk management matters are considered;
- reviewing the Head of Internal Audit's formal annual report to the Accounting Officer which includes their overall opinion of the adequacy and effectiveness of the organisation's risk management, control and governance processes;
- relating the statement made by the Accounting Officer to our knowledge of the entity obtained during the audit of the financial statements (although the scope of the Accounting Officer's review will be considerably broader in its scope than the knowledge the engagement team can be expected to have obtained during the audit); and
- any other procedures the Engagement Director deems appropriate, including in relation to wider NAO objectives with respect to the entity's governance and internal control.

The Governance Statement – significant internal control issues

32.53 The engagement team should consider carefully if they believe there are any "significant internal control issues" for the purposes of the Governance Statement and raise these with management. If the engagement team has identified any significant deficiencies in internal control, these would usually be expected to be reported in the Governance Statement.

32.54 The engagement team should also consider whether any identified significant deficiencies in internal control should be reported to those charged with governance, with reference to the requirements of ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* and Chapter 57: Reporting to those charged with governance.

32.55 Our responsibility consists of assessing whether the disclosures made by the Accounting Officer of the processes they have applied to address any significant internal control issues appropriately reflect those processes.

32.56 The engagement team is not required to assess whether the processes described in the Governance Statement will, in fact, remedy any underlying weakness associated with the significant internal control issue.

32.57 If the engagement team is aware of a significant internal control issue that the Accounting Officer has not disclosed, they should discuss the position with the senior management of the entity and seek to resolve the discrepancy. If the engagement team is not able to agree with the Accounting Officer how the matter should be disclosed, they should consider the impact on the audit opinion.

32.58 Where the Accounting Officer does not undertake a review of the effectiveness of internal control, this departure from the Treasury's requirements should be disclosed and explained by the Accounting Officer in the Governance Statement. The engagement team should consider whether this requirement is met and whether the explanation is consistent with our understanding. If the engagement team decide that it is not, they should consider the impact on the audit opinion and/or whether it is an issue which should be reported.

32.59 Where appropriate, the Accounting Officer is required to set out details of actions taken or proposed, to deal with significant internal control issues. The purpose of this disclosure is to deliver assurance that significant internal control issues have been, or are being, addressed and that the Governance Statement is a balanced reflection of the actual position.

32.60 Determining significant internal control issues is a matter of judgement and cannot be defined to suit all contexts; the same issue may or may not be significant depending on the circumstances.

32.61 Managing Public Money notes the following non-exhaustive factors to consider when determining significant internal control issues to disclose in the Governance Statement:

- Might the issue prejudice achievement of the business plan or other priorities?
- Could the issue undermine the integrity or reputation of the organisation?
- What view does the Audit Committee take on the point?
- What advice or opinions have internal audit and / or external audit given?
- could delivery of the standards expected of the Accounting Officer be at risk?

- Might the issue make it harder to resist fraud or other misuse of resources?
- Does the issue put a significant programme or project at risk?
- Could the issue divert resources from another significant aspect of the business?
- Could the issue have a material impact on the accounts?
- Might national security or data integrity be put at risk?

32.62 ***Consultation required*** At the time of preparing the Governance Statement for a particular year, disclosure of information about a significant internal control issue might prejudice the outcome of a special investigation (possibly preventing successful prosecution of a case of fraud or inhibiting a disciplinary case against members of staff). In such circumstances, HM Treasury requires that the Governance Statement records that there are issues which cannot be disclosed because to do so would prejudice the outcome of an investigation. However, if the engagement team is not able to agree with the Accounting Officer how the matter should be resolved, they should again consider the impact on the audit opinion in consultation with FAPQ.

The Governance Statement – material inconsistencies

32.63 The impact on our opinion of a material inconsistency contained in the Governance Statement is the same as for a material inconsistency in the other information published with the financial statements and is considered in Section 13: Concluding and reporting.

The Governance Statement – knowledge from our wider work

32.64 Parliament and the relevant devolved government authorities might reasonably expect the engagement team to draw upon knowledge gained from all their audit work in performing their review of the Governance Statement. Thus, in concluding our review of the Statement, the engagement team should take account of not only the results of our financial audit work, but also any other relevant work carried out during the year.

32.65 The Engagement Director should specifically evidence that in concluding their review of the Governance Statement, account has been taken of all aspects of our work. In the case of contracted out audits, the Engagement Director also has prime responsibility for ensuring, and evidencing, that all relevant aspects of our work have been considered, in addition to the Governance Statement review work undertaken by the partner firm in the context of the financial audit.

32.66 For audited bodies with little or no relevant Value For Money (VFM) activity, a verbal assurance from the VFM director will be sufficient. However, for bodies subject to significant VFM activity, the responsible directors should use a formal sign off procedure.

Responsibilities in respect of the UK Corporate Governance Code

32.67 Paragraphs A53-8 to A53-13 of ISA (UK) 720 (Revised November 2019) (Updated May 2022) include requirements for entities that apply the UK Corporate Governance Code (not to be confused with HM Treasury's Corporate governance in central government departments: code of good practice).

32.68 As per paragraph A53-10 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), the engagement team is not required by the Listing Rules to review the directors' narrative statements of how they have applied the UK Corporate Governance Code principles and is required only to review the directors' compliance statement in relation to certain of the provisions applicable to entities. Nevertheless, because the directors' narrative statement comprises other information

included in the annual report, there is a broader requirement to read and consider all the other information. If the engagement team becomes aware of any material inconsistency between the financial statements or their knowledge obtained in the audit or otherwise appears to be materially misstated, the engagement team should seek to resolve it in accordance with ISA (UK) 720 (Revised November 2019) (Updated May 2022).

32.69 As per paragraph A53-11 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), the engagement team is required to obtain an understanding of the entity and its environment, including its internal control, sufficient to identify and assess the risks of material misstatement of the financial statements. To the extent that the engagement team has obtained an understanding of the internal control, they should use this knowledge when considering whether the other information contains a material inconsistency. However, when reviewing the Corporate Governance Statement, the engagement team is not expected to assess whether all risks and controls have been addressed by the directors or that risks are satisfactorily addressed by internal controls, as the requirements to comply with the UK Corporate Governance Code are wider than the requirements in the ISAs (UK).

32.70 As per paragraph A53-12 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), the engagement team should perform procedures to obtain appropriate evidence to support those statements made by management which the engagement team are required by the Listing Rules to review. Examples of such procedures include:

- Reviewing the minutes of the meetings of the board of directors, and of relevant board committees.
- Reviewing supporting documents prepared for the board of directors or board committees that are relevant to those matters specified for review by the engagement team.
- Making enquiries of certain directors (such as the chairman of the board of directors and the chairman of relevant board committees) and the company secretary to satisfy themselves on matters relevant to those provisions of the UK Corporate Governance Code specified for review by the engagement team.
- Attending meetings of the audit committee (or the full board if there is no audit committee) at which the annual report and account, including the statement of compliance, are considered and approved for submission to the board of directors.
- Requesting the directors to provide written confirmation of oral representations made during the course of the engagement team's review.

32.71 As per paragraph A53-13 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), if there is departure from a provision of the UK Corporate Governance Code but there is appropriate disclosure of this fact and the reasons for departure, as envisaged by the Listing Rules, the departure does not need to be referred to in the auditor's report. However, where the engagement team considers that there is not appropriate disclosure of a departure from a provision in the UK Corporate Governance Code, the engagement team should report this in the auditor's report.

Section 9: Testing techniques

Chapter 33: Analytical procedures

Relevant standards and guidance

33.1 ISA (UK) 330 (Revised July 2017) (Updated May 2022) includes requirements and guidance regarding the nature, timing and extent of audit procedures in response to assessed risks; these audit procedures may include substantive analytical procedures.

33.2 ISA (UK) 520 (Updated May 2022) *Analytical procedures* deals with the auditor's use of analytical procedures as substantive procedures ("substantive analytical procedures"). It also deals with the auditor's responsibility to perform analytical procedures near the end of the audit that assist the auditor when forming an overall conclusion on the financial statements.

33.3 Paragraphs 2-49 and 2-82 of Practice Note 10 (Revised 2022) include guidance on the use of analytical procedures in the audit of regularity.

33.4 This Chapter does not generally deal with the use of analytical procedures as risk assessment procedures, which is covered in Chapter 15: Gathering entity initial information and ISA (UK) 315 (Revised July 2020). However, when using analytical procedures as risk assessment procedures, engagement teams may refer to the sections in this Chapter entitled 'Types of SAPs' for guidance on forms of analytical procedure that may be appropriate to use as risk assessment or concluding procedures.

Background

33.5 As set out in paragraph 4 of ISA (UK) 520 (Updated May 2022), the term "analytical procedures" means evaluations of financial information through analysis of plausible relationships among both financial and non-financial data. Analytical procedures also encompass such investigation as is necessary of identified fluctuations or relationships that are inconsistent with other relevant information or that differ from expected values by a significant amount.

33.6 Where the engagement team are able to develop a reliable expectation to compare the recorded amounts against, SAPs can provide sufficient appropriate audit evidence to provide assurance:

- on their own for assertions not affected by significant risks; or
- in combination with tests of controls or tests of detail for significant risks.

33.7 An expectation may be developed based upon:

- comparable information for prior periods where there is an expectation for the current year outturn to be the same;
- anticipated results of the entity, such as budgets or forecasts, or expectations of the engagement team, such as an estimation of depreciation;
- similar entity information, such as a comparison of cost levels to similar entities;

- relationships that would be expected to conform to a predictable pattern based on the entity's experience, such as National Insurance as a proportion of salary costs, receivables as a proportion of income; or
- relationships between financial information and relevant non-financial information, such as payroll costs to number of employees, number of individuals eligible for a grant, etc.

33.8 The planned audit approach to each risk of material misstatement should reflect the Engagement Director and Engagement Manager's consideration of the most effective and efficient way of obtaining sufficient appropriate audit evidence the risk of material misstatement through a combination of tests of controls and substantive procedures, or substantive procedures alone.

33.9 Where SAPs are an effective and efficient source of substantive assurance, the Engagement Director and Engagement Manager should plan to use them as the substantive procedures required by ISA (UK) 330 (Revised July 2017) (Updated May 2022).

33.10 SAPs may provide high quality evidence, through coverage of the entire population, over completeness of expenditure or income (and so also completeness of payables and receivables). The appropriateness of using a SAP is dependent upon a number of factors including:

- the nature of the entity and its operations;
- the extent to which the account or the items to be examined can be predicted with reasonable accuracy;
- the engagement team's knowledge of the audited entity, gained from previous years' audits or auditing similar entities;
- the availability of financial and non-financial data from independent or assured internal and external sources;
- the relevance, level of detail and reliability of the information available; and
- the comparability and independence of information from different sources.

33.11 When auditing significant risks through substantive procedures alone, the extent of tests of detail and SAPs may vary to obtain the planned level of assurance. As an alternative to obtaining all assurance through tests of detail providing a High level of assurance, engagement teams may either:

- perform SAPs providing a Medium level of assurance, and tests of detail providing a Low level of assurance (in combination giving a High level of assurance); or
- perform SAPs providing a Low level of assurance, and tests of detail providing a Medium level of assurance (in combination giving a High level of assurance).

33.12 Planning and performing SAPs requires the engagement team to use professional judgement in:

- determining whether it is appropriate to use SAPs;
- determining whether the data used to develop an expectation is reliable;
- developing the expectation based upon an identified relationship in the data;
- determining the tolerable difference;
- investigating results of SAPs; and
- concluding upon the SAP.

33.13 Achieving the planned level of assurance is dependent upon the quality of the design of the SAP. In general, SAPs based upon a predictive model provide higher quality audit evidence than comparative analytical procedures.

33.14 However, depending upon the circumstances, relatively simple predictive or comparative analyses may be appropriate.

33.15 The appropriateness of SAPs will depend upon the nature of the assertion and our assessment of the risk of material misstatement. For example, if controls over processing of payments are deficient, the engagement team may decide to use tests of detail for expenditure rather than SAPs.

33.16 SAPs may also be appropriate to perform in combination with tests of detail. For example, when obtaining audit evidence regarding the valuation of accounts receivable balances, the engagement team may apply analytical procedures to an ageing of customers' accounts in addition to performing tests of detail on subsequent cash receipts to determine the collectability of the receivables.

33.17 Factors to consider when determining whether a SAP is appropriate include:

- source of the information available – for example, information may be more reliable when it is obtained from independent sources outside the entity;
- comparability of the information available – for example, broad economic data such as the overall inflation rate may not be appropriate for a department with particular cost pressures;
- nature and relevance of the information available – for example, whether budgets have been established as results to be expected rather than as goals to be achieved;
- controls over the preparation of the information that are designed to ensure its completeness, accuracy and validity – for example, controls over the preparation, review and maintenance of budgets; and
- prior year knowledge and understanding – for example, knowledge that there have been issues in prior years with the accuracy of a data source.

33.18 It may be appropriate to test the operating effectiveness of controls over the entity's preparation of information used by the engagement team in performing SAPs – if they are operating effectively, this would give greater confidence in the SAP. The operating effectiveness of controls over non-financial information may often be tested in conjunction with other tests of controls: for example, controls over payroll may also give assurance over data on headcounts.

33.19 The precision of a SAP is affected by:

- the accuracy with which the expected results of substantive analytical procedures can be predicted – for example, the engagement team may expect greater accuracy when predicting payroll costs than when comparing discretionary expenses, such as advertising, to prior periods as an expectation of current year outturn;
- the degree to which information can be disaggregated – for example, SAPs may be more effective when considering an expectation of salary costs by grade, or by different divisions, rather than the overall salary cost; and
- the availability of the information, both financial and non-financial – for example, the engagement team may consider whether financial information, such as budgets or forecasts, and non-financial information is available to design SAPs. If the information is available, its reliability should be considered as discussed above

33.20 It is unrealistic to expect analytical procedures to predict financial amounts or ratios exactly. Hence expected values, or the range within which they are likely to lie, need to be estimated. To help ensure that any bias that might be introduced by the engagement team is limited, the expected values and / or their range should be estimated before the analytical procedure is performed.

33.21 The expected value or its range should be determined using professional judgement. In some cases, where a statistically-based analytical procedure is used e.g. regression analysis, the range can be set to the confidence limits for that expected value. If the estimated range or the uncertainty associated with the expected value is very wide, the SAP may not be able to provide adequate assurance that the actual amount is not materially misstated.

33.22 A more complex procedure, with accurate and detailed input data, and a more complex model will usually provide higher precision and hence a higher level of assurance.

33.23 When conducting or evaluating the results of complex analytical procedures engagement teams may consult FAPQ.

33.24 As SAPs are effectively 100% tests of a risk of material misstatement, they will usually provide the planned level of assurance even if they detect a misstatement which exceeds the expected error rate for the audit identified at planning stage (i.e. a misstatement greater than the difference between materiality and performance materiality).

33.25 Engagement teams should not assume that just because data is generated from the audited entity's IT systems that it is a reliable basis for performing SAPs. Even if the engagement team has assurance over the operating effectiveness of general IT controls, this does not necessarily mean that the data has been appropriately inputted into the system.

33.26 Engagement teams should perform procedures to earn the right to rely on system-generated data used in developing an expectation for SAPs.

33.27 The section later in this Chapter entitled 'Testing of staff reports used in payroll SAPs' includes requirements relating to the use of Information Produced by the Entity (IPE) in SAPs covering payroll costs.

33.28 Engagement teams should inquire of management whether they consider the relationship selected to develop the expectation to be a plausible one.

33.29 Where variances are identified, the engagement team should inquire of management as to the reasons for them and obtain appropriate supporting audit evidence.

33.30 Planning and performing SAPs requires the engagement team to use professional judgement and achieving the planned level of assurance is dependent upon the quality of the design of the SAP. Accordingly, the Engagement Manager and Engagement Team-Leader will typically be involved in the design of SAPs for more complex or riskier balances.

33.31 Engagement team members performing SAPs should remember that they are intended to provide an equivalent level of assurance to a test of detail, and so should be based upon a comparable quality of audit evidence.

33.32 Reviewers should consider:

- the plausibility of the relationship used to develop the explanation;
- the reliability of the data used;
- the quality and plausibility of management's explanations of variances; and
- the audit evidence obtained to support the final conclusions reached.

Types of SAPs

33.33 Methods of analysis vary considerably from simple comparisons to complex analysis, using advanced statistical techniques. The sophistication, extent and timing of the procedures are based on the engagement team's judgement and may vary depending on the size and complexity of the audited entity. Teams may wish to consider whether they wish to use data analytics in deriving an expectation to use in performing the SAP.

Types of SAPs – reasonableness testing

33.34 Reasonableness testing is the analysis or modelling of the relationships of certain account balances to other balances, within an accounting period. The tests involve developing an independent expectation or prediction of an account balance based on financial and or non-financial data.

33.35 The effectiveness of this test is reliant on:

- the use of independent data (without which the test is redundant); and
- linkage of financial data directly to relevant operating data.

Types of SAPs – common size analysis

33.36 Common size analysis uses ratios to compare financial statements:

- from the same entity over different periods of time; or
- of different entities of a similar size and nature.

33.37 Common size analysis will usually be more appropriate as a preliminary or concluding analytical procedure, rather than as a SAP.

33.38 The ratios are calculated by expressing items in proportion to a common base, creating standardised financial statements, hence revealing trends and allowing easy comparisons to be made. The common size ratio for each line on the financial statement is given by the following equation:

$$\text{Common size ratio} = \frac{\text{Item of interest}}{\text{Reference item}}$$

33.39 For example, if the engagement team are considering inventory compared to total assets, then the common size ratio is:

$$\frac{\text{Inventory}}{\text{Total assets}}$$

33.40 The ratios are often expressed as percentages of the reference amount. Common size statements can usually be prepared for performance statements and statements of financial position, as follows:

- performance items expressed as a percentage of total expenditure; and
- statement of financial position items expressed as a percentage of total assets.

33.41 The ratios within the common size statement tend to have less variation compared to the absolute values themselves and hence trends in the ratios can also be used:

- to highlight significant fluctuation within the entity; or
- to develop time-series analysis using historical data.

33.42 Common size analysis is also seen as a combination of both ratio and trend analysis.

Types of SAPs – ratio analysis

33.43 Ratio analysis is any method that involves the comparison of:

- classes of transactions;
- relationships between account balances;
- relationships between financial statement accounts;
- an account to non-financial data; and/or
- relationships between entities of a similar nature or which operate within a particular sector or industry.

33.44 Ratio analysis will usually be more appropriate as a preliminary or concluding analytical procedure, rather than as a SAP. Ratio analysis is most effective when:

- the relationship between accounts is fairly predictable and stable; and
- the analysis is performed on disaggregated data (at aggregated level it tends to be relatively imprecise).

33.45 All comparisons made can be between two periods or over time, against budgets or against industry or sector statistics. Because ratio analysis can be used at both planning and review stages, it is also useful to compare both ratios against each other.

Types of SAPs – trend analysis

33.46 Trend analysis is the analysis of historical data which is used to establish patterns or relationships that can also be used to project future values. The item of audit interest can either be an absolute value or a ratio, which is examined over a period of time to determine a trend and possibly the extent of the deviation from an average value. Trend analysis will usually be more appropriate as a preliminary or concluding analytical procedure, rather than as a SAP.

33.47 Trend analysis is most effective when the account or relationship is fairly stable and hence is less appropriate when the entity being audited has experienced significant operating or accounting changes. Best results and higher levels of assurance are achieved when using disaggregated data, which tend to be more precise.

33.48 Methods include:

- graphical techniques such as scatter plots which rely on visual inspection;
- time-series analysis, which isolates trends from data by removing seasonal fluctuations; and
- regression analysis.

Building up audit assurance using SAPs

33.49 As set out in Chapter 17: Risk assessment and response planning, it is not possible to obtain the substantive assurance required for a significant risk through SAPs alone: i.e., at least some tests of detail should be performed if using a SAP. SAPs are capable of providing a maximum of Medium substantive assurance. However, even where Low or Medium substantive assurance is required to address a Significant risk (i.e. where controls assurance is also obtained), paragraph 21 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) requires that the substantive response to a Significant risk must include a test of detail.

33.50 Responses to significant risks relating to accounting estimates should be consistent with the requirements of ISA (UK) 540 (Revised December 2018) (Updated May 2022) and Chapter 36: Accounting estimates.

33.51 ***Figure 32A*** below shows how audit assurance is built up when using substantive analytical procedures.

Figure 32A: Possible build-up of audit assurance when using substantive analytical procedures

Level of inherent risk is Significant – Assurance from controls testing, SAP and test of detail

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Medium	SAP (Low) Test of detail (required under paragraph 21 of ISA (UK) 330 (Revised July 2017)) Total: Low

or

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Low	SAP (Low) Test of detail (Low) Total: Medium

Level of inherent risk is Significant – Assurance from SAP and test of detail

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	None	SAP (Medium) Test of detail (Low) Total: High

or

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	None	SAP (Low) Test of detail (Medium) Total: High

Level of inherent risk is Medium – Assurance from controls testing and SAP

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Medium	Low	Low	SAP (Low) Total: Low

Level of inherent risk is Medium – Assurance from SAP only

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Medium	Low	None	SAP (Medium) Total: Medium

Level of inherent risk is Medium – Assurance from SAP and test of detail

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Medium	Low	None	SAP (Low) Test of detail (Low) Total: Medium

Level of inherent risk is Low – Assurance from SAP only

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Low	Medium	None	SAP (Low) Total: Low

33.52 In planning whether to use SAPs to test area risk of material misstatement, the engagement team should, in accordance with paragraph 5(a) of ISA (UK) 520 (Updated May 2022), determine the suitability of particular SAPs for the transaction stream or balance subject to the RoMM, taking account of the relevant inherent risk factors and tests of detail, if any, for these risks of material misstatement.

33.53 Engagement teams should only plan to rely on SAPs if they give a comparable or higher quality of audit evidence to a test of detail.

Performing substantive analytical procedures

33.54 In accordance with paragraph 5(b) of ISA (UK) 520 (Updated May 2022), the engagement team should evaluate the reliability of data used to develop the engagement team's expectation, taking account of source, comparability, and nature and relevance of information available, and controls over preparation.

33.55 The engagement team should ensure that, where they use information produced by the entity, and/or system generated information, they carry out procedures sufficient to enable them to obtain adequate assurance that the information is reliable. The engagement team must also ensure that the audit file adequately reflects their consideration and assessment of this.

33.56 In doing this, the engagement team should consider the source, comparability, nature and relevance of the data as well as confirming its accuracy and completeness. Source data obtained from an entity's non-finance department is not independent of the entity and additional, proportionate audit procedures are needed to validate this data. These procedures should be directly referenced and explained in the SAP procedure write up in the audit file.

33.57 The engagement team should confirm with management that they consider the relationship used to be a plausible basis for developing an expectation.

33.58 In accordance with paragraph 5(c) of ISA (UK) 520 (Updated May 2022), the engagement team should develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated.

33.59 Paragraph 5(d) of ISA (UK) 520 (Updated May 2022) requires the engagement team to determine the amount of any difference of recorded amounts from expected values that is

acceptable without further investigation – this difference is termed the “tolerable difference”. The tolerable difference should be determined before comparing the expectation to the recorded amount.

33.60 The level of assurance that is to be obtained from any SAP is dependent upon the amount of assurance needed from that procedure to reduce audit risk to a specified level. The risk assessment performed at the planning stage, within the Risk Assessment in Apex, should be used to determine the level of assurance required from the analytical procedure. As the level of assurance increases, the corresponding level of precision required for the analytical procedure increases.

33.61 If performing SAPs to obtain a Medium level of assurance, the tolerable difference is given by the following equation:

$$\text{Tolerable difference} = \text{Materiality} \times \sqrt{\frac{\text{Recorded amount}}{\text{Materiality base}}}$$

where:

- Materiality = the materiality level of the whole account;
- Recorded amount = the recorded amount that is being audited (i.e., the figure recorded in the accounts); and
- Materiality base = the value used to calculate materiality (for example, gross expenditure).

33.62 The tolerable difference is capped at performance materiality. For example, in cases where the account area value can exceed the materiality base, such as where the surplus generated by an entity is adopted as the most appropriate materiality base, the tolerable difference should be set at performance materiality.

33.63 If performing SAPs to obtain a Low level of assurance, the tolerable difference is given by setting a percentage of 25% of the recorded amount based on auditor’s judgement, capped at performance materiality. The maximum assurance level provided by a SAP is Medium assurance, and therefore a SAP in isolation cannot provide High assurance.

33.64 The engagement team should compare the recorded amount to the expectation that they have developed.

33.65 If the variance between recorded amount and expectation is within the tolerable difference and there are no fluctuations or relationships apparent from the analysis which are inconsistent with other audit evidence or expectations, then the SAP has provided the planned assurance.

33.66 If the variance between recorded amount and expectation is greater than the tolerable difference or the engagement team identifies fluctuations or relationships apparent from the analysis which are inconsistent with other audit evidence or expectations, then in accordance with paragraph 7 of ISA (UK) 520 (Updated May 2022), the engagement team should investigate the differences as follows:

- inquire of management as to the reasons for the differences, and obtain appropriate audit evidence relevant to management's responses; and
- perform other audit procedures as necessary in the circumstances.

33.67 The engagement team should determine whether it is possible to evaluate management’s responses in the context of the engagement team’s understanding of the entity and other audit evidence obtained, or whether it is necessary to obtain additional audit evidence to support their explanations.

33.68 If management's explanations indicate that there are additional factors that should have been considered in establishing an expectation, the engagement team should consider revising the expectation and evaluate whether the revised expectation and recorded amount are within tolerable difference.

33.69 The evidence supporting the revised expectation should be of equivalent quality to the initial expectation. On occasion, it may be necessary go through more than one cycle of this process before arriving at an audit conclusion.

Testing of staff reports used in payroll SAPs

33.70 SAPs which are performed to obtain assurance over staff costs using a comparison to a prediction based on the entity's records of employee details and salary information (payroll SAPs) involve the use of Information Produced by the Entity (IPE), as described in Chapter 20: Evidence assessment and evaluation. In this case, the IPE usually consists of a report run from the entity's system or maintained by the personnel function which includes data such as employee starting and leaving dates, grades, contractual hours and pension scheme membership (staff reports).

33.71 If a payroll SAP has been performed in the prior year, then a level of assurance is assumed to have been built up over the data in the staff reports for existing staff, which reduces the inherent risk surrounding the accuracy of this data. Therefore, the approach to testing IPE within staff reports used in payroll SAPs is predicated largely on rolling forward this assurance and then focusing on any changes or amendments.

33.72 Unless concerns have been raised or errors identified in the prior year relating to the accuracy or completeness of payroll data, the engagement team should undertake the following procedures when performing a SAP covering payroll costs:

- select a sample from the population of all employees from the staff report, following the principles set out in the next paragraph;
- for each individual selected within the sample test of staff report data:
    - review their salary banding and confirm whether their actual salary falls within the banding for their stated grade; and
    - carry out full testing on any amendments affecting the individual (i.e., agree the relevant data points to an alternative source of primary evidence, such as employment contracts, employment offer letters, leaving forms, amendment forms, pay award letters, promotion forms or personnel records – this is not an exhaustive list of possible sources of primary evidence); and
- for each individual within the sample who was included in the prior year staff reports, agree the data relevant to producing the staff costs prediction within the SAP (including, as relevant: grade, proportion of full-time equivalent hours, pension scheme membership and allowances) to the prior year listing to confirm whether the data is consistent.

33.73 The sample test of employees from the staff report should be performed within the 'Accuracy of Data' tab in the Payroll SAP workbook using the following parameters:

- For Low assurance, the sample size should be 5% by volume (minimum 10 to maximum 15) and for Medium assurance the sample size should be 10% by volume (minimum 10 to maximum 30) subject to the following caveats:
    - For Low assurance, the sample should include a minimum of 5 starters and 5 leavers, or all of these if there are fewer than 5. The remaining sample size should be taken from the residual population.

- For Medium assurance or where the following IRFs are present with a weighting of Medium in the payroll risk assessment within the Risk Assessment in Apex, a minimum of 10 items of the relevant type (i.e., 10 starters and 10 leavers) should be included within the sample (the increases should be made even if they increase the total sample size to more than the 15 normally required to provide a Low level of substantive assurance):
  - The entity employs a seasonal workforce or otherwise has to increase its workforce in response to short term increases in the demand for its services (minimum of 10 starters and 10 leavers).
  - There have been staff transfers from other bodies (minimum of 10 starters and 10 leavers).
  - A recruitment campaign has occurred during the year (minimum of 10 starters).
  - The entity is restructuring or there is a redundancy round (minimum of 10 leavers).

- If the engagement team is performing interim audit procedures in accordance with Chapter 47: Interim audit procedures, including hard close audits and a significant volume of starters and leavers is not expected in the remaining stub period, the sample may be selected entirely from the population for the interim period. If this approach is taken, the engagement team should:
  - perform a risk assessment to confirm there has not been a significant volume of starters and leavers within the stub period (if a significant volume of starters or leavers is identified, the engagement team may decide to select top-up sample items to cover these);
  - confirm the individuals tested at interim flow through to the listing for the full year; and
  - test any amendments or departures affecting the sample items tested within the stub period.
- If the engagement team expects a significant volume of starters and leavers in the stub period, they may instead decide to test only an appropriate proportion of the sample from the interim period (for example, 25 out of a sample of 30) and then select the remaining items from the stub period population during the final audit stage.

33.74 If concerns have been raised or errors identified in the prior year relating to the accuracy or completeness of payroll data, the engagement team should perform procedures to obtain sufficient appropriate audit evidence to address the identified risks to accuracy or completeness in relation to the data points to which these risks are relevant.

33.75 There is a potential risk that employees may have left the organisation without this having been reflected within the payroll system, leading to their still being in receipt of salary to which they are not entitled. This risk is not relevant to the engagement team's assurance over the IPE within staff reports used in a payroll SAP, because this testing is concerned with the completeness and accuracy of the payroll costs recognised in the financial statements – instead, this amounts to a risk of fraud and/or irregular transactions.

33.76 The engagement team should therefore consider these risks as part of the Engagement Team Discussion on Risk and Fraud:

- Where no heightened fraud risk has been identified as part of this discussion, the risk is not considered to be material to the financial statements and no further action is required.
- Where a fraud risk is identified in relation to leavers, the engagement team should undertake procedures to ensure that the individuals in receipt of salary are entitled to that salary. Such procedures may include physically verifying the existence of the employee or seeking other evidence to demonstrate that they are still employed (for example an extant contract, correspondence with their line manager, evidence that they have interacted with business systems, clocking in cards, timesheets etc.).

Concluding and reporting

33.77 Where a suitable expectation has been developed and actual results (i.e., figures recorded within the financial statements are within a tolerable amount of the expectation), this provides the planned level of substantive assurance.

33.78 Where fluctuations or relationships are identified that are inconsistent with other relevant information or that differ from expected values by a significant amount, the engagement team should investigate the reasons for these and either:

- obtain the planned level of assurance by identifying appropriate evidence to support the explanations received;
- identify misstatements in the recorded amounts; or
- (unusually) identify evidence that the identified relationship is not an appropriate basis for SAPs and revise their planned approach.

33.79 If management is unable to provide an explanation of a matter identified when performing an analytical procedure, or the explanation, together with the audit evidence obtained relevant to management's response, is not considered adequate, the engagement team should consider whether a misstatement has been identified.

33.80 If the engagement team does not consider there to have been a misstatement identified, they may conclude that the identified relationship is not an appropriate basis for substantive analytical procedures and revise our planned approach to include alternative substantive procedures.

33.81 The engagement team should not automatically adopt an alternative approach without understanding why the relationship identified was inappropriate.

33.82 If a misstatement has been identified, the engagement team should consider whether they have achieved the planned level of assurance or whether additional procedures are required. If the misstatement identified exceeds the expected error rate assessed at the planning phase (i.e. is greater than the difference between materiality and performance materiality), the engagement team should clearly document the rationale for their conclusion on the adequacy of the scope of work performed.

33.83 The engagement team should understand the nature and cause of the misstatement and determine whether they indicate that other misstatements may exist. This may be due to a previously unidentified significant risk.

33.84 Indications that other misstatements may exist include if a misstatement arose from a breakdown in internal control, or from inappropriate assumptions or valuation methods that have been widely applied by the entity.

33.85 If there is a risk that other misstatements may exist that, aggregated with identified misstatements, may be material, the engagement team should revise the overall audit strategy and the audit plan, including the risk assessment and response planning process carried out in the Risk Assessment in Apex and the Regularity Testing Plan.

Chapter 34: Tests of detail

Relevant standards and guidance

34.1 ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks* deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor in accordance with ISA (UK) 315 (Revised July 2020) in an audit of financial statements.

34.2 ISA (UK) 450 (Revised June 2016) (Updated May 2022) *Evaluation of misstatements identified during the audit* deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.

34.3 ISA (UK) 500 (Updated May 2022) *Audit evidence* deals with the auditor's responsibility to design and perform audit procedures to obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the auditor's opinion. The standard provides guidance on the means available to the auditor for selecting items for testing, of which audit sampling is one means.

34.4 ISA (UK) 501 (Updated May 2022) *Audit evidence – specific considerations for selected items* deals with specific considerations by the auditor in obtaining sufficient appropriate audit evidence in accordance with ISA (UK) 330 (Revised July 2017) (Updated May 2022), ISA (UK) 500 (Updated May 2022) and other relevant ISAs (UK), with respect to certain aspects of inventory, litigation and claims involving the entity, and segment information in an audit of financial statements.

34.5 ISA (UK) 505 (Updated May 2022) *External confirmations* deals with the auditor's use of external confirmation procedures to obtain audit evidence.

34.6 ISA (UK) 530 (Updated May 2022) *Audit sampling* deals with the auditor's use of statistical and non-statistical sampling when designing and selecting the audit sample, performing tests of controls and tests of details, and evaluating the results from the sample.

Background

34.7 "Tests of detail" (ToD) are substantive audit procedures which do not involve analytical review.

34.8 ToD can include:

- 100% tests, covering every item in a population, possibly assisted with computer based techniques;
- Computer Assisted Audit Techniques, used to identify and focus testing on relevant items in the population; and
- audit sampling.

34.9 The procedures performed may include:

- physical examination;
- vouching;
- recalculation;
- confirmation of individual items or transactions;
- observation; and/or;
- inspection.

34.10 Appropriately designed ToD can provide sufficient appropriate audit evidence to provide all of the required assurance over an assertion, including when there is an Assertion-level significant risk. ToD may also be combined with tests of control or substantive analytical procedures to provide the overall planned assurance.

34.11 There are specific requirements under ISA (UK) 501 (Updated May 2022) for ToD to be performed when testing litigation and claims, inventory, and segmental information. Further guidance on these requirements is provided in Chapter 37: Other specific audit procedures.

34.12 The use of tests of controls (see Chapter 35: Controls testing) significantly reduces the required extent of ToD. Where there is a significant risk, although all assurance cannot be obtained from Substantive Analytical Procedures (SAPs), it may be effective and efficient to obtain our assurance through a combination of ToD and SAPs (see also Chapter 33: Analytical procedures).

34.13 ***Figure 33A*** in Chapter 33: Analytical procedures shows how the engagement team may build up assurance when using substantive analytical procedures, including where this is in combination with ToD.

34.14 Although using both SAPs and ToD require teams to perform two separate tests, this will often provide high quality audit evidence through providing assurance from both analysis against appropriately generated expectations and tests of underlying transactions.

34.15 SAPs are, in general, an effective and efficient source of audit evidence over large volumes of transactions which tend to be predictable over time. The planned approach should reflect the most effective and efficient approach to obtaining the planned levels of assurance.

34.16 The appropriateness of testing a risk of material misstatement through ToD (and through any particular test) is dependent upon a number of factors, including:

- the nature of the entity and its operations;
- the engagement team's knowledge of the audited entity, gained from previous years audits or auditing similar entities;
- our assessment of inherent risk factors and the inherent risk associated with the RoMM, including whether it is a significant risk and our assessment of the risk of fraud;
- the reliability of the control environment;
- the risk of management override of controls;
- the extent to which assurance over multiple assurances can be obtained at the same time;
- the need to incorporate an element of unpredictability into the testing; and
- the availability of financial and non-financial data from internal and external sources to enable testing, including whether information is available to perform computer assisted techniques such as recalculation, re-performance, auditor's estimation, stratification, statistical analysis and so on.

34.17 100% testing is where all transactions in the population are tested. This may be appropriate where, for example:

- the population constitutes a small number of large value items, and so it is time-efficient;
- there is a significant risk and other means do not provide sufficient appropriate audit evidence; and/or
- the repetitive nature of a calculation or other process performed automatically by an information system makes a 100% examination cost effective.

34.18 Common examples of 100% testing include testing the audit fee and remuneration of senior staff.

34.19 Selecting specific items – the engagement team may decide that, based on their understanding of the entity, assessed risks of material misstatement, and characteristics of the population, they wish to judgementally select specific items within the population to obtain assurance. Specific items selected may include:

- High value or key items: items are selected where they are of high value and/or have some other characteristic, such as items that are suspicious, unusual, particularly risk-prone or that have a history of error.
- All items over a certain amount: The engagement team may decide to examine items whose recorded values exceed a certain amount so as to verify a large proportion of the total amount of a class of transactions or account balance.
- Items to obtain information: The engagement team may examine items to obtain information about matters such as the nature of the entity or the nature of transactions

34.20 Selecting specific items for testing is a non-statistical sampling approach and will normally only provide sufficient assurance over the population where the engagement team are able to conclude and document that the risk of material misstatement has been reduced to the target level in respect of other items in the population, as it does not provide assurance over items which have not been selected. Selecting specific items may be appropriate for addressing a significant risk, where all items with characteristics of interest can be selected. Further guidance may be found later in this Chapter in the section entitled 'Sampling methods – non-statistical sampling'.

Planning and performing tests of detail

34.21 The risk assessment and response planning process for identified risks of material misstatement (RoMMs) should reflect the Engagement Director and Engagement Manager's consideration of the most effective and efficient way of obtaining sufficient appropriate audit evidence over each RoMM through a combination of tests of controls and substantive procedures, or substantive procedures alone.

34.22 Depending upon the entity's circumstances, appropriately designed tests of detail (ToD) may provide substantive assurance over any RoMM.

34.23 Although it may be possible to obtain all assurance over a RoMM from ToD, the engagement team should consider, as part of the risk assessment and response planning process, whether delivery of a quality audit requires ToD testing in combination with tests of controls (such as management accounts) or substantive analytical procedures (SAPs). Further guidance on these procedures may be found in Chapter 35: Controls testing and Chapter 33: Analytical procedures respectively.

34.24 In planning whether to use ToD to provide assurance over a RoMM, the engagement team ensure they are aware of:

- the level of assurance required from the ToD (i.e. a Low, Medium or High level of assurance);
- the nature of the populations and Inherent Risk Factors affecting the RoMM; and
- the outcomes (or expected outcomes) of any controls testing associated with the RoMM.

34.25 In particular, engagement teams should not assume that ToD based on large sample sizes will automatically provide a high level of assurance, as the assurance achieved depends upon the nature and timing of the procedures performed, as well as their extent.

34.26 In accordance with paragraph 10 of ISA (UK) 500 (Updated May 2022), the engagement team should determine means of selecting items for ToD and tests of controls that are effective in meeting the purpose of the audit procedure. There are three main selection methods available for ToD: 100% testing, selecting specific items and audit sampling.

34.27 ***Consultation required*** The engagement team should consult AMT when there are multi-location issues which affect the testing approach. In addition, engagement teams may consult AMT in determining the testing approach when:

- the account is a new assignment to the NAO;
- the account has historically high level of error or more errors than anticipated have occurred in the initial testing; and/or
- there are challenges in obtaining documentation.

34.28 In a ToD relating to the existence of accounts receivable, such as obtaining external confirmations, payments made by the customer before the confirmation date but received shortly after that date by the audited entity are not considered a misstatement. In addition, a mis-posting between individual receivable accounts does not affect the total accounts receivable balance is not considered a misstatement. Therefore, it may not be appropriate to consider this a misstatement in evaluating the sample results of this particular audit procedure, even though it may have an important effect on other areas of the audit, such as the assessment of the risk of fraud or the adequacy of the expected credit loss allowance.

34.29 A test only provides assurance over a risk of material misstatement if the nature of the test is appropriate. For example:

- Inspection of documents evidencing existence of an asset (such as a share certificate) may not provide assurance over ownership or valuation.
- Inspection of tangible assets may provide reliable audit evidence with respect to their existence, but not necessarily about the entity's rights and obligations or the valuation of the assets.
- Evidence of post-year-end receipt of payment on a receivable may evidence valuation, but not that it was a receivable of the entity at the period-end date (i.e. cut-off).

34.30 Other means of obtaining audit evidence are re-performance, observation and inquiry. In general, these are not appropriate for tests of detail, as set out below:

- Re-performance: independently executing procedures that were originally performed as, e.g., part of the audited entity's internal control. This may be done manually or through the use of computer assisted techniques such as auditing the logic and function of the audited entity's models in spreadsheets using a spreadsheet audit tool such as OAK.
- Observation: looking at a process or procedure being performed by others. Examples include the observation of the performance of control activities and observation of the counting of inventory by management. Observation provides audit evidence about the performance of a process or procedure, but it is limited to the point in time at which the observation takes place.
- Inquiry: seeking information from knowledgeable persons, both financial and non-financial, within and outside the audited entity's organisation. Inquiry alone ordinarily does not provide sufficient audit evidence and it should therefore be supported with corroboration through other types of procedure and/or inquiring of another knowledgeable person within or external to the entity.

34.31 In planning ToD, the engagement team should consider whether there are any assertions which external confirmations would be particularly appropriate to test, with reference to the requirements of ISA (UK) 505 (Updated May 2022) *External confirmations*. Paragraph 19 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) specifically requires the engagement team to

consider whether external confirmation procedures should be performed as substantive audit procedures. NAO policy is to confirm non-Government Banking Service bank balances and other information relevant to banking relationships, but it may be appropriate to obtain confirmations of:

- the terms of agreements, contracts, or transactions between an entity and other parties, including the absence of certain conditions or side agreements;
- accounts receivable balances and terms;
- property title deeds held by lawyers for safe custody or as security;
- amounts due to lenders, including relevant terms of repayment and restrictive covenants; and/or
- accounts payable balances and terms.

34.32 The higher the risk of material misstatement, the more likely it is that the engagement team may decide it is more effective to perform substantive procedures nearer to, or at the period end rather than at an earlier date, or to perform audit procedures unannounced or at unpredictable times (e.g. performing audit procedures at selected locations on an unannounced basis). This is particularly relevant when considering the response to the risks of fraud.

34.33 The appropriateness of a test to obtaining the planned level of assurance depends upon the nature, timing and extent of the procedures performed.

34.34 It is usually efficient to obtain an electronic listing of the population in order to select items for testing for overstatement. The engagement team should use the AIMS GL-TB Application to reconcile this listing to the amount included in the draft account or trial balance. They should then test any reconciling items.

34.35 The engagement team may obtain more persuasive evidence by increasing the quantity of the evidence through more extensive testing, or by obtaining evidence that is more relevant or reliable, such as by placing more emphasis on obtaining third party evidence.

34.36 The members of the engagement team designing and performing the procedures should have a clear understanding of what would constitute a misstatement so that the results of the procedures can be appropriately evaluated.

34.37 If an Assertion-level significant risk of material misstatement has been identified, paragraph 21 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) requires the engagement team to plan and perform procedures that are specifically responsive to that risk. Possible tests of detail include:

- External Confirmation: where representation of information is obtained directly from a third party. A bank certificate giving details of a bank balance at a specific date is an example of confirmation evidence.
- Recalculation: involves checking the mathematical accuracy of documents or records. Recalculation can be performed through the use of information technology, such as by obtaining an electronic file from the entity and using CAATs (spreadsheets or other analysis software) to check the accuracy of the file for calculations therein or totals derived therefrom.
- Inspection: involves examining records or documents, whether internal or external, in paper form, electronic form, or other media, or a physical examination of an asset. Inspection of records and documents provides audit evidence of varying degrees of reliability, depending on their nature and source and, in the case of internal records and documents, on the effectiveness of the controls over their production.

34.38 In general, the extent of audit procedures increases as the risk of material misstatement increases:

- As stated in paragraph 7(b) of ISA (UK) 330 (Revised July 2017) (Updated May 2022), the engagement team should obtain more persuasive audit evidence the higher the auditor's assessment of risk.
- As stated in paragraph A8 of ISA (UK) 500 (Updated May 2022), the quantity of audit evidence needed is affected by the auditor's assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required).

34.39 However, increasing the extent of an audit procedure is effective only if the audit procedure itself is relevant to the significant risk.

34.40 The use of computer-assisted audit techniques (CAATs) may enable more extensive testing of electronic transactions and account files, which may be useful to enable more extensive testing in response to a risk of fraud or material misstatement. Such techniques can be used to select sample transactions from electronic files; to sort transactions with specific characteristics; or to test or recalculate an entire population instead of a sample.

34.41 Although it is often appropriate to test a number of risks of material misstatement and irregularity through ToD, the engagement team should consider whether there are more effective and efficient ways to obtain assurance. In particular, if SAPs would provide sufficient appropriate audit evidence over risks of material misstatement, but not over regularity, it may be appropriate to design an alternative approach to obtaining regularity assurance.

34.42 Tests of detail based upon extensive sample tests of recorded amounts to supporting documentation can be simple to design and perform.

34.43 However, this does not mean that they are automatically the most appropriate way of obtaining all audit assurance required over an audit area:

- Tests from recorded information to supporting documentation do not provide assurance over completeness, so other testing will be required (see ***Table 33A*** above).
- Tests of detail can give very large sample sizes, without necessarily giving an understanding of unusual items or movements in the balance.
- Great care must be taken that the procedures performed do provide assurance over the risks of material misstatement that they are planned to cover.

34.44 In particular, when testing regularity, the nature of an appropriate ToD may vary significantly depending upon the precise nature of the balance, the risks identified and the relevant framework of authorities.

34.45 Engagement teams should only plan to obtain regularity assurance through comparison to supporting documentation once they have identified how that documentation will provide assurance over the regularity of the income or expenditure, either as a stand-alone test or in combination with other procedures; for example:

- Seeing that an invoice has been authorised does not necessarily evidence that it is regular – seeing that a grant has been authorised for payment based on a supporting file that evidences the spending incurred is in line with the purposes of the grant programme may do so.
- The engagement team cannot necessarily see that costs were incurred on a programme which has been authorised by Parliament simply by examining what an invoice is for.
- In a body with no specific requirements over staff expenditure, the engagement team may not need to test to documentation for pay. The engagement team may be able to get assurance over the risks of material misstatement through SAPs, and to obtain sufficient assurance over regularity by:

- a high-level calculation of whether they are at risk of having breached their pay remit (with follow-up if it appears that they may have); and
- review of any new activities undertaken in the year to see that these are permitted.

Reliability of information used in tests of detail

34.46 Paragraph 7 of ISA (UK) 500 (Updated May 2022) and the related application guidance require the engagement team to consider the relevance and reliability of the information to be used as audit evidence, including information obtained from an external information source, when designing and performing audit procedures. Paragraphs 1-113 to 1-114 of Practice Note 10 (Revised 2022) include guidance on the use of external information sources in the public sector.

34.47 Paragraph 9 of ISA (UK) 500 (Updated May 2022) and the related application guidance including requirements where the auditor uses information produced by the entity.

34.48 Audit evidence about the accuracy and completeness of information used in testing is necessary as the results of tests will be less reliable if they are based on inaccurate or incomplete data; for example, evaluating the recoverability of aged receivables is dependent upon the accuracy of the ageing used.

34.49 Evidence about the accuracy and completeness of information used in performing an audit procedure can be obtained concurrently as an integral part of the audit procedure itself, by testing controls over the preparation and maintenance of the information, or by additional audit procedures.

34.50 The engagement team should not assume that data is reliable simply because it is generated from the audited entity's IT systems. Even if assurance over the operating effectiveness of general IT controls has been obtained, this does not necessarily mean that the data has been appropriately inputted into the system. Engagement teams should perform procedures to earn the right to rely on any system-generated data that is used as the basis for ToD.

Timing of tests of detail and non-coterminous evidence

34.51 Tests of detail may be performed at an interim date or at the period end. The extent of the procedures performed should reflect materiality; the assessed risk; and the degree of assurance the engagement team plans to obtain.

34.52 Performing tests at an interim date may enable the engagement team to identify significant matters at an early stage. This enables the engagement team to resolve them with the assistance of management, or to develop an effective audit approach to address the issue. Further guidance may be found in Chapter 47: Interim audit procedures, including hard close audits. The process for interim and final sampling using the five-stage approach is set out in the section later in this Chapter entitled 'Sampling methods – statistical assurance sampling'.

34.53 Certain audit procedures can be performed only at or after the period end; for example:

- agreeing the financial statements to the accounting records;
- examining adjustments made during the course of preparing the financial statements; and
- procedures to respond to a risk that, at the period end, the entity may have entered into improper payments in advance of need, or transactions may not have been finalised.

34.54 Other factors that influence our consideration of when to perform audit procedures include:

- the control environment (as a strong control environment supports performing work at an interim date);
- when relevant information is available (for example, electronic files may subsequently be overwritten or procedures to be observed may occur only at certain times);
- the nature of the risk (for example, if there is a risk of manipulation of the inventory balance, the engagement team may wish to attend a year-end inventory count in accordance with ISA (UK) 501 (Updated May 2022)); and
- the period or date to which the audit evidence being tested relates.

34.55 Where the most recent evidence available supporting a balance is produced at a date different to the period-end date (non-coterminous year-ends), the engagement team should consider the sufficiency of that evidence. They should consider what procedures have been performed to bridge the assurance gap for non-concurrent year-ends, such as on significant investments, inventory and pension assets/valuations.

34.56 ***Consultation required*** The engagement team should also consult FAPQ where audit evidence supporting a balance is at a date different to the period-end date.

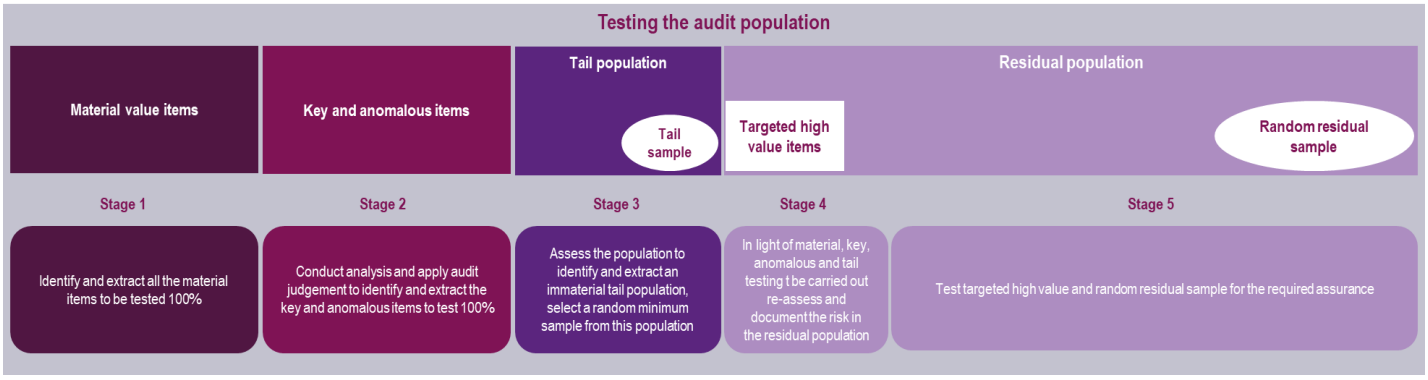
Background to the NAO's sampling approach

34.57 Audit sampling techniques avoid the onerous task of checking all entries making up a set of financial statements. The results of sampling work provide an estimate of misstatement in the accounts which comes with an associated precision or uncertainty. It is important for the engagement team to consider both the estimate of error and the precision around this estimate to make appropriate conclusions from the results of sample testing.

34.58 A risk-based approach to sampling is used and the sample sizes used are designed to provide a minimum ±5% precision for the required assurance. Sample sizes are determined within the Sample Planning Tool.

34.59 The overall process for substantive sampling in NAO audits is shown in ***Figure 34A*** below.

Figure 34A: The substantive sampling process



34.60 The sample source should be reliable and complete and tied to the trial balance and any reconciling items should be tested. The AIMS GL-TB Application should be used to agree the general ledger to the trial balance and identify potential duplicate entries. It will usually be most efficient to obtain an electronic listing of the population in order to perform sample testing.

34.61 After cleansing the sample of duplicates and journals, the engagement team should upload the cleansed data into the appropriate sample planning tool. Once the account planning information has been entered into the tool stage one is to identify all the material items for extraction. Stage two is to identify if there are items which appear to be of audit interest, these should be included as "key and anomalous items", documenting why this has been done. All material, key and anomalous items should be tested 100%.

34.62 To help target testing towards the areas of highest value, it may be applicable to identify an immaterial tail (which must be below performance materiality in total with no individual item being greater than 0.2% of performance materiality). This tail can be tested using a minimum sample, and this is stage three of the approach.

34.63 Stage four looks at the risk in the residual population, that is the population less the identified populations of material, key and anomalous, and immaterial tail items. The audit team may, at this point make a case to reduce the assurance required over the residual population if the planned testing in stages one to three address the risks of material misstatement to such an extent that the risk in the residual population is reduced from high to medium, or medium to low. This reduction in assurance over the residual population must be agreed by the Engagement Director. The assurance over the population as a whole remains the same and in line with the requirement established through risk assessment.

34.64 Stage five is the planned testing of the residual population. This is done on two levels, targeted testing of the highest value items, and random sampling of the remaining residual. The sample sizes are determined by the substantive sampling frames which are built into the sample planning tools. There are situations where this five stage approach is not the most suitable and the population lends itself to a different method. There is guidance available on these circumstances and the reasons for their choice should be noted by the audit team.

34.65 The residual population should be examined for batching as batched populations disguise the true audit population and can lead to either over or under misrepresentation of the sample. If batches are identified within the population, then in the first instance the client should be contacted to produce a sample listing that is unbatched and reconciles to the ledger. If this is not possible then the sampling a batched population flowchart should be followed. The engagement team should be aware that the sample size will increase due to this batching and the need to gain the required assurance in a multi-stage sampling approach. Further guidance on sample testing of batched populations is available in the section later in this Chapter entitled 'Batched populations'.

34.66 It is important to note that any items excluded from the sample source cannot be said to be represented in the results of the sample. Such exclusions bring bias to the sample results and this bias should be considered in the evaluation of the results of testing. Any excluded items, and not tested via other means, must be considered as known errors.

34.67 ***Consultation required*** A multi-location sampling approach may be required if transactions are processed or accounting records held at a number of locations such that a sample cannot be extracted from across the entire population. The sample should therefore be drawn in two stages: the number of locations to be visited, and the number of items to test at those locations. When evaluating the results, the engagement team should extrapolate the error at each location and across all locations. This will require expert help, which must be obtained from AMT.

34.68 In designing the procedures to be performed, the engagement team should be clear what would count as a misstatement. For example, in testing completeness of liabilities, a mis-posting between the accounts for two creditors would not represent a misstatement (although the

engagement team may need to consider whether this affects other areas of the audit, including reliance on controls).

34.69 The evaluations should be performed using one of the sampling evaluation tools. If the UEL exceeds materiality, the engagement team should follow the process set out above to evaluate the scope of work performed. If the engagement team changes their planning assumptions, they should ensure the revised approach is reflected throughout the audit file and update the overall audit strategy and audit plan, including the Risk Assessment in Apex and/or Regularity Testing Plan, as appropriate.

34.70 The engagement team should consider whether the misstatements identified appear to be due to a systematic error, or random (non-systematic).

- For systematic errors, teams should attempt to obtain evidence through the audited entity enabling them to quantify the total error:
- If the error is able to be quantified, then the engagement team would conclude that the planned assurance has been achieved from the test and the scope of work is adequate (albeit that the total error may be above materiality, which would then require adjustment for an unmodified audit opinion to be issued).
- ***Consultation required*** If it has not been possible to quantify the error, then this may indicate a scope limitation to the audit and the engagement team should consult with FAPQ.
- For random (non-systematic) errors, teams should first recheck the calculation of the error and additional precision. If this indicates the UEL is below materiality, then the engagement team would conclude that the planned assurance has been achieved from the test and the scope of work is adequate.

34.71 If sample testing is being performed on income or expenditure for the true and fair opinion, this can be extended to cover regularity. Engagement team members performing this testing need to have a good understanding of the framework of authorities (including the delegated authority limits for the entity).

34.72 The work performed should be documented in sufficient detail to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the procedures performed and their results.

34.73 Documentation should usually include:

- the total value of the population;
- the number and value of material items ;
- the number and value of key and anomalous items and why they were identified as such;
- the source of the listing used to generate the sample;
- the assessment and testing of an immaterial tail;
- any reassessment of the residual risk after the completion of the material, key and anomalous testing;
- the assurance level being tested and the number of targeted and residual sampled items;
- the tests performed on sampled items and how these tests address each risk of material misstatement;
- the results of the tests performed; and
- our investigation of the nature and cause of misstatements or irregularities and evaluation of their impact.

Sampling methods

34.74 Paragraphs 6 to 8 of ISA (UK) 530 (Updated May 2022) include requirements for sample design, size and selection of items for testing.

34.75 The five-stage sampling approach is shown in ***Figure 34B*** below and has five key stages:

- 100% testing of all material items;
- analysis of the audit population and use of audit judgement to identify and test all key and anomalous items;
- assess if the residual population has an immaterial tail of trivial or nil value items, if so remove and test a minimum random sample in the tail;
- assess the risk in the residual population and determine if the work conducted on material, key, anomalous and trivial items has mitigated this risk to the point where a reduced level of assurance is required in the residual; and
- using this risk assessment target, test the highest value items in the population and a random sample of the residual items.

Figure 34B: The five-stage approach to substantive tests of detail

Stage	Inherent assurance
1	Identify and test all material items.
2	Conduct analysis and apply audit judgement to identify key and anomalous items to test 100%.
3	Assess the population to identify a tail (immaterial total of trivial and nil values); if so, test a minimum random sample on the distribution tail.
4	In light of material, key and anomalous and tail testing, re-assess and document the risk in the residual population.
5	Test targeted high value and random residual sample for the required assurance.

34.76 Using this approach will:

- allow teams to exercise their audit judgment to target risk areas within a sample framework that gives representation;
- provide the required assurance given sufficient quality and rigour in the inherent and controls work conducted; and
- provide a clarity and consistency to the audit approach making review of the process simpler.

34.77 Detailed guidance on statistical assurance sampling and non-statistical sampling is given at the end of this Chapter.

Sample sizes

34.78 Substantive sample testing is divided into three elements and the overall sample size will be determined by the level required in each:

- the number of material, key and anomalous items which must be tested 100%;
- the testing of a minimum sample of an immaterial tail; and
- the assurance required as a result of the testing.

34.79 The assurance-based testing of the residual population (the total population less the material, key, anomalous and tail) is set out in the substantive assurance sampling frame and is divided into two parts: targeted testing of the highest value items and random testing of the remaining population (random residual testing). This entire approach ensures that each item in the population has a chance of selection whilst ensuring a minimum ±5% precision at the required assurance level.

34.80 The population should be tested for a skew towards a small volume of the population holding a high proportion of the value. Where this is the case the skewed substantive sampling frame shown in ***Figure 34C*** is used. Where there is no skew in the population then the standard substantive sampling frame shown in ***Figure 34D*** should be used. A separate sampling frame applies for low volume populations of 50 items or fewer (see following paragraph). The qualitative terms of Low, Medium and High assurance are used to determine the level of assurance provided by sample testing.

34.81 Where the population is 50 items or fewer, the low volume population sampling frame shown in ***Figure 34D-a*** should be used. A test of skew will determine (after testing all material, key and anomalous items) if more than 90% of the remaining population value is in the five highest value items:

- If more than 90% of the remaining population value is in the five highest value items, the engagement team should follow the skewed population part of the sampling frame.
- Where there is no skew in the population after testing all material, key and anomalous items, the engagement team should follow the non-skewed part of the frame.

Figure 34C: The skewed substantive sampling frame

Test to identify a skewed population				
Test for skew in the residual population	**Targeted testing of highest value items**	**Random sample of the remaining residual**		
		High assurance	**Medium assurance**	**Low assurance**
90% to 99% in largest 5 items	5	1 if immaterial 5 if < 5 x materiality 10 if > 5 x materiality	1 if immaterial 3 if < 5 x materiality 5 if > 5 x materiality	1 if immaterial or switch to standard frame
80 to 89% in largest 10 items	10	3 if < 5 x materiality 5 if 5 to 20 x materiality 10 if >20 x materiality	3 if < 5 x materiality 4 if 5 to 20 x materiality 8 if >20 x materiality	Use standard frame
70 to 79% in largest 15 items	15	3 if < 5 x materiality 10 if 5 to 20 x materiality 15 if > 20 x materiality	3 if < 5 x materiality 5 if 5 to 20 x materiality 10 if > 20 x materiality	Use standard frame
60 to 69% in largest 20 items	20	3 if < 5 x materiality 15 if 5 to 20 x materiality 20 if > 20 x materiality	3 if < 5 x materiality 10 if 5 to 20 x materiality 15 if > 20 x materiality	Use standard frame

***Note** – the audit team may elect to test additional high value items to reach either a percentage threshold or to reduce the ratio to materiality and hence reduce the level of residual testing required, for example if testing an additional 2 items takes you from 69% to 72% then test the highest 17 and use the appropriate residual for the 70 to 79% skew.*

Figure 34D: The standard substantive sampling frame

Material, key and anomalous items		Test 100% of those identified	
Immaterial tail of individually trivial items		Test a minimum of 2, or 1 per audit stage (interim and final)	
Residual population testing in a NON-SKEWED population			
1. Low assurance required	**Targeted testing of highest value items**	**Random sample of the residual population**	**Overall sample**
Residual < 2 times materiality		3	3
Residual 2 to 5 times	3	3	6
Residual > 5 times materiality	3	5	8
2. Medium assurance required	**Targeted testing of highest value items**	**Random sample of the residual population**	**Overall sample**
Residual < 5 times materiality	5	5% of volume (min 10 to max 15)	15 (20)
Residual 5 to 20 times materiality	10	8% of volume (min 10 to max 20)	20 (30)
Residual > 20 times materiality	10	10% of volume (min 15 to max 30)	25 (40)
3. High assurance required	**Targeted testing of highest value items**	**Random sample of the residual population**	**Overall sample**
Residual < 5 times materiality	10	15% of volume (min 20 to max 30)	30 (40)
Residual 5 to 20 times materiality	10	20% of volume (min 30 to max 45)	40 (55)
Residual > 20 times materiality	10	25% of volume (min 30 to max 60)	40 (70)

Figure 34D-a: The low population volume sampling frame

Material, key and anomalous items		Test 100% of those identified		
Residual population testing in a SKEWED low volume population				
Positive skew level (%)	**Targeted testing of highest value items**	**High assurance**	**Medium assurance**	**Low assurance**
90% to 99% in largest 5 items	5	1 if immaterial 5 if < 5x materiality 10 if > 5x materiality	1 if immaterial 3 if < 5x materiality 5 if > 5x materiality	1 if immaterial or use NON-SKEWED low volume assurance
Residual population testing in a NON-SKEWED low volume population				
		Targeted testing of highest value items	**Random sample of the residual population**	**Overall sample**
Low assurance	< 2x materiality	-	3	3
	> 2x materiality	3	3	6
Medium assurance	< 2x materiality	5	3	8
	> 2x materiality	5	5	10
High assurance	< 2x materiality	5	7	12
	> 2x materiality	5	10	15

Sample sizes – payroll testing

34.82 ***Table 34E*** below shows the sample sizes that should be used for substantive testing in response to a risk of material misstatement (RoMM) associated with starters, leavers and amendments, in order to provide either a Low, Medium or High level of assurance over the RoMM. These sample sizes relate to employees rather than transactions and sample items should be selected randomly from payroll reports.

Table 34E: Sample sizes for substantive ToD over payroll employees

Level of substantive assurance required	Low	Medium	High
Starters	5	10	15
Leavers	10	15	20
Amendments	10	12	15
In-year	10% by volume, min 5 to a max of 10	15% by volume, min 5 to a max of 15	20% by volume, min 5 to a max of 20
Max sample size	35	52	80

34.83 ***Table 34F*** below shows the sample sizes that should be used for controls testing in response to a risk of material misstatement (RoMM) associated with starters, leavers and amendments in order to provide either a Low, Medium or High level of assurance over the RoMM. These sample sizes relate to individual payroll transactions (for example, a sample item may be one month's pay for an employee).

Table 34F: Sample sizes for controls testing over payroll transactions

Level of controls assurance required	Low	Medium	High
Starters	10	15	20
Leavers	10	15	20

Amendments	10	15	20

Sample selection

34.84 Sampling is reliant upon the quality of the data from which the sample is selected, the sample source. The engagement team should check that the sample source is suitable and that the source is a complete and accurate record of the total population to be audited. The population should be cleansed and sense checked, and where possible cleansed of batches so that data is obtained at the most granulated level possible whilst being able to be reconciled to the general ledger.

34.85 When selecting the sampled items, the engagement team should ensure that, where possible, bias is avoided. When selecting items for testing, the engagement team should take into account the purpose and objectives of the audit test. The engagement team should not be drawn by easily available items or interesting looking files or allow the audited body to select the samples on their behalf.

34.86 A random element should be included in sample section to ensure the sample is representative of the population and is reliable enough to allow inferences to be made about the population from which the sample was drawn. Ideally one of the sampling planning tools should be used for this purpose.

34.87 ***Consultation required*** Engagement teams need to evidence on file the basis for the sample approach. Sample sizes should comply with the guidance in this Chapter unless otherwise approved by AMT: for example:

- where there are complexities around additional stratification requirements;
- where the engagement team believes the sample effort to be disproportionate;
- where there is a high volume low value population; or
- where a multi-locational element exists.

Batched populations

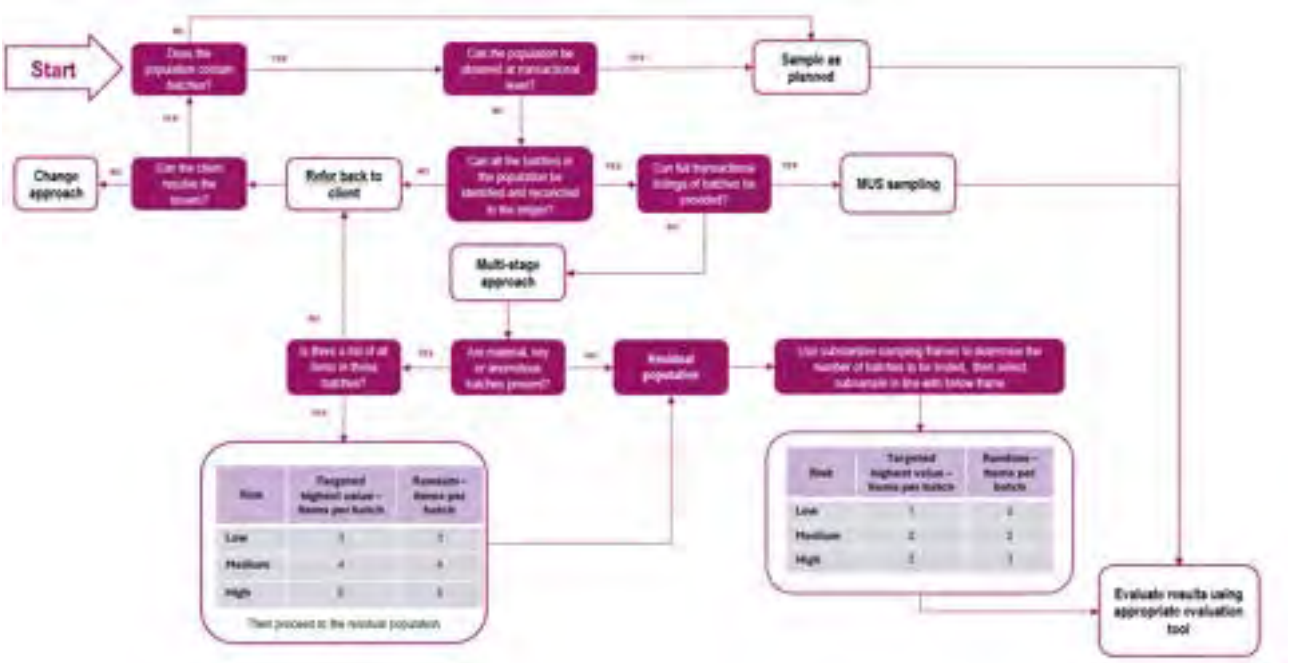
34.88 In tests of detail, sample items are usually selected at the transactional level: this allows for selection, testing and evaluation to be conducted at one level and for the results found to represent this level. Batched populations hide the population distribution, meaning that error estimates may either over- or underestimate the true position.

34.89 Where the population contains batches, these may:

- be few or many in number – the lower the proportion of the population that is batched, the less the distortion of the population distribution;
- contain few or numerous items – the more items in the batch, the less likely that a single item is representative; and
- contain similar or varied content – the former can be represented by a single item; the latter may require representation of the range of items.

34.90 The sample size required to test a batched population may therefore be higher than for a non-batched population, as the sample becomes a multi-stage one where there is a required precision that needs to be achieved at each stage. The engagement team should follow the sampling a batched population flowchart shown in ***Figure 34G*** below to determine the approach.

Figure 34G: Sampling a batched population



Performing sample tests

34.91 Paragraphs 9 to 11 of ISA (UK) 530 (Updated May 2022) and the related application guidance set out requirements to perform audit procedures on selected items, or replacement items (see following paragraph), and to treat a selected item as a misstatement where the auditor is unable to apply the designed audit procedures, or suitable alternative procedures, to that item. The engagement team should apply similar principles to sample testing for the purpose of the regularity opinion (for example, by treating a selected item as an irregular transaction where the auditor is unable to apply the designed audit procedures over regularity, or suitable alternative procedures, to that item).

34.92 Using a replacement item under paragraph 10 of ISA (UK) 530 (Updated May 2022) is not an alternative to recording identified misstatements or irregular transactions and should only be used where there are genuine and explainable reasons why a replacement had to be used. The reasons for any replacement items should be documented on the Apex audit file.

34.93 If the selected items are not tested appropriately, this will invalidate the tests being performed. The engagement team should:

- ensure all items within the population are available for sample selection;
- make sure that the audit test complies with the audit plan so that the responses to the tests provide the required evidence;
- test the sample item against the evidence;
- verify any discrepancies between the book value and audit value;
- gain explanations and evidence for those explanations - these must be credible and from an appropriate source; and
- record results accurately.

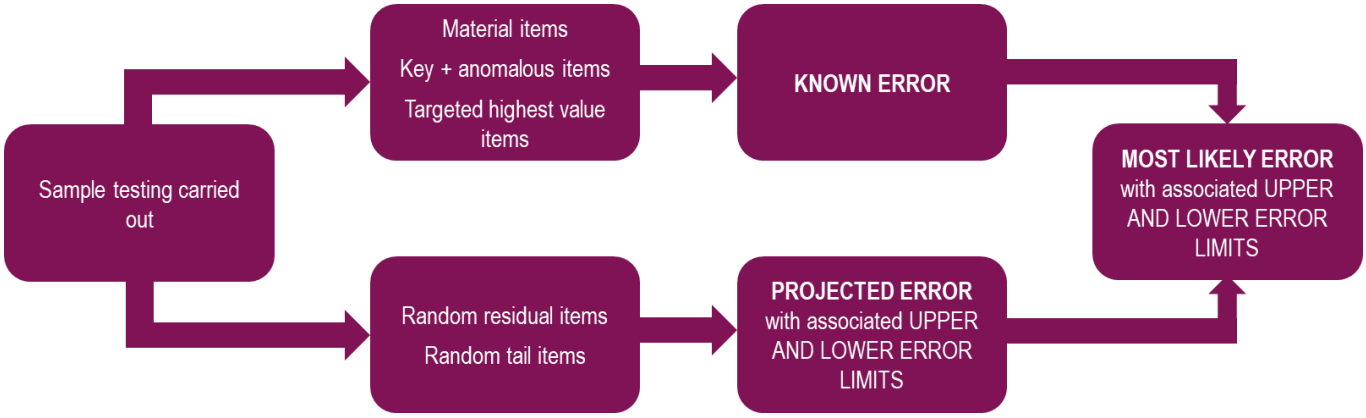
Sample evaluation, concluding and reporting

34.94 In accordance with paragraph 15 of ISA (UK) 530 (Updated May 2022) and the related application guidance, the engagement team should evaluate the results of sample ToD and whether the use of audit sampling has provided a reasonable basis for conclusions about the population that has been tested.

34.95 The Most Likely Error (MLE), as shown in ***Figure 34H*** below, is a combination of the findings of the:

- 100% testing of material, key and anomalous items, and the targeted testing of the highest value items which are the known errors, and
- the extrapolated impact of the sampled tail and residual populations, which are the projected errors under paragraphs 14 and A18 to A20 of ISA (UK) 530 (Updated May 2022). The extremely rare circumstances where sampling errors are considered to be anomalies and not extrapolated are dealt with in paragraph 13 of ISA (UK) 530 (Updated May 2022).

Figure 34H: Most Likely Error



34.96 In accordance with paragraph 12 of ISA (UK) 530 (Updated May 2022) and the related application guidance, the engagement team should understand the nature and cause of any deviations or misstatements (or, where a regularity opinion is provided, irregular transactions) identified and determine whether they indicate that other misstatements (or irregular transactions) may exist, including whether they impact upon other areas of the audit. This may be due to previously unidentified risks of material misstatement or risks of material irregular transactions, including significant risks.

34.97 Indications that other misstatements or irregular transactions may exist include if a misstatement or irregular transaction arose from a breakdown in internal control or from inappropriate assumptions or valuation methods that have been widely applied by the entity.

34.98 If there is a risk that other misstatements or irregular transactions may exist that, aggregated with identified misstatements or irregular transactions, may be material, the engagement team should, as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan to reflect any additional risks of material misstatement or risks of material irregular transactions (the Engagement Manager and Engagement Director should be involved in this process).

34.99 In understanding the nature and cause of misstatements or irregular transactions, the engagement team may identify that many have a common feature, such as type of transaction, location, or time period. In such circumstances, the engagement team may decide to identify all items in the population that possess the common feature and extend audit procedures to those items.

34.100 In addition, such misstatements or irregular transactions may be intentional, and may indicate the possibility of fraud. Where the engagement team identifies a misstatement, paragraph 36 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires them to obtain an understanding of how the misstatement arose and evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the engagement team should revisit the Engagement Team Discussion on Risk and Fraud and, as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan to reflect any additional risks of material misstatement or risks of material irregular transactions. Further guidance may be found in Chapter 30: Fraud responsibilities.

34.101 The approach to quantitatively assessing misstatements varies depending upon the testing approach adopted. For 100% tests, the actual error in the population will have been quantified and can be evaluated. For sample tests, the engagement team need to evaluate both the errors identified and whether the planned assurance has been obtained.

34.102 The engagement team should evaluate whether the planned level of assurance has been achieved from the sample by comparison of the MLE + associated precision (giving the Upper Error Limit (UEL)) to materiality. The possible outcomes of this evaluation are shown in ***Table 34I*** below.

Table 34I: Possible outcomes of extrapolated sample testing

Upper Error Limit	Most Likely Error	Lower Error Limit	Conclusion on misstatement	Conclusion on scope
Less than materiality	Less than materiality	Less than materiality	95% confident that not materially misstated	Planned level of assurance achieved.
Greater than materiality	Less than materiality	Less than materiality	***Consultation required*** Insufficient evidence to draw a conclusion. Additional work may be required (refer to additional sampling guidance) and AMT advice should be sought if necessary.	
Greater than materiality	Greater than materiality	Less than materiality	***Consultation required*** Planned level of assurance not achieved and scope limitation may be required. AMT advice should be sought.	
Greater than materiality	Greater than materiality	Greater than materiality	***Consultation required*** 95% confident that a material misstatement has occurred. Planned level of assurance not achieved and scope limitation may be required. FAPQ and AMT advice should be sought.	

34.103 If the UEL is less than materiality, reasonable assurance has been obtained that the balance is not materially misstated. If the UEL is above Materiality, then sufficient assurance may not have been obtained from the work performed. The engagement team should follow the process set out in ***Figure 34J*** below to evaluate the scope of work performed.

Figure 34J: Process where UEL exceeds materiality

34.104 In addition to evaluating the impact of the misstatements identified within the population being tested, the engagement team should evaluate errors identified by totalling the MLE from each population tested. The total MLE from all populations subject to sample testing should be calculated and compared to performance materiality to assess whether further audit work is required.

34.105 UELs can also be combined and the way this is done will depend on the sampling method. Where a combination of sampling methods has been used, the individual area UELs will need to be assessed against materiality so that an audit judgement can be made if the combination of all the errors would lead to the combined UEL breaching materiality.

34.106 The engagement team should communicate any errors identified and obtain representations in respect of any uncorrected misstatements. Further guidance may be found in Section 13: Concluding and reporting.

34.107 If the engagement team has not identified any errors in their testing, the planned assurance will have been achieved, unless any other issues for consideration have been identified.

Sampling methods – statistical assurance sampling – the five-stage approach

34.108 To gain substantive assurance from an audit population via tests of detail using the five-stage approach, the auditor will need to follow the five-stage approach shown in ***Figure 34B*** earlier in this Chapter.

34.109 The skewed and standard substantive assurance sampling frames, from which sample sizes are derived for the five-stage approach, are shown in ***Figure 34C*** and ***Figure 34D*** earlier in this Chapter.

34.110 The sample sizes within the frame have been calculated to achieve a minimum ±5% precision with the expected risk of error for the required assurance, and those sample sizes are determined for the entire accounting period.

34.111 Most audits are broken down into several phases of audit sampling so that audit teams can progress work at the earliest stage, such as during one or more interim fieldwork visits.

34.112 An interim sampling phase is defined as any audit testing period that does not cover the entire accounting period. For example, testing periods covering periods 1 to 6 or periods 11 to 12 of the year would be interim sampling phases. The sum of the lengths of the interim sampling phases should equal the entire accounting period to ensure that each item has had a chance of selection.

34.113 For each sampling phase the audit team should enter the data for that period into one of the sample planning tools. The data should be marked as interim with the number of months to be tested being marked in the Tool (the data should only be marked as final when it contains the data for the entire accounting period).

Figure 34K: Splitting the audit work at interim and final

	Material	Key and anomalous	Tail	Residual	
				Highest value items	Random
At each interim	All identified	All identified	1	**Either** the proportion of the required number in relation to the number of periods tested **or** none	The proportion of the required number in relation to the number of periods tested
At final	All identified	All identified	1	**Either** the proportion of the required number in relation to the number of periods tested **or** all required	The proportion of the required number in relation to the number of periods tested
Overall	**All those identified across the whole period**		**Minimum of 2**	**Full period complement from the appropriate sampling frame**	

Notes:

a) ***Tail*** *– the tail will be calculated based on the proportion of performance materiality and the use of a cut-off value in accordance with the tail rules. If an error is found in the tail an additional item may be required to be tested*

b) ***Highest value items in the residual population*** *– the auditor can elect to test a proportion of these at interim or leave them until the year end, the benefit of leaving until the year end is that the population is known and there is no risk of testing items at interim that fall out of the highest required number.*

c) ***Test of skew*** *– this can be carried out at each interim but it may be the situation where an interim is skewed but another is not, or it could be that each interim is not skewed but the overall may have been – where the population volume is expected to be low the audit may be more efficiently carried out as a whole period to accurately determine the test of skew*

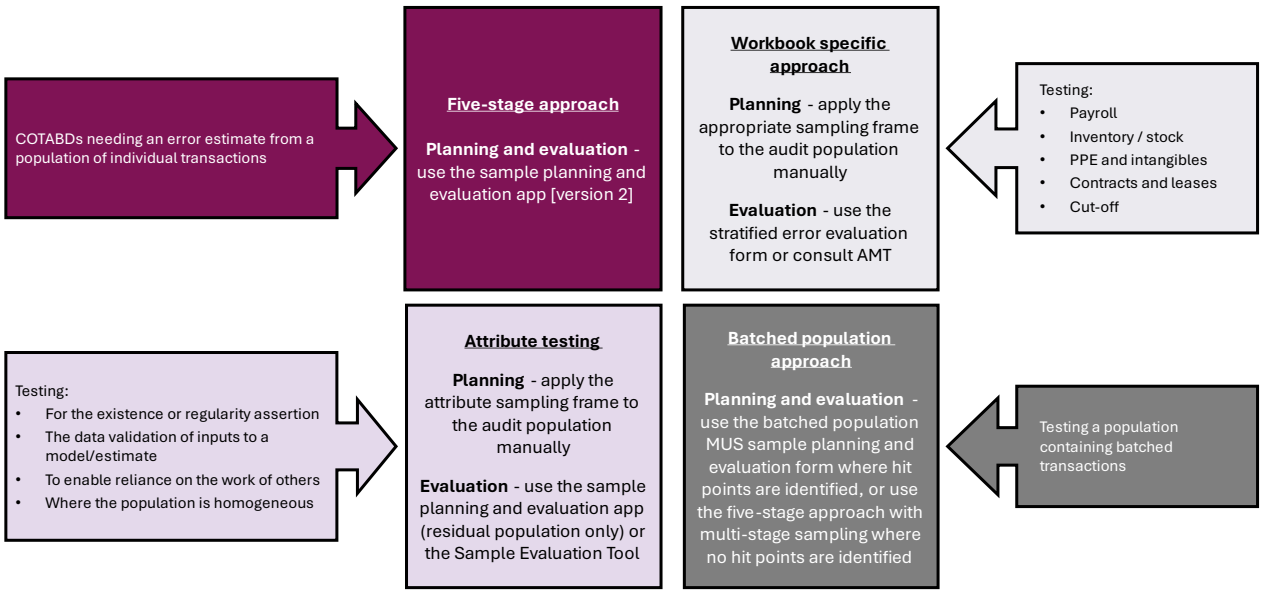
34.114 Once testing has been completed for a phase, the results for that phase may be entered into one of the sample evaluation tools to see the impact of the errors found. At each subsequent phase the test results can be added into the existing evaluation whilst updating the tool for the values and volumes of the population that has been tested.

34.115 At final audit, once any testing for their final sampling phase (i.e., the last period(s) leading up to P12 or beyond if applicable) has been identified, the audit team should:

1. Check that all material items have been identified and tested across the entire accounting period.
2. Check that all key and anomalous items have been identified and tested across the entire accounting period.
3. Check that where applicable the tail items have been tested across the whole accounting period.
4. Identify the highest value items in the population and test them (if some were tested at interim then top up with the remaining sample items), and
    - If any of these items have been tested previously as they were selected as part of the random sample them count them as part of the highest value item testing and randomly select a residual item to be tested as a replacement in the random residual element.
    - Any high value items that were tested at interim but have since fallen out of the targeted population should be marked as key and anomalous items.

34.116 ***Consultation required*** There may be occasions where other statistical methods may be required to gain substantive assurance, and these are shown in ***Figure 34L*** below. There may also be occasions where the engagement team believe the standard approach is disproportionate to the identified risk. Where this is the case, it may be appropriate to use an alternative approach such as Monetary Unit Sampling (MUS) after consultation with FAPQ or AMT. This consultation process must be documented on the audit file. The planning and evaluation forms for this approach will be provided as part of the consultation process.

Figure 34L: Comparison of different sampling approaches



Sampling methods – non-statistical sampling

34.117 Non-statistical sampling methods are any sampling techniques where either a random selection of sampled items is not made, or probability theory is not used to evaluate sample results, including measurement of sampling risk.

34.118 Wherever possible a statistical method of sampling should be used; it is only in very specific circumstances which must be well documented that it may be appropriate to use a non-statistical sampling method:

- testing for understatement errors (i.e. whether items are omitted or recorded at too low a value in the ledger - in general as a test of the completeness assertion); or
- performing testing to obtain an understanding of a balance, but not to obtain assurance over an assertion per se. This is often in order to select a series of case studies to examine an issue on a sample basis.

34.119 Non-statistical sampling methods provide indicative results and cannot be extrapolated to be representative of the population because:

- the way that the sample is picked does not give every item in the population a chance of selection;
- engagement teams do not have the information to evaluate the assurance achieved using probability theory;

- engagement teams are only able to test from part of the population (e.g. when testing completeness of liabilities from unpaid invoices, engagement teams can only test from invoices which have been received to date, not ones which are still to be received – as time goes by, the coverage of the population will increase);
- the sample size is insufficient to be statistically valid; and
- a combination of these factors.

34.120 More senior members of the engagement team would typically be involved in the judgements applied in deciding whether it is appropriate to use non-statistical sampling to obtain assurance over an assertion and whether the planned level of assurance has been achieved when using non-statistical sampling.

Sampling methods – non-statistical sampling – principles of using non-statistical sampling to obtain assurance over assertions

34.121 Although non-statistical sampling does not enable the engagement team to draw statistically based conclusions about balances, if engagement teams wish to obtain assurance over an assertion the sampling method and tests used still need to enable them to draw conclusions that there is not a material misstatement.

34.122 ***Table 34M*** below sets out when to use non-statistical sampling to obtain assurance over assertions.

Table 34M: Appropriateness of using non-statistical sampling to obtain assurance over assertions

Non-statistical sampling is appropriate when:	Non-statistical sampling is not appropriate when:
The completeness assertion (or otherwise for understatement) is being sample tested, and the engagement team are unable to obtain a complete listing of the relevant population to sample from.[5]	In general, when selecting a sample from recorded amounts in the entity's ledgers.
The engagement team wishes to focus the sample selection upon items with particular characteristics, and it is not effective and efficient to use profiling (for example, due to the lack of an electronic breakdown of the balance).	Electronic breakdowns of the balance are available, enabling the engagement team to use profiling to select items.

34.123 The process for testing a population through non-statistical sampling consists of:
- determining whether it is appropriate to use non-statistical sampling;
- determining the sample size;
- determining the sampling approach and selecting sampled items;
- performing tests of detail; and
- evaluating the results of procedures performed.

34.124 The approach adopted should be fully documented. If a test is being performed to generate case study or illustrative information, the engagement team may agree the approach at the planning stage with the audited body to help when reporting the results of the work.

Sampling methods – non-statistical sampling – determining the sample size

[5] (*) I.e. the engagement team is testing from a population "in the world" which they are not able to establish is the full population. For example, the engagement team is selecting from the population of invoices received through to the end of April - this may not include all pre-year-end liabilities invoiced post-year-end (as some might be invoiced in May)

34.125 Determining a sample size for non-statistical sampling requires the exercise of professional judgement, and more senior members of the engagement team should normally agree or be involved in setting sample sizes for non-statistical tests.

34.126 Non-statistical methods may only be used for low or medium assurance they cannot be used for high assurance where the testing would need to be supplemented by other substantive procedures such as an analytical procedure. In order to provide assurance over an assertion, the minimum sample size is:

- 30 items for medium assurance; or
- 15 items for low assurance.

34.127 If it is considered appropriate, given the nature of the balance and the associated risks, to set a lower sample size, the engagement team should clearly document the rationale for the sample size selected and how this provides an appropriate level of assurance over the balance.

34.128 Although the decision whether to use a statistical or non-statistical sampling approach is a matter of judgment, this should not be on the basis of the relative sample sizes. Lower sample sizes will usually be appropriate if the engagement team are only seeking case study information, rather than assurance over a balance.

Sampling methods –cut-off testing

34.129 Assessment of cut-off is a matter of judgement. Occurrence and completeness tests of the same class of transactions will give some assurance over cut-off. Where error is identified, teams should reconfirm the appropriateness of the population sampled with the audited entity.

34.130 When considering the risk to the cut-off assertion inherent in the population, the auditor should consider the risks associated with the entity's business practices and business cycle. Consider the income/ expenditure profile, the control environment and any changes made to it in year, management incentive to manipulate income/ expenditure and any new projects undertaken that may be misclassified. Where risks are higher, or an error is identified the engagement team may choose to extend testing or undertake specific testing to reduce the risk to this assertion.

34.131 Additional risks to the cut-off assertion for income include:

- long payment terms;
- management incentive to manipulate income;
- complex transactions or accounting policies giving rise to significant judgement; and/or
- poor controls over income recognition.

34.132 The cut off period should reflect the business process of the audited entity. Usually, the cut-off period covers the fortnight before and after the cut-off date (i.e., the financial year end), but this can be extended to a month prior and post year end. This is a judgement for the engagement team to make and document on file.

34.133 Samples should be selected randomly as this allows for a statistical evaluation of any errors. However, teams can elect to select the sample judgementally; however, the engagement team cannot extrapolate any error as judgemental sampling is non-statistical. This is a judgement the engagement team should make carefully, and judgemental criteria should be clearly documented on the audit file.

34.134 All material items should be tested. The remaining cut-off population for pre and post year end is split into two strata: high value and low value, which is based on the individual items in the population being greater than or less than performance materiality.

34.135 Where there is no controls assurance, samples should be selected in line with the sample frame in ***Figure 34M-a*** below.

Figure 34M-a: Cut-off sample testing – no controls assurance

Level of assurance	Low[7]	Medium	High
Material items	All	All	All
High value (i.e., all individual items with value greater than performance materiality)	3 pre-year end 3 post-year end	4 pre-year end 4 post-year end	5 pre-year end 5 post-year end
Low value (all individual items with value less than performance materiality)	1 pre-year end 1 post-year end	1 pre-year end 1 post-year end	2 pre-year end 2 post-year end
Overall total sample size (excluding material items)	8	10	14

34.136 If there is controls assurance over the cut-off assertion for the relevant COTABD, then the substantive element will be reduced, as the purpose of the substantive sample will be to support the assurance obtained via the controls assurance with the focus solely on higher value items per Figure 34M-b below.

Figure 34M-b: Cut-off sample testing – with controls assurance

Level of assurance	Low[8]	Medium	High
Material items	All	All	All
High value (i.e., all individual items with value greater than performance materiality)	1 pre-year end 1 post-year end	2 pre-year end 2 post-year end	3 pre-year end 3 post-year end
Overall total sample size (excluding material items)	2	4	6

34.137 Errors should be evaluated in line with the method selected: i.e., statistical or non-statistical.

Sampling methods – non-statistical sampling – evaluating non-statistical sampling

34.138 In non-statistical sampling, the errors identified cannot be used to statistically represent the remainder of the population. Our documentation and communication with management and those

[7] Low assurance: if the population is immaterial, then select 2 pre-year end and 2 post-year end samples from the population as a whole – there is no need to split between high and low value.
[8] Low assurance: if the population is immaterial, then select 2 pre-year end and 2 post-year end samples from the population as a whole – there is no need to split between high and low value.

charged with governance should be clear, so that inferences from the errors found do not mislead readers into thinking that they are statistically valid extrapolations.

34.139 Although non-statistical sampling provides less persuasive evidence than statistical sampling, it can still provide sufficient appropriate audit evidence over a risk of material misstatement.

34.140 If the engagement team have identified any errors, the assessment of whether the planned level of assurance has been achieved will require professional judgement. From the discussion with management, the engagement team should assess whether the misstatement identified is an isolated or a systematic occurrence. Where the engagement team have considered that further work is required, this should reflect the nature of misstatements identified.

34.141 Depending upon the circumstances and the nature and cause of the identified errors, this may involve:

- identifying other items with the same characteristics to quantify the error more precisely;
- applying the error rate identified to the recorded amount;
- applying the error identified to the population used as the sample source (where appropriate information about its characteristics is available);
- where testing completeness through a non-statistical sample:
    - extending the scope of population;
    - extending the sample size;
    - focusing the testing on a population where misstatements were identified; and/or
    - considering implications from the review of board minutes; and/or
- performing a review of significant balances within the source population.

34.142 The impact on the audit should be evaluated, specifically indications of weaknesses in internal controls and misstatements in other audit areas. Where engagement teams have identified misstatements and evaluated whether additional procedures are required, they should clearly document the rationale for their conclusion on the adequacy of the scope of work performed.

Sampling methods – non-statistical sampling – use of non-statistical sampling for purposes other than obtaining assurance

34.143 If non-statistical sampling is being used for case-study or illustrative purposes, then the engagement team should:

- pick a sample size considered appropriate to provide useful examples;
- select items for testing and perform the planned tests subject to similar considerations to those discussed above; and
- evaluate the results of the work performed.

34.144 The evaluation of results will generally be qualitative in nature. Judgement must, therefore, be applied in evaluating whether the planned level of assurance has been achieved when non-statistical sampling is used, and more senior members of the engagement team would typically be involved in agreeing the sample design and evaluating its results. In particular, the Engagement Manager (and for riskier items, the Engagement Director) would ordinarily decide at the planning phase:

- the appropriate basis for setting the sample size;
- the sample source that will be used in testing; and
- any criteria to be used in sample selection.

34.145 Any decision to use non-statistical sampling to test items where sufficient information is available to use a statistical sampling approach should be approved by the Engagement Director.

Sample testing of items with tolerable estimation uncertainty

34.146 A sample test of detail approach may be applied to items that are individually accounting estimates, meaning a level of estimation uncertainty is expected. For example, the valuation of individual derivatives may be sample tested and the audit value of each item may be different from the book value due to instances of rounding and small fluctuations.

34.147 When testing a population of accounting estimates using a sample test of detail, the engagement team should calculate a tolerable difference to determine whether the variances between book value and audit value are unexpected.

34.148 Tolerable difference for these purposes is set in relation to the following factors:

- the sensitivity of the data;
- the materiality of the valuation;
- the Likelihood and Financial Statement Impact (magnitude) of the risk of material misstatement;
- the required level of assurance; and
- the quality of the instrument being tested.

34.149 The auditor should use these factors to determine a required precision. For example, where greater assurance is required, the precision should be higher and the tolerable difference tighter. The tolerable difference should be set in advance of the sample testing taking place. Tolerable differences should be set using the following thresholds as a percentage of book value:

- for a High level of assurance or when obtaining an independent market price for a security: 1%;
- for a Medium level of assurance: 2%; and
- for a Low level of assurance: 3%.

Sampling approach for contract reviews

34.150 In some situations, a sample test of contracts (or similar documents) is required to assess whether or not a method or requirements specified in the audited entity's financial reporting framework has been applied correctly. For example:

- whether a contract meets the definition of a lease under IFRS 16;
- whether a financial instrument has been correctly classified under IFRS 9; or
- whether performance obligations have been correctly identified and treated within a revenue contract under IFRS 15.

34.151 In these situations, an attribute sampling approach should be used, as described in ***Figure 34L*** above. However, a purely random approach may not be efficient in some situations: for example, where:

- standardised terms are used for many contracts and can therefore be viewed as key items; and/or
- the level of risk in the population is concentrated in a relatively small number of higher value or unusual contracts.

34.152 The contract review approach set out in this section addresses these issues, via a form of attribute sampling that adopts some of the principles of the five-stage approach. There are two approaches to select from:

- The Standard approach should be used for testing of new contracts or of contracts whose treatment is under review as a result of first-time adoption of a new accounting standard.

- The Review approach should be used where the engagement team is testing management's re-assessment of existing contracts (being accounted for under the same standard) using data brought forward from the prior year.

34.153 As set out in ***Table 34N*** below, under both approaches, the engagement team should test 100% of material and key and anomalous items. The table provides sample sizes for additional testing of the residual population under the respective approaches. The residual sample sizes are smaller under the Review approach than the Standard approach, because they combine to provide assurance over the reassessment exercise as a whole.

Table 34N: Contracts and leases sampling frame

	New contracts (standard approach)			Existing contracts (review approach)		
Material contracts	Test all			Test all		
Key and anomalous contracts	Test all			Test all		
	Low assurance	**Medium assurance**	**High assurance**	**Low assurance**	**Medium assurance**	**High assurance**
Targeted highest value contracts	3	5	5	3	5	5
Random residual contracts	5	15% (min 5 to max 15)	20% (min 5 to max 20)	5	7.5% (min 5 to max 10)	10% (min 5 to max 15)

Technical appendix – the probability of selecting an atypical sample

34.154 The main risk for the auditor to address is that there is material error present and that the audit fails to detect it. This would mean that the sample would be free of material error and therefore atypical. The NAO's sampling methodology considers the probability of such a situation occurring.

34.155 The auditor would be concerned if an error rate of a level that would breach materiality existed and were not detected.

34.156 As the proportion of errors increases, the chance of not finding them decreases.

34.157 Most NAO audits have very large populations in terms of the number of transactions. As the population size increases the risk increases.

34.158 As the population size tends to infinity the risk of an atypical sample tends to 5%, which is the audit risk that the NAO adopts. This is the origin of the NAO's 5% audit risk of not detecting a material error – where there is a 5% risk, 95% assurance needs to be achieved.

Technical appendix – confidence intervals and precision definitions

34.159 Confidence interval is used to express the degree of uncertainty associated with a sample statistic such as the estimate of the error value.

34.160 A confidence interval is an interval estimate combined with a probability statement. When calculating the error value based on a sample, the auditor uses the confidence level to describe the uncertainty associated with the estimate of the error value. If the confidence interval is 95%, this means that if the auditor used the same sampling method to select different samples and estimated the error value for each sample, the auditor would expect the true population parameter to fall within the interval estimates 95% of the time.

34.161 Confidence intervals indicate both the precision of the estimate and the uncertainty of the estimate. Precision refers to how close estimates from different samples are to each other. This measures the repeatability of the estimate. Precision is inversely related to standard error. The standard error is a measure of the variability of a statistic. It is an estimate of the standard deviation of a sampling distribution. When the standard error is small, sample estimates are more precise; when the standard error is large, sample estimates are less precise.

34.162 The confidence interval gives an indication of the precision of the sample mean as an estimate of the "true" population mean.

34.163 A sample with 10% precision and 95% confidence means that the estimate will be within 10 percentage points of the actual 95% of the time.

34.164 ***Table 34O*** below defines terms relating to confidence intervals and precision.

Table 34O: Definitions of terms relating to confidence intervals and precision

Term	Definition
Confidence interval	A range of values calculated from the sample that are believed, with a particular probability, to contain the true parameter value. A 95% confidence interval implies that if the estimation procedure were repeated then 95% of the calculated intervals would be expected to contain the true parameter value.
Confidence level	The certainty with which the estimate lies within the margin of error: the percentage of confidence intervals that contain the true parameter value.
Precision	A measurement of the accuracy of the sample estimate compared to the population value.
Standard deviation	A measure of the variability in a set of observations about their mean value: equal to the square root of the variance.
Standard error	A measure of the precision of a statistic used to estimate the population parameter. Also, the standard deviation of the sampling distribution of a statistic. For example, the standard error of the sample mean.

Technical appendix – the theory underpinning the assurance model

34.165 The NAO audits to 95% assurance. This assurance comes from three sources:

- inherent assurance (IA);
- controls assurance (CA); and
- substantive assurance (SA).

34.166 The formula from probability theory is:

$$IA \times CA \times SA$$

34.167 The model is more useable when additive:

$$IA + CA + SA$$

34.168 For a multiplicative model to become additive, logarithms are used and the assurance factor (AF) is calculated:

$$AF = -1\ln(1 - CL)$$

where:

- CL is the confidence level; and
- ln is the natural log:

34.169 For 95% confidence, or 5% risk, the AF equates to 3.0.

34.170 Assurance factors are not visible in the assurance model, but are built into the wording of the model (High, Medium and Low levels of assurance) and sample size determination to ensure that a minimum 5% precision is achieved.

34.171 Simple Random Sampling (SRS) sample sizes are given by the following formula

$$\frac{z^2 \times (p \times (1-p))}{\text{Required precision}^2}$$

where:

- z is the z score associated with the required assurance; and
- p is the proportion in the population in error.

34.172 ***Figure 34P*** in the following section illustrates how each sample size has been determined to achieve a minimum of 5% precision at the required confidence levels.

Technical appendix – precision around the sample sizes

34.173 The predetermined sample sizes have been selected with the following underlying assumptions:

- to ensure a minimum 5%: when the random and targeted testing is combined this is achieved in all cases:
  - Low substantive assurance is based on an equivalent assurance factor of 1.0 or 0.7 with low controls assurance and an error rate of 1% or below;
  - Medium substantive assurance is based on an equivalent assurance factor of 2.0 as a sole procedure or 0.7 as one of two procedures and an error rate of 2% or below or on an equivalent assurance factor of 2.0 as a sole procedure or 1.0 as one of two procedures and an error rate of 3% or below; and
  - High substantive assurance is based on an equivalent assurance factor of 3.0 as a sole procedure or 2.3 as one of two procedures and an error rate of 3% or below.

34.174 For precision to be calculated, the auditor requires the sample size, the assurance required and the rate of expected error in the population.

Chapter 35: Controls testing

Relevant standards and guidance

35.1 ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* deals with the auditor's responsibility to identify and assess the risks of material misstatement in the financial statements, which includes consideration of control risk and the entity's system of internal control.

35.2 Paragraphs 1-72 to 1-82 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 315 (Revised July 2020) in the public sector.

35.3 ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks* deals with the auditor's responsibility to design and implement responses to the risks of material misstatement identified and assessed by the auditor.

35.4 ISA (UK) 530 (Updated May 2022) *Audit sampling* applies when the auditor has decided to use audit sampling in performing audit procedures. It deals with the auditor's use of statistical and non-statistical sampling when designing and selecting the audit sample, performing tests of controls and tests of details, and evaluating the results from the sample.

35.5 Paragraphs 2-40 to 2-47 of Practice Note 10 (Revised 2022) provide guidance on designing and performing tests of the operating effectiveness of controls over regularity.

Background

35.6 The responsibility for preparing financial statements that are demonstrably 'true and fair' lies with the audited entity and specifically with their Accounting Officer/Board/Directors/Trustees as appropriate. An effective system of internal control contributes to providing assurance that the financial statements are 'true and fair' and ensures that the Accounting Officer/Board/Directors/Trustees can submit accounts that are robust enough to withstand an audit.

35.7 A robust control environment should prevent or detect and correct material misstatements in the financial statements. In accordance with the principles of Managing Public Money this includes:

- enforcing financial compliance across the organisation while guarding against fraud and delivering continuous improvement in financial control;
- applying strong internal controls in all areas of financial management, risk management and asset control
- establishing budgets, financial targets and performance indicators to help assess delivery;
- reporting performance of both the organisation and its ALBs to the board, HM Treasury and other parties as required;
- value management of long-term commercial contracts; and
- ensuring that the organisation's capital projects are chosen after appropriate value for money analysis and evaluation using the Green Book.

35.8 If the engagement team is able to obtain assurance over the operating effectiveness of appropriately designed and implemented controls, this reduces the extent of substantive procedures required. Testing the operating effectiveness of controls is also a required procedure in situations where substantive procedures alone cannot provide sufficient appropriate audit evidence at the

assertion level, as outlined in paragraph 8(b) of ISA (UK) 330 (Revised July 2017) (Updated May 2022). Controls tests, as defined in paragraph 4(b) of ISA (UK) 330 (Revised July 2017) (Updated May 2022), are audit procedures designed to evaluate the operating effectiveness of controls in preventing, or detecting and correcting, material misstatements at the assertion level.

35.9 Controls testing can be the most effective way to obtain sufficient appropriate audit evidence regarding the assessed risks of material misstatement. Controls are never completely infallible and hence engagement teams are always required to perform an appropriate amount of substantive testing in addition to tests of controls, to support the opinion on financial statements.

35.10 Although the engagement team is not responsible for the system of internal control, they are able to play a valuable role in recommending improvements which may assist management in rectifying deficiencies in the system of internal control identified through our tests or from comparison with other entities. As defined in paragraph 6(a) of ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management*, a deficiency in internal control exists when a control is designed, implemented or operated in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements on a timely basis; or a control necessary to prevent, or detect and correct, misstatements in the financial statements on a timely basis is missing.

35.11 Controls testing enables the engagement team to reduce the scope and extent of substantive procedures. It is therefore important that engagement teams are clear on how the identified controls that are also being tested provide assurance over each related risk of material misstatement, and that they have appropriate evidence to support their conclusion that the control would prevent or detect and correct a material misstatement.

35.12 “Internal control” is the process designed, implemented and maintained by those charged with governance, management and other personnel to provide reasonable assurance about the achievement of an entity's objectives with regard to reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

35.13 The term "controls" refers to any aspect of one or more of the components of internal control.

Types of control

35.14 Controls may be classified as:

- preventative controls, which aim to prevent misstatements arising; or
- detective controls, which aim to identify misstatements and correct them.

35.15 Controls may also be classified as:

- transaction level controls, which operate around the initiation and processing of transactions; or
- monitoring controls, which operate by considering, for example, reports of results, or by monitoring that transactional level controls have operated as expected.

35.16 Monitoring controls are generally detective in nature, and transactional controls are generally preventative in nature.

35.17 Where there are multiple controls which address a control objective or risk, the engagement team would normally evaluate detective or monitoring controls in preference to preventative or transactional controls, provided that they address the control objective or risk with sufficient precision

to detect and correct a material misstatement. A preventative control may only provide assurance at one point of the process and may not cover all relevant stages in that control process.

35.18 Examples of types of control include:

- Management's monitoring controls, such as a regular critical review of management accounts against an appropriately detailed budget, risk-based reviews of operations by management, the use of directors' statements on the state of their risks/controls and other performance data. NAO engagement teams are not permitted to place reliance on the operating effectiveness of budgetary controls.
- Organisational controls, which derive from the way in which the organisation is structured and can be both detective and preventive. They will normally include well-defined responsibilities and the segregation of incompatible functions such as the initiation, processing and recording of transactions.
- Authorisation controls, which will normally operate at the individual transaction level and will be preventative in nature. Their purpose will be to stop a transaction being processed if it has not been approved at an appropriate level. Good authorisation controls will be specific about who can approve what, the extent of checking required before approval and how the check should be evidenced.
- Operational controls, which are concerned with the completeness and accuracy of processing and may be either preventive or detective. They may include comparison of one set of documents to another, such as purchase orders to invoices, and the use of control totals and reconciliations.
- Physical controls, which are usually designed to be preventative and include controls over access to assets and accounting records through simple physical measures such as passes and safes but also logical controls such as password access to computer files.

35.19 Further examples of the types of controls that would be expected in respect of particular risks are set out below.

- Transactions governed by complex regulations: mitigating controls might be based on the use of procedural manuals (that are updated regularly) and management re-performance or review of transactions to check compliance.
- Functions carried out at a number of different locations: mitigating controls could address risks of weakened management control or of inconsistencies between the locations. Controls might include budgets and outturn comparisons within each location and between locations and checks to ensure that procedural manuals and supervisory arrangements are followed.
- Transactions based on claims or certificates from external parties: mitigating controls could include established criteria for claims, standard requirements for evidence to support claims and independent verification.
- Transactions not in the normal course of business: mitigating controls might be the production of exception reports and documented follow-up actions, and senior management/board authorisation
- Accounting estimates: mitigating controls might include management or independent reviews of the basis of the estimates and checks on supporting documentation.
- Period-end adjustments: it is possible to introduce a material error with an accounting adjustment, even though the control procedures have operated effectively up to that point. Mitigating controls might include detailed checking and management review of supporting documentation for accounting adjustments.

Planning procedures around the control environment

35.20 As part of their risk assessment procedures, the engagement team should obtain an understanding of internal control relevant to the audit (see Chapter 15: Gathering entity initial information).

35.21 The NAO interprets paragraph 26 of ISA (UK) 315 (Revised July 2020) as requiring the engagement team to evaluate the design and implementation of the following controls:

- At least one control that addresses each RoMM that has either one or both of a final Financial Statement Impact (magnitude) placement or a final Likelihood placement of High (i.e., effectively the initial assessment of the RoMM will end up in an inherent risk position of a rebuttable significant risk or higher)). Where the audited entity operates more than one control that addresses such a RoMM, the engagement team is only required to evaluate the design and implementation of one of these controls. However, if the engagement team concludes that the control which has been initially evaluated is not adequately designed and implemented (using the criteria specified in the 'Design and implementation of controls' section later in this Chapter), they should evaluate the design and implementation of an alternative control that addresses the same RoMM, continuing until either:
    - an adequately designed and implemented control is identified which addresses that RoMM; or
    - having evaluated the design and implementation of all controls operated by the audited entity which purport to address that RoMM, the engagement team concludes that none of these controls are adequately designed and implemented to address that RoMM.
- Controls that address significant risks relating to regularity.
- Controls surrounding journal entries.
- Controls relating to the reconciliation of the trial balance to the general ledger.
- Complementary user entity controls where controls assurance is being obtained from controls operated by a service organisation.
- Controls which the auditor plans to test the operating effectiveness of in order to obtain controls assurance.

35.22 NAO policy additionally requires engagement teams in all audits to evaluate the design and implementation of the following controls as "other controls that the auditor considers is appropriate to enable the auditor to meet the objectives of paragraph 13 [of ISA (UK) 315 (Revised July 2020)] with respect to risks at the assertion level, based on the auditor's professional judgment", for the purpose of paragraphs 26(a)(iv) and 26(d) of ISA (UK) 315 (Revised July 2020):

- management's monitoring controls over financial data;
- controls around the financial close process, including the preparation of the Governance Statement, Annual Report and financial statements;
- controls surrounding the selection and application of accounting policies; and
- controls over risks of material irregular transactions.

35.23 At the audit assertion level, the engagement team should ensure that the proposed audit procedures are responsive to the assessed risks of material misstatement or material irregular transactions. In designing the audit procedures, including deciding whether to rely upon the operating effectiveness of controls, the engagement team should consider:

- the significance of each risk;
- the likelihood that a material misstatement or material irregularity will occur;
- the characteristics of the transactions and balances; and
- the nature of the specific internal controls (in particular, whether they are manual, IT dependent or automated).

35.24 Management's monitoring controls usually take the form of management's review of management accounts, however other controls may be more appropriate in some entities such as grant giving bodies where they may, for example, monitor total grants given against a profile set against budgets. NAO engagement teams are not permitted to place reliance on the operating effectiveness of budgetary controls.

35.25 An effective control environment may allow the engagement team to place more reliance on internal controls and upon the reliability of audit evidence generated within the entity itself.

35.26 If there are weaknesses in the control environment that management cannot overcome, the engagement team should consider the most effective and efficient alternatives. Paragraph A2 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) suggests that the auditor may respond to an ineffective control environment by:

- conducting more audit procedures as of the period end rather than at an interim date;
- obtaining more extensive audit evidence from substantive procedures (which could include, for example, using the work of internal audit or carrying out a substantive analytical procedure that is predictive in nature); and/or
- increasing the number of locations to be included in the audit scope.

35.27 As stated in paragraph A3 of ISA (UK) 330 (Revised July 2017) (Updated May 2022), deficiencies in the control environment have a significant bearing on the auditor's general approach, including whether the auditor adopts a substantive approach. In light of these considerations, if there are significant deficiencies in any of the audited entity's indirect components of the system of internal control assessed as part of the risk assessment process, then it would not be appropriate for the engagement team to place reliance on controls.

35.28 The process of understanding the entity's internal control and planning where to form an expectation of effective operation of controls may be an iterative process, with the engagement team's conclusions about the wider control environment leading them to re-evaluate their approach to controls. For example:

- The engagement team planned to rely on controls over accruals and evaluated their design and implementation. However, they concluded that weaknesses in indirect components of the system of internal control indicated that they should not plan to rely on any controls in this organisation.
- The engagement team may have planned to test a significant risk substantively, evaluated the design and implementation of relevant controls and determined that they were adequately designed to prevent or detect material misstatement so decided to plan to rely on their operating effectiveness.
- The engagement team may not initially plan to rely on controls to test expenditure, but from our general understanding of the entity's internal control may determine it would be appropriate to do so. They evaluated the design and implementation of expenditure controls before going on to test their operating effectiveness, in addition to performing equivalent work on the supporting relevant general IT controls.

Design and implementation of controls

35.29 A control is appropriately designed if, possibly in combination with other controls which have been assessed, it is capable of either preventing or detecting and correcting material misstatements effectively.

35.30 A control is appropriately implemented if it exists and it is being used by the entity in the manner it was designed to be used to prevent or detect and correct material misstatements (this should include consideration across all risks of material misstatement that the engagement team are seeking to obtain assurance over).

35.31 Where engagement teams are planning to rely on the operating effectiveness of a control operated by the entity, they should carry out the following steps:

- RoMM mapping:
    - assess which risks of material misstatement are covered by the controls.
- Design:
    - for each control, document characteristics of the control including:
        - if a manual control, persons who perform each component of the control (and who performs it in their absence) and whether these persons have sufficient competence, expertise and authority;
        - different ways the control operates;
        - whether the control is reliant upon segregation of duties controls or review;
        - whether the control is preventative or detective;
        - whether the control is IT dependent or is semi/fully automated and if so whether configured or programmed and whether IT audit consultation is required;
        - whether the control is dependent on any non-IT dependent controls;
        - whether, if the control relies on a review, this review is sufficiently precise;
        - the frequency of operation of the control; and
        - whether the control is reliant on any system-generated reports or other information that the engagement team will need to assess;
    - conclude whether the controls, whether considered either in isolation or collectively, are designed appropriately to prevent or detect and correct material misstatement and/or material irregular transactions; and
    - if they are not, assess whether the deficiencies in control design are significant deficiencies and consider the implications for the audit.
- Implementation:
    - for each control, carry out an initial assessment of:
        - whether there are any instances where the control activity operated in a way other than how it was expected to operate;
        - whether there have been any modifications to the control during the reporting period;
        - whether there have been any known issues (including misstatements, irregular transactions or unusual items) that the control failed to prevent, or detect and correct; and
        - based on the above answers, whether it is appropriate to continue assessing implementation through a walkthrough;
    - for each control that has passed the initial assessment:
        - walk through one instance of the control, ideally as it is being performed, observing and obtaining evidence such as emails and full screen captures with dates, and software application included, and clearly highlighting and documenting where that evidence demonstrates the expected characteristics of effective operation of the control;
        - conclude whether the control is implemented in line with the engagement team's understanding of its design;
        - if the implemented operation differs to the auditors understanding of the design, conclude whether the control would remain effective when operated in this manner and update design documentation; and
        - if any weaknesses have been identified in the implementation of the control, document whether there are any compensating controls that mitigate these weaknesses;
    - conclude whether the controls, when considered either in isolation or collectively, are implemented appropriately to prevent or detect and correct material misstatement and/or material irregular transactions;

- if they are, conclude whether testing of these controls would be practical and provide an appropriate approach to gain assurance over their effectiveness; and
- if they are not assess whether the deficiencies in controls are significant deficiencies and consider the implications for the audit.

35.32 Separate steps for assessing the design and implementation of controls operated by a service organisation are set out in Chapter 46: Service organisations and shared service centres.

35.33 In accordance with paragraph 10(b) of ISA (UK) 330 (Revised July 2017) (Updated May 2022), the engagement team should determine whether the control is dependent upon other controls (indirect controls), and if so, whether it is necessary to obtain audit evidence that the indirect controls are appropriately designed and implemented and then test their operating effectiveness. Where controls upon which engagement teams plan to rely are dependent upon general IT controls (for example, access and change controls), they should consider the procedures they need to perform over general IT controls.

35.34 If the control is adequately designed and implemented, engagement teams may continue with the planned approach of testing its operating effectiveness.

35.35 Depending upon the reasons, if the control is not adequately designed and or implemented, the engagement team may conclude that assurance is needed over the operation of a complementary or alternative control to achieve assurance over the risk of material misstatement, in which case engagement teams should evaluate the design and implementation of the other control as well. Alternatively, engagement teams may conclude that a controls approach is inappropriate to testing that risk of material misstatement.

35.36 If the team concludes that a control is not designed or implemented appropriately, the team should consider reporting to management and those charged with governance a significant deficiency in internal control (see Chapter 57: Reporting to those charged with governance).

35.37 If controls are identified which are not adequately designed or implemented, including where a control that the engagement team would expect is absent, engagement teams should consider whether this has an impact upon the assessment of control risk within the Risk Assessment in Apex. The engagement team should also consider reporting the control deficiency to management and/or those charged with governance.

35.38 If the entity has used substantially different controls at different points in the period, the engagement team should evaluate each of them separately if they are seeking to rely on the operating effectiveness of controls throughout the period.

35.39 The implementation of controls may be evaluated through similar types of procedures to tests of the operating effectiveness of controls, or through walkthroughs. Engagement teams may decide that the walkthrough counts as one of the required tests of controls during the period. Where engagement teams use the walkthrough as one of their required tests of controls, they should clearly document this. The types of procedures used to evaluate the implementation of the controls may include:

- inquiry of entity personnel (coupled with other procedures);
- walkthroughs;
- observing the operation of a specific control; and/or
- inspecting documents and reports.

35.40 Walkthroughs involve following one or more transactions through the accounting system and its controls to confirm the engagement team's understanding of the controls, to help them document the accounting process and provide an indication of how the controls operate in practice: i.e. whether they are implemented as designed to prevent or detect and correct a material misstatement.

35.41 If the engagement team evaluates the design and implementation of controls over purchasing and identifies that there is no segregation of duties between creating suppliers on the system, inputting orders and processing payments, they should:

- conclude that the controls are not appropriately designed to prevent, or detect and correct, material misstatement or material irregular transactions; and
- assess whether the deficiencies in controls are significant deficiencies and consider the implications for the audit, which should include:
    - revisiting the assessment of risks of material misstatement and control risk within the Risk Assessment in Apex (and, if appropriate, the risks of material irregular transactions in the Regularity Risk Assessment);
    - considering whether there is a need to re-visit the Engagement Team Discussion on Risk and Fraud and the identification and assessment of the risks of material misstatement due to fraud carried out in accordance with ISA (UK) 240 (Revised May 2021) (Updated May 2022); and
    - communicating in writing any significant deficiencies in internal control to those charged with governance in accordance with ISA (UK) 265 (Updated May 2022).

Operating effectiveness testing of controls

35.42 Paragraphs 8 to 15 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) and the related application guidance set out how the engagement team should design and perform tests of controls to obtain sufficient appropriate audit evidence as to the operating effectiveness of identified controls, including controls over significant risks; these paragraphs cover the nature, timing and extent of those tests of controls and the use of audit evidence obtained during an interim period or in previous audits.

35.43 Where engagement teams are planning to rely on controls that address significant risks, they should obtain more persuasive evidence (in accordance with paragraph 9 of ISA (UK) 330 (Revised July 2017) (Updated May 2022)) by varying the nature, timing and extent of their procedures.

35.44 ***Figure 35A*** below shows how audit assurance is built up when using tests of controls.

Figure 35A: Possible build up of audit assurance when using tests of controls

Level of inherent risk is Significant – Assurance from controls testing, SAP and test of detail

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Medium	SAP (Low)
			Test of detail (required under paragraph 21 of ISA (UK) 330 (Revised July 2017))
			Total: Low

or

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Low	SAP (Low)
			Test of detail (Low)
			Total: Medium

Level of inherent risk is Significant – Assurance from controls testing and test of detail

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Medium	Test of detail (Low)
			Total: Low

or

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Significant	None	Low	Test of detail (Medium)
			Total: Medium

Level of inherent risk is Medium – Assurance from controls testing only

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Medium	Low	Medium	None

Level of inherent risk is Medium – Assurance from controls testing and SAP

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Medium	Low	Low	Test of detail (Low)
			Total: Low

Level of inherent risk is Medium – Assurance from controls testing and test of detail

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Medium	Low	Low	Test of detail (Low)
			Test of detail (Low)

Level of inherent risk is Low – Assurance from controls only

Inherent risk	Inherent assurance	Controls assurance	Substantive assurance
Low	Medium	Low	None

35.45 As demonstrated in ***Figure 35A*** above, significant risks can be addressed through one of the following approaches (noting that substantive procedures to address a significant risk must include a test of detail):

- obtaining a Medium level of controls assurance and designing and performing substantive procedures to provide a Low level of assurance, either through a test of detail or a test of detail and a SAP;
- obtaining a Low level of controls assurance and designing and performing substantive procedures to provide a Medium level of assurance, either through a test of detail or a test of detail and a SAP; or
- not obtaining controls assurance and designing and performing substantive procedures to provide a High level of assurance: this may be through substantive procedures individually providing a High level of assurance, or else through combining a substantive procedure providing a Medium level of assurance with another substantive procedure providing a Low level of assurance.

35.46 Engagement teams should only test the operating effectiveness of controls that are suitably designed to prevent, or detect and correct, a material misstatement in the financial statements – this should not include budgetary controls, as NAO engagement teams are not permitted to place reliance on the operating effectiveness of such controls. If the entity has used substantially different controls at different times during the period under audit, each of these should be considered separately.

35.47 A test of operating effectiveness of controls consists of a combination of inquiry and other audit procedures as set out in paragraph 10(a) of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

35.48 In testing the operating effectiveness of the controls, the engagement team should:

- calculate the required sample size for the control test using ***Table 35B*** below;
- select instances of the control to test;
- perform the planned procedures to test the selected instances; and
- evaluate and conclude upon whether the control has been performed as expected in each instance, or whether there were deviations from adequate performance of the control.

Table 35B: Sample sizes for controls testing

Expected number of failures in sample	**0 failures**		**1 failure**	
Controls assurance required	**Low**	**Medium**	**Low**	**Medium**
Frequency of control activity				
Annual	1*	1*		
Quarterly	2*	2*		
Monthly	3*	5*		
Weekly	5*	10*		
Daily	15	20		
Many times a day – batch controls	20	30	45	60
Many times a day – transactional controls	20	35	50	65
Demand-led controls *(instances of where a control is operated throughout the period and usually in response to a triggering event)*	5% (minimum 5 to maximum 15)	10% (minimum 15 to maximum 30)	20% (minimum 15 to maximum 30)	25% (minimum 30 to maximum 60)
Automated	1	1		

For items marked with an asterisk (*), one of the controls tested must include the control's operation at the year-end.

35.49 A control failure is defined as an instance where the control has not operated in accordance with its design in a manner which may result in a misstatement or irregularity in the financial statements.

35.50 A control deviation is defined as an instance where the control has not operated in accordance with its design. This may or may not lead to a misstatement or irregularity in the financial statements, depending on whether compensating controls are in place to mitigate the risk caused by the control deviation.

35.51 If there have been significant changes in the controls after testing has been performed, the engagement team should:

- evaluate the design and implementation of the new control and test its operating effectiveness; and
- not take controls assurance for the remainder of the year, and either:
    - attempt to perform a substantive procedure such as a substantive analytical procedure that is predictive in nature; or
    - increase the extent of their substantive procedures on transactions in the stub period to the year-end.

35.52 No control system can guarantee proper administration and the completeness and accuracy of transactions. All audit evidence cannot therefore be obtained solely from controls. In evaluating and testing controls, the engagement team should be aware of these limitations and the factors that may diminish the effectiveness of control systems, such as:

- the precision with which the control may be expected to operate: i.e. if comparing to a budget, how much volatility would be expected anyway, and so how small a misstatement may be identified;
- the potential for controls to be overridden by those responsible for them;
- improper application of controls due to human error as a result of mistaken judgement or interpretation, carelessness or distraction;
- the inability of standardised control systems to deal with non-routine transactions; and
- control breakdown due to changes in processing transactions and the development of non-standard procedures.

35.53 Inquiry alone is not sufficient to provide evidence of the operating effectiveness of controls. The nature of the procedures performed will depend upon the nature of the control. For example, if operating effectiveness is evidenced by documentation, the engagement team may inspect it to obtain audit evidence about operating effectiveness. For other controls, documentation may not be available or relevant, such as segregation of duties or control activities performed by the IT system. The engagement team may obtain evidence about these controls through procedures such as observation, inspection or the use of data analysis to look at whole populations.

35.54 The engagement team will also have identified what characteristics would indicate adequate performance of the control, and what conditions would indicate deviations from adequate performance of the control or a failure.

35.55 Tests of the operating effectiveness of controls are more extensive than the procedures performed in evaluating their implementation, although this will involve similar types of procedures.

35.56 The Engagement Director may therefore decide as part of establishing the overall audit strategy that it is efficient to test the operating effectiveness of controls at the same time as evaluating their design and determining that they have been implemented.

35.57 Alternatively, the engagement team may plan to test controls alongside substantive tests on the same transactions. Although the purpose of a test of controls is different from the purpose of a test of detail, both may be accomplished concurrently by performing a test of controls and a test of detail on the same transaction, also known as a dual-purpose test.

35.58 A dual-purpose test is designed and evaluated by considering each purpose of the test separately. The documentation in the audit file should be clear as to which elements of testing are used for which tests.

35.59 The engagement team may perform controls tests during and or at the end of the period being audited. Some tests of controls can be best performed after a period end, such as controls over year-end provisions.

35.60 If controls testing is conducted before the period end, it can identify significant matters at an early stage so that they may be resolved before the year-end, this is however a matter of judgement. Bank reconciliations are an example of where testing the controls in-year provides little assurance over the year end cash balance but by testing an in-year instance, can provide an indication as to whether the control will be effective at the year-end.

35.61 In practice, the engagement team typically will use tests of controls to provide assurance over both the performance statement and the statement of financial position, testing throughout the period, including at the year-end. As such, it is possible that a single test of controls may provide assurance over multiple risks of material misstatement.

35.62 As discussed in Chapter 47: Interim audit procedures, including hard close audits, if the operating effectiveness of controls is tested during an interim period, at the year-end the engagement team should obtain audit evidence about significant changes to those controls subsequent to the interim period.

35.63 Depending upon the circumstances, the engagement team may obtain evidence about whether or not controls have changed significantly through one or more of:

- inquiry of management;
- walking through a transaction to check that the controls are still implemented in line with the engagement team's understanding;
- examining process manuals or other documentation; and/or
- other procedures appropriate to the control being tested.

35.64 The assessment of the nature and extent of the procedures required to obtain additional evidence should take account of the significance of the identified risks at the assertion level, the degree of assurance obtained to date, the nature of the control and the length of the remaining period.

35.65 The approach to testing the stub period should be agreed with the Engagement Director. This will usually be done when the Engagement Director approves the audit plan.

35.66 In most cases, the engagement team will need to extend the controls testing to cover the entire period or confirm that the control remained in place and review the entity's monitoring of that control over the remaining period.

35.67 If the engagement team plans to test controls for the stub period, the controls sample will be split between the interim period and the stub period. For example, if a daily control is being tested to obtain a Low level of assurance at Period 9, 11 items might be tested at interim and 4 items from the stub period at the year-end to achieve the total required sample size of 15 items.

35.68 If it is appropriate to use evidence obtained on the operating effectiveness of controls from prior periods, the engagement team should enquire whether there have been any changes to the control (including supporting general IT controls), document the design of the control and confirm it is still implemented as expected through observation or inspection of the control (for example, performing a walkthrough). This will be sufficient appropriate work to rely on evidence obtained in prior periods relating to the operating effectiveness of the controls in question in accordance with paragraph 14 of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

35.69 For each key control, engagement teams should consider whether it is appropriate to use evidence obtained on the operating effectiveness of controls from prior period. Teams should consider:

- the effectiveness of other elements of internal control and evidence from prior periods;
- the risks arising from characteristics of the control including authorisation thresholds and the effectiveness of general IT controls if automated controls the engagement team are testing are dependent upon them;
- the effectiveness of the control, including the nature and extent of deviations in the application of the control noted in previous audits and whether there have been personnel changes that significantly affect the application of the control;
- whether the audited entity or business circumstances have changed sufficiently that the engagement team would expect the control also to have changed; and
- the risks of material misstatement and the extent of reliance on the control: for example, whether the control is over a significant risk or is a single failure likely to cause a material misstatement – if the answer to either of these is yes, it is not appropriate to use evidence from prior periods.

35.70 It is not appropriate to use evidence from a prior audit for controls over significant risks or controls where one failure would cause a material misstatement due to the increased audit risk associated with them.

35.71 In determining the extent of tests of controls, engagement teams should also consider:

- the frequency of the control;
- the level of assurance expected from the test;
- the expected rate of deviation from a control;
- the relevance and reliability of the audit evidence to be obtained regarding the operating effectiveness of the control at the assertion level;
- the length of time during the period that the engagement team are relying on the operating effectiveness of the control (typically, this will be the full period);
- the extent to which audit evidence is obtained from tests of other controls related to the risk of material misstatement (typically, engagement teams will only need to test one control to obtain assurance over a risk of material misstatement); and
- whether a control deviation would be expected in the operation of the control; and whether the control relates to individual transactions or batches of transactions/transactions within a particular period.

35.72 If the engagement team is only relying upon the operation of a control for part of the year, the sample sizes should be reduced on a pro-rata basis.

35.73 If the engagement team plans to take assurance from the operation of a control, it would not normally be expected that there will be any deviations in its operation. However, for controls which operate many times a day, the engagement team may plan to accept a certain level of control failure.

35.74 Control deviations in themselves may not necessarily lead to a misstatement or irregular transaction in the financial statements. Engagement teams therefore need to evaluate any deviations identified to consider their impact on the financial statements and/or the regularity of transactions. Where engagement teams consider that a control deviation has led to a misstatement or irregular transaction in the financial statements, then it would constitute a control failure.

35.75 Where a small number of control failures are expected, engagement teams should plan to test a larger sample of items to obtain assurance that the control is operating sufficiently reliably to provide assurance over the relevant risks of material misstatement despite the control failures.

35.76 Some controls are operated on a divisional basis within the audited entity. This might include monitoring controls such as payroll headcount controls or variance analysis of management accounts. When deciding how many divisions to test, and how many times the control should be tested for each division, engagement teams should use their professional judgment. Not all divisions necessarily need to be tested in order to provide controls assurance.

35.77 When determining the appropriate coverage, teams should consider factors such as whether the divisions all have similar risk profiles in relation to controls, and the relative size of each division. Teams may consult FAPQ on their proposed approach if unsure whether the extent of planned controls testing is adequate.

35.78 For tests of controls, the nature of the “sampling units” that are being picked between will vary depending upon the nature of the control and the detail of how it operates. For example, if testing a control based upon month-end reconciliation reviews, the sampling unit may be months (if there is a single review carried out of a file of reconciliations) or may be individual reconciliations (if many different individuals prepare and review particular reconciliations at different stages in the month-end process).

35.79 Depending upon the details of the control, this may increase how frequently the control has operated during the year and so the required extent of testing.

35.80 If engagement teams are unable to find a selected reconciliation to see whether it has been prepared, or are unable to obtain evidence that it was prepared and reviewed on a timely basis, this should be treated as a failure in the operation of the control.

35.81 Evidence of the operating effectiveness of controls may be obtained in a number of ways, depending on the nature of the control that is being tested. These would ordinarily use some combination of the following techniques:

- Observation and enquiry: watching what people do, how they do it and asking questions. It is unlikely that the engagement team will be able to cover the entire period with this technique, so it will not usually provide sufficient evidence on its own for manual controls. In addition, individuals may perform controls differently when observed than at other times.

- Examination: reviewing documentary evidence of how controls have operated at other times: for example, showing that transactions have been properly authorised, or records of management reviews. This will give more assurance about the continuous operation of controls. Examination may include walkthroughs or re-performing the control.
- Re-performance: where a control operates over individual transactions, it will usually be necessary to examine a sample that was subject to the control to check that the control has been applied.

35.82 Engagement teams may rely on the operating effectiveness of controls over regularity in the same way as from tests of controls addressing risks of material misstatements supporting the opinion on financial statements.

35.83 When engagement teams are planning to rely on a control which provides assurance over multiple risks of material misstatement, they should consider carefully whether this will provide assurance on the regularity opinion.

IT controls

35.84 Information Technology (IT) controls should be considered as an integral part of the financial audit as it will be rare that audited entities will have an accounting system or prepare financial statements with processes that do not rely on controls. It is important that all members of the engagement team understand IT concepts, appreciate the technical risks and are able to understand the impact of unmanaged IT risk on the business and to the audit opinion.

35.85 Most public sector organisations make extensive use of IT to process financial transactions and to produce their financial statements. These systems should also be considered when engagement teams are planning the tests of the operating effectiveness of internal controls, in addition to meeting the requirements of ISA (UK) 315 etc.

35.86 The engagement team should carry out the evaluation of the design and implementation of controls described in paragraph 26(d) of ISA (UK) 315 (Revised July 2020) for identified general IT controls where all of the following circumstances apply, in which case the relevant general IT controls are considered to be controls addressing risks arising from the use of IT as defined in paragraph 26(c)(ii):

- the engagement team is required to evaluate the design and implementation of a control;
- the control is automated, semi-automated or manual but IT-dependent; and
- there are risks arising from IT which affect the operation of the control.

35.87 Where engagement teams are planning to test the operating effectiveness of automated (application) controls, they should assess the design and implementation as well as operating effectiveness of general IT controls (such as those over access and change to systems and programs), which are indirect controls for the purpose of paragraph 10(b) of ISA (UK) 330 (Revised July 2017) (Updated May 2022).

35.88 For IT dependent manual controls, it may be possible to obtain assurance through reconciliations of inputs to source populations and systems or two-way testing as an alternative to performing design and implementation and operating effectiveness work over IT general controls.

35.89 ***Consultation required*** Where it is necessary to test general IT controls, the engagement team should determine which general IT controls to test to obtain the required assurance. This should reflect the risks that the IT system presents to the effective operation of the business controls which the engagement team plan to rely on in support of the production of the financial statements.

The rationale for the approach adopted should be clearly documented and the team must consult with the Digital Financial Audit team in doing so.

35.90 Due to the inherent consistency of IT processing, it will usually only be necessary to test a single instance of the operation of an automated and in some instances, a semi-automated application control.

35.91 Where engagement teams plan to test the operating effectiveness of a user review of exception reports detailing sales in excess of authorised credit limits, the user review and related follow up is the control that is directly being tested. Controls over the accuracy of the information in the reports, including the general IT-controls over the system and data feeding the report, are described as "indirect" controls. The fact that the exception reports are reliant upon both accurate and current standing data (e.g. the report's underlying design to ensure the correct authorisation limits are picked up), and on those limits being subject to appropriately controlled access and change controls, means that the indirect general IT controls over access to this information and the ability to change it should be evaluated and tested also. This is normally restricted to access and change controls as relevant to this part of the system. The engagement team may also need to ensure that the correct credit limits have been allocated to the correct customers, either by testing the entity's controls over this, or by performing substantive testing to assure the same.

35.92 ***Consultation required*** If the engagement team believes they may need to evaluate the design, implementation and operating effectiveness of indirect general IT controls, or is uncertain whether this will be the case, they must contact the Digital Financial Audit team for advice.

35.93 The engagement team may find in the above example that there is a higher number than expected of staff with 'administrator' or 'super-user' access to the IT system, giving them the ability to change standing data. This initially calls into doubt the effectiveness of the design of the indirect general IT controls over the exception reports. However, judgement can and should be applied to consider the likelihood and risk of material misstatement resultant from so many with this level of access. It may be that most are in the IT support function with limited knowledge of finance controls or that the team considered that while material, the transaction or balance subject to risk is well-understood and has not seen any noticeable volatility in past years so the risk of a material misstatement is highly unlikely still. Management may have sufficient controls over who receives this level of access and regularly checks reports to ensure only those who have a legitimate business need are granted it. Otherwise, in consultation with the IT Audit team, the engagement team may consider reporting a deficiency in this area of control.

35.94 An automated control can be expected to function consistently unless the program (including the tables, files, configuration or other permanent data used by the program) is changed. Once it has been determined that an automated control is functioning as intended (which could be done at the time the control is initially implemented or at some other date), the engagement team will usually plan to perform tests to determine that the control continues to function effectively. Such tests might include determining that:

- changes to the program are not made without being subject to the appropriate program change controls;
- the authorised version of the program is used for processing transactions;
- authority and access to make such changes is appropriately restricted to persons in accordance with their business function; and
- other relevant general IT controls are effective.

35.95 Such tests might also include determining that changes to the programs have not been made, as may be the case when the entity uses packaged software applications without modifying or maintaining them.

Concluding and reporting

35.96 Paragraphs 16 to 17 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) and the related application guidance set out how the engagement team should evaluate the operating effectiveness of controls (including any indications from misstatements detected by substantive procedures that controls are not operating effectively) and respond to any deviations or failures from controls upon which they intend to rely.

35.97 In accordance with paragraph 15 of ISA (UK) 530 (Updated May 2022), the engagement team should evaluate the results of controls samples and whether the use of audit sampling has provided a reasonable basis for conclusions about whether the controls being tested have operated effectively.

35.98 Engagement teams need to conclude whether a control is operating effectively. This means that a detective control is detecting material errors and corrective action is implemented and followed up, and that a preventative control is preventing material errors with appropriate follow up action to ensure repetition does not happen.

35.99 In accordance with paragraph 12 of ISA (UK) 530 (Updated May 2022), the engagement team should investigate the nature and cause of any control deviations identified and evaluate their possible effect on the purpose of the audit procedure and on other areas of the audit. Where necessary, the engagement team should obtain evidence to support their understanding of the impact of the deviation and any mitigating factors.

35.100 Judgement is necessary in evaluating the impact of control deviations. Apparently minor deviations in how a control has operated may indicate that it is not operating to prevent or detect misstatements, whereas in other circumstances these may not be significant

35.101 The engagement team should consider whether a failure in controls testing indicates a wider control environment weakness and, in particular, whether the original assessment of the risk of material misstatement, of fraud and of irregularity remains valid. This judgement should be documented.

35.102 If the control operates, the engagement team may take the planned level of assurance from controls. If it does not, the engagement team will undertake alternative procedures such as a substantive analytical procedure before undertaking substantive sampling. It is, however, important that the engagement team use their judgement in evaluating the results and consider the following in all cases of apparent control deviations and failures:

- The nature and cause of the failures: this will help the engagement team to identify the potential impact of the deviation and therefore the additional procedures that they will need to complete. For example, it may be that the failure can be isolated to a particular location, time or other set of circumstances. In such cases, provided the engagement team can satisfy themselves that they can identify all similar circumstances, the engagement team can target their substantive testing in these areas and may be able to take assurance from controls in others.
- The possibility of compensating controls: the engagement team may have identified a control as key where there are, in fact, compensating controls that operate in the event of a deviation or failure. For example, the engagement team may identify a failure to check and authorise an invoice

for payment at a supervisory level but then find that all such "unauthorised" invoices are identified during processing and subject to checking at a higher management level.

- The impact of the deviation on the initial risk assessment and other sources of audit evidence: where the engagement team finds significant breakdowns in the general system of control, they should consider the implications for the entire audit approach and in particular the reliability of management representations on the effectiveness of internal controls (see Chapter 56: Management representations).

35.103 In the extremely rare circumstances when a deviation discovered in a sample is considered an anomaly, the engagement team should obtain a high degree of certainty that the deviation is not representative of how the control has operated through the period considered by performing additional audit procedures to obtain sufficient appropriate audit evidence that the deviation does not affect the remainder of the population. The nature and extent of these additional procedures are a matter of audit judgement and as such should involve more experienced engagement team members, including at least the Engagement Manager.

35.104 For monthly or quarterly controls which are based on cumulative information that is prepared on a regular basis and the control failure is not at the end of the financial period, the engagement team may assess that the effective operation of the control towards the period end still gives the controls assurance that they planned to obtain.

35.105 However, the engagement team should consider if there is an effect on the Governance Statement and what information needs to be disclosed. If a control ceases to operate in the period, the engagement team cannot take the planned assurance for the entire financial period but may be able to take some assurance and reduce the level of substantive testing for the period when the control operated effectively.

35.106 These are matters of judgement and the engagement team should involve the Engagement Director in reaching conclusions about the extent to which controls assurance is appropriate.

35.107 When seeking to rely on controls that operate many times a day, a deviation in the operation of the control may be expected. If this is expected at the planning phase, the sample size should be set accordingly as discussed above. If a failure is not anticipated at the planning stage, or more than one deviation is detected during testing, then this would usually prevent the engagement team from being able to take assurance from the operating effectiveness of controls.

35.108 When the engagement team assesses that they cannot take the planned level of audit assurance from controls testing, they must revisit the planning assumptions and resubmit the audit plan for review and approval by the Engagement Director.

35.109 Where control deviations or failures have been identified, the engagement team should consider whether this should be communicated to management and those charged with governance (see Chapter 57: Reporting to those charged with governance).

Documentation

35.110 The results of all controls testing should be clearly documented showing:-

- how the planned tests of controls address the risks of material misstatement that the controls were addressing;
- what work was carried out when and by whom;

- which documents were examined, which procedures were observed and which staff were interviewed;
- what control deviations or failings were identified, how these were investigated and the impact of these on the planned level of assurance;
- where appropriate, the additional procedures undertaken as a result of the control deviations or failings;
- any recommendations to management resulting from the engagement team's work; and
- our conclusions on the extent of reliance to be drawn from our tests of controls.

35.111 Engagement teams should clearly document their assessment of whether control deviations or failures indicate a wider control environment weakness and whether the original assessment of the risks of material misstatement, of fraud and of material irregular transactions remains valid. Where weaknesses are identified in the wider control environment, the engagement team should, as appropriate to reflect these weaknesses, update the Understanding the Entity's System of Internal Control template, the risk assessment set out in the Risk Assessment in Apex and the Regularity Testing Plan.

35.112 If, the engagement team has planned to use audit evidence about the operating effectiveness of controls obtained in previous audits, they should include in the audit documentation the conclusions reached about relying on such controls that were tested in a previous audit. These conclusions should include sufficient detail about the testing performed in a previous audit to enable the reviewer to understand the extent of procedures performed and the result of the testing.

35.113 Evaluating the adequacy of the design and implementation of controls, and the implications of control deviations, requires familiarity with how control systems operate. Accordingly, more experienced members of the engagement team should be involved in this process.

35.114 Where issues are identified, the Engagement Manager and Engagement Director should be involved at an early stage in order to agree an appropriate response.

35.115 Engagement team members should ensure that they are familiar with how the controls that they are testing are intended to operate and how this provides assurance over the risks of material misstatement that are being tested.

35.116 Documentation should make clear how each relevant aspect of the operation of the control for the items selected has been tested.

Chapter 36: Accounting estimates

Relevant standards and guidance

36.1 ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures* deals with the auditor's responsibilities relating to accounting estimates and related disclosures in an audit of financial statements. Specifically, it includes requirements and guidance that refer to, or expand on, how ISA (UK) 315 (Revised June 2016), ISA (UK) 330 (Revised July 2017) (Updated May 2022), ISA (UK) 450 (Revised June 2016) (Updated May 2022), ISA (UK) 500 (Updated May 2022) and other relevant ISAs (UK) are to be applied in relation to accounting estimates and related disclosures. It also includes requirements and guidance on the evaluation of misstatements of accounting estimates and related disclosures, and indicators of possible management bias.

36.2 Paragraphs 1-108 to 1-115 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provides guidance on applying ISA (UK) 540 (Revised December 2018) (Updated May 2022) in the public sector.

Background

36.3 Accounting estimates are items included in financial statements which cannot be measured precisely but can only be estimated. The nature and reliability of information available to management to support the making of an accounting estimate varies widely, which thereby affects the degree of estimation uncertainty associated with accounting estimates. The degree of estimation uncertainty affects, in turn, the risks of material misstatement of accounting estimates, including their susceptibility to unintentional or intentional management bias. Examples include financial instruments held at fair value, land and buildings valuations, assets held for sale, depreciation, provisions, impairments, and accruals.

36.4 When auditing accounting estimates, including fair values, the quality of our work is dependent upon understanding the broader picture of the accounting estimate being considered. The exercise of due professional scepticism requires the engagement team (including the specific team members allocated to the work) have an appropriate understanding of:

- the business context of the transaction or balance being audited;
- management's incentives and motivations and how these impact on the accounting estimate;
- the method used to determine the accounting estimate; and
- how the judgements and assumptions made in determining the accounting estimate compare to other judgements and assumptions that management have made.

36.5 Engagement teams should use this understanding to challenge the appropriateness of the methodology being used and the assumptions being made.

Design of further audit procedures

36.6 When testing management's estimate, audit procedures should cover the following key areas:

- Selection and application of methods used in the estimate.
- Selection and application of significant assumptions used.
- Selection and application of the data used by management.
- How management selected the point estimate and developed related disclosures.

36.7 There may sometimes be a higher than normal degree of inherent risk in respect of the method, the use of models, data, selecting assumptions or in addressing estimation uncertainty. Examples of estimates for which this may be the case include:

- specialised estimates where the use of additional expertise may be considered, such as defined benefit pensions, property valuations and unusual provisions (see also Section 12: Use of experts); or
- estimates where complex models may be used, such as some types of accruals, financial assets or public infrastructure assets. These may be unusual or even unique to the entity.

36.8 The NAO has developed standardised approaches to responding to the risks associated with these types of complex estimates. For these estimates where there is a higher than normal degree of inherent risk, the appropriate more complex procedures within the NAO's risk library should be selected as part of the risk assessment and response planning activities set out in Chapter 17: Risk assessment and response planning.

36.9 Regardless of the approach adopted, the Risk Assessment in Apex should be used to document our choices of further audit procedures and how they relate to the identified risks of material misstatement.

Design of further audit procedures – evaluating the selection and application of methods

36.10 This evaluation is likely to involve the exercise of professional judgement in considering the appropriateness of the measurement method adopted, and teams may need to consider measurement methods adopted elsewhere in government or in industry for comparable balances in making this determination.

36.11 For example, certain estimates (for example property, private equity or actuarial estimates), may be subject to professional standards or guidelines outside the field or auditing and accounting that define the methods, techniques or data sources which should be used. Use of specialised skills or knowledge may be required to make this assessment.

36.12 Where the engagement team is seeking to rely on any work done in the prior year, they will need to document clearly whether this remains relevant, and whether the team has considered any alternatives. For example, methods may need to change to take account of:

- Changes in the economic environment.
- The size and sensitivity of the estimate in the context of the financial statements and materiality.
- Changes in the financial reporting framework.
- Changing industry or professional practice in the making of comparable estimates.

36.13 However, it is important to understand whether a change in accounting estimate or method of calculation is arbitrary (i.e. not based upon a change in the entity's circumstances or new information being received). Arbitrary changes in an accounting estimate result in inconsistent financial statements over time and may give rise to a financial statement misstatement or be an indicator of possible management bias.

36.14 Management may be able to demonstrate good reason for a change in an accounting estimate or the method for making an accounting estimate from one period to another based on a change in circumstances. What constitutes a good reason, and the adequacy of support for management's contention that there has been a change in circumstances that warrants a change in an accounting estimate or the method for making an accounting estimate, are matters of judgment.

Design of further audit procedures – selection and application of significant assumptions

36.15 Paragraph A103 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) discusses the use of a sensitivity analysis by management to evaluate alternative assumptions or outcomes of accounting estimates.

36.16 If management does not appear to have considered alternative assumptions or outcomes, or their documentation and assessment of assumptions is incomplete, this may indicate that management have not taken appropriate steps to understand and/or address estimation uncertainty within the estimate. In these cases, the engagement team shall:

- Request management to perform additional procedures to understand estimation uncertainty or to address it by reconsidering the selection of management's point estimate or considering providing additional disclosures relating to the estimation uncertainty. The engagement team shall then evaluate management's response.
- If the engagement team determines that management's response to the auditor's request does not sufficiently address estimation uncertainty, to the extent practicable, develop an auditor's point estimate or range.
- Evaluate whether a deficiency in internal control exists and, if so, communicate to those charged with governance.

36.17 ***Consultation required*** If alternative assumptions or outcomes do exist, or information available to the engagement team suggests that management's estimate is not the most reasonable in all the circumstances, the engagement team should challenge management on the robustness of their estimation processes. This may require management to undertake additional work and/or may require the engagement team to consider the impact on the audit opinion. Engagement teams should consult FAPQ in these circumstances.

Design of further audit procedures – selection and application of data

36.18 Paragraphs A106 and A107 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) include requirements regarding the appropriateness of data used by management.

36.19 The engagement team is also required to assess whether changes from prior periods in the sources or items of data selected are based on new circumstances or new information. When they are not, they are unlikely to be reasonable or in compliance with the applicable financial reporting framework. Arbitrary changes in an accounting estimate result in inconsistent financial statements over time and may give rise to financial statement misstatements or may be an indicator of possible management bias.

36.20 In some cases, the risks associated with the use of data can relate to its understanding and interpretation, such as with to respect to contractual terms. Procedures that the engagement team may consider when accounting estimate is based on complex legal or contractual terms are listed in paragraph A108 of ISA (UK) 540 (Revised December 2018) (Updated May 2022).

Design of further audit procedures – addressing estimation uncertainty

36.21 Estimation uncertainty is the susceptibility of an accounting estimate and related disclosures to an 'inherent lack of precision in its measurement' and relates to factors outside the reporting entity's control.

36.22 The inherent uncertainty present when measuring an accounting estimate means management must exercise judgment in selecting a point estimate and in deciding upon the appropriate level of disclosure about that uncertainty. Making these judgments requires management to understand the level of uncertainty, through identifying its sources and the degree of inherent variability in the measurement of the estimate.

36.23 The engagement team should therefore evaluate whether management has taken appropriate steps to understand and address estimation uncertainty in relation to an accounting estimate. Management may, for example, have carried out a sensitivity analysis to understand the sources and scale of uncertainty. If carried out adequately, this can be used by engagement teams to determine where they should focus their attention (for example, which are the significant assumptions).

36.24 Performing an adequate sensitivity analysis itself requires appropriate skills and knowledge in the context of the nature and characteristics of the estimate, coupled with the need to exercise professional judgment. For instance, the range of possible values of assumptions analysed should not be arbitrary but chosen from a range of reasonably possible amounts. Specialised skills or knowledge may be required to make this assessment.

36.25 Where risks of material misstatement exist due to the complexity or subjectivity inherent in the measurement process, the engagement team might conclude that management have not taken appropriate steps to understand and address estimation uncertainty if they have not addressed the resulting potential for misstatement through applying:

- appropriate skills and knowledge in making accounting estimates; and
- professional judgment, including by identifying and addressing susceptibility to management bias.

36.26 Where the engagement team concludes that management has not taken appropriate steps to understand and address estimation uncertainty, consulting with internal or external specialists relevant to the estimate in question can be helpful when challenging management in accordance with paragraph A115 of ISA (UK) 540 (Revised December 2018) (Updated May 2022); for example, to:

- comment on the robustness of their estimation process;
- establish what alternative assumptions, data sources or methods might exist; and
- if required, to develop our own sensitivity analysis or auditor's estimate.

36.27 ***Consultation required*** However, in the circumstances envisaged by paragraph A117 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) (after considering management's response, the auditor determines that it is not practicable to develop an auditor's point estimate or range), the engagement team should consult FAPQ on their evaluation of the implications for the audit or the auditor's opinion on the financial statements.

Assessing the need for specialised skills or knowledge

36.28 Paragraphs A61 to A63 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) include requirements on the use of specialised skills or knowledge.

36.29 At the start of the audit the Engagement Director should consider whether the engagement team has necessary skills, knowledge and experience to perform the audit.

36.30 Specialised skills or knowledge could be required to carry out the risk assessment procedures, identify and assess the risks of material misstatement, design and perform audit procedures to respond to those risks, or to evaluate the audit evidence obtained.

36.31 In making their judgment on whether specialised skills or knowledge is required, the engagement team should be guided by advice and guidance from relevant internal centres of expertise, such as for property valuation and pensions. For example, centres of expertise may develop standard risk assessment tools and/or or undertake specific consultation meetings with teams. Where the relevant field is not covered by a centre of expertise, FAPQ can provide guidance and help in finding an appropriate internal or external expert if required.

36.32 Regardless of whether an auditor's expert used, or not, further specific actions may be required to ensure the engagement team has the necessary skills, knowledge and experience to carry out their work. Further information is provided later in this Chapter regarding engagement quality control in relation to accounting estimates.

Audit evidence and the use of experts

36.33 Where the engagement team decides to make use of the work of an internal or external expert, they should be mindful of the requirements of ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert*. Further information is available in Section 12: Use of experts.

36.34 The engagement team is required to consider the reliability of information used as audit evidence. This applies to information produced by the entity, but also that provided to management or to the engagement team by an external information source. Such external information sources could include, for example, providers of economic data, statistics or pricing information for financial assets, which are commonly used in the making of estimates. Paragraphs 1-113 to 1-114 of Practice Note 10 (Revised 2022) provide further guidance on the use of external information sources in public sector audits.

36.35 Where management have made use of an expert, the engagement team must perform sufficient work to earn the right to rely on this as evidence. The engagement team should not accept the output of management's expert's work as appropriate without further consideration. It is important to understand the instructions that the expert received and how this affects the reliability of their work.

Indicators of possible management bias

36.36 When evaluating whether judgments and decisions made by management in making the accounting estimates included in the financial statements, even if they are individually reasonable, are indicators of possible management bias in accordance with paragraph 32 of ISA (UK) 540 (Revised December 2018) (Updated May 2022), the engagement team should exercise particular professional scepticism when reviewing management estimates relating to fair values, the impairment of assets and provisions.

36.37 In considering whether there are indicators of bias, possible factors to consider include:

- strong political motives for a particular estimate;
- a changing or unstable political environment;
- higher than normal expectations to meet budget; and
- reductions in budgets without corresponding reduction in service delivery expectations.

36.38 The engagement team should consider instances of possible bias as part of our consideration of the pervasive risk of management override of controls.

36.39 The engagement team should consider the risk of an excess vote in considering possible indicators of management bias in accounting estimates. Although the excess vote would be at departmental level the treatment in consolidating arm's length bodies (ALBs) could also impact this and should therefore be considered.

Overall evaluation based on audit procedures performed (the 'stand back' requirement)

36.40 ***Consultation required*** In making the 'stand back' evaluation required by paragraphs 33 and 34 of ISA (UK) 540 (Revised December 2018) (Updated May 2022), if the auditor is unable to obtain sufficient appropriate audit evidence, the engagement team should consult FAPQ on their evaluation of the implications for the audit or the auditor's opinion on the financial statements.

36.41 In evaluating the reasonableness of an accounting estimate, it is important to take a holistic view of what is being measured and the underlying substance of the balance, whether commercial in nature or driven by public policy.

36.42 In making this overall assessment, the engagement team should draw together the totality of audit evidence obtained; both that which supports management's judgments (corroborative) and that which casts doubt upon them (contradictory) and consider whether that evidence is consistent with that obtained throughout the audit.

36.43 This assessment should also, critically, cover the financial statement disclosures supporting the estimate. The specific requirements will depend upon the nature of the estimate and the financial reporting framework. However, as a general rule, for a significant estimate, the financial statements should clearly explain:

- The nature of the transactions or balances giving rise to the estimate;
- The measurement basis;
- How management made their estimate, including the significant judgments they made in doing so; and
- An indication of the level of estimation uncertainty inherent in the estimate;

36.44 In some cases, high estimation uncertainty gives rise to a significant risk that the carrying values of assets or liabilities could require material adjustment in the next financial year. Financial reporting frameworks (including the FReM, IFRS and FRS 102) require additional disclosures in these circumstances to help users understand the sources of uncertainty and the judgments about the future that management has made.

Determining whether the accounting estimates are reasonable or misstated

36.45 The FReM and IFRS are fair presentation frameworks for the purpose of paragraph 36(a) of ISA (UK) 540 (Revised December 2018) (Updated May 2022) (evaluation of whether management has included disclosures, beyond those specifically required by the framework, that are necessary to achieve the fair presentation of the financial statements as a whole).

36.46 Where management has changed an accounting estimate, or the method in making it, from the prior period based on a subjective assessment that there has been a change in circumstances, the engagement team may conclude based on the audit evidence that the accounting estimate is

misstated as a result of an arbitrary change by management or may regard it as an indicator of possible management bias.

36.47 ***Consultation required*** Very high estimation uncertainty can lead to an emphasis of matter paragraph being issued on the audit certificate or report. However, where there is uncertainty in the estimate arising from factors within the audited entity's control (for example, management does not have sufficiently good data and it is reasonable to expect them to have such data) this could indicate a limitation on the scope of the audit. It is important for engagement teams to evaluate whether management has done everything reasonable to reduce uncertainty in the estimate. Engagement teams should consult with FAPQ in these circumstances.

36.48 A difference between the outcome of an accounting estimate and the amount originally recognised or disclosed in the financial statements does not necessarily represent a misstatement of the financial statements.

36.49 This is particularly the case for fair value accounting estimates, as any observed outcome is invariably affected by events or conditions subsequent to the date at which the measurement is estimated for the purposes of the financial statements.

36.50 However, in some cases, failure to consider information available before the financial statements are authorised for issue could represent a misstatement, if it would reasonably affect the measurement of that estimate under the relevant financial reporting framework.

Documentation

36.51 Significant accounting estimates may be significant documentation matters. In these cases, the engagement team should pay particular attention to the requirements in paragraphs 8 to 11 of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation*.

Communication

36.52 The engagement team is required to communicate with those charged with governance their views about significant qualitative aspects of the entity's accounting practices relating to accounting estimates and relevant disclosures. Appendix 2 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) provides examples of a wide range of issues the engagement team may consider communicating in this manner.

Quality management in respect of accounting estimates

36.53 The audit of accounting estimates is often one of the more complex, judgmental and challenging areas of an audit and is subject to a higher degree of audit quality risk. A higher degree of focus on these areas is therefore required: both in terms of file review and in actions to ensure the competence and capability of the engagement team members assigned to these areas.

36.54 In addition, there is a need for specialist skills or knowledge to be assessed at all stages of an audit; from risk assessment procedures through to evaluating audit evidence. This may be addressed via use of an auditor's expert but might also include specific education or professional development in the relevant field and/or or discussions with auditors who have performed similar engagements by individual team members.

36.55 Within the engagement team:

- Each team member should consider whether they have sufficient understanding of the audited entity, the estimate and the relevant requirements of the financial reporting framework before starting testing in order to be able to effectively audit the estimate. They should discuss with the Engagement Director any additional information they feel they need in order to effectively audit their assigned balances.
- Engagement team members should document clearly the work performed, the judgements made, and the conclusions of their tests.
- The Engagement Director should review the plan for auditing accounting estimates and related disclosures and the conclusion of the work. Their review should include consideration of the overall truth and fairness of the financial statements and so of the reasonableness and potential for bias of significant accounting estimates and related disclosures.
- The Engagement Manager, Director and EQR (where relevant) should ensure they have sufficient skills and knowledge to perform their review responsibilities effectively, in the context of the risk and requirement for specialised skills and knowledge to prepare and audit accounting estimates.
- Where a member of the engagement team uses specialised skills or knowledge to carry out audit procedures, the Engagement Manager or Director may not possess the skills or knowledge to effectively review certain technical aspects of their work. In this case, the engagement team should ensure that appropriate quality assurance procedures are in place over the work of the specialist. For example, technical aspects of their work could be reviewed by another experienced individual in the field. Such procedures supplement rather than replace the need for detailed first-stage review.
- EQR (where applicable) - where the level of uncertainty in determining accounting estimates is high, they have a significant impact on the financial statements, there are indicators of management bias, or for any other reason accounting estimates are a significant judgment, the Engagement Quality Reviewer should review the judgements made and conclusions reached in respect of accounting estimates.

36.56 Due to their potential complexity and impact on the financial statements, clear documentation of the work performed on accounting estimates is important to enable efficient and effective review.

36.57 The reviewer has a wider visibility of the accounting estimates that have been made and the audit evidence obtained than individual engagement team members. The reviewer should therefore consider as part of their review the consistency and appropriateness of the accounting estimates as a whole and in relation to other audit evidence. This overall understanding is particularly important in considering whether there are indicators of management bias or of estimates being prepared on the basis of inconsistent assumptions.

36.58 Documentation of the professional judgments made, where significant, serves to explain our conclusions and to reinforce the quality of the judgment in the file.

Chapter 37: Other specific audit procedures

Relevant standards and guidance

37.1 ISA (UK) 501 (Updated May 2022) *Audit evidence – specific considerations for selected items* deals with specific considerations by the auditor in obtaining sufficient appropriate audit evidence in accordance with ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks*, ISA (UK) 500 (Updated May 2022) *Audit evidence* and other relevant ISAs (UK), with respect to certain aspects of:

- inventory;
- litigation and claims involving the entity; and
- segment information in an audit of financial statements.

The objective of the auditor under ISA (UK) 501 (Updated May 2022) is to obtain sufficient appropriate audit evidence regarding the:

- existence and condition of inventory;
- completeness of litigation and claims involving the entity; and
- presentation and disclosure of segment information in accordance with the applicable financial reporting framework.

37.2 ISA (UK) 505 (Updated May 2022) *External confirmations* deals with the auditor's use of external confirmation procedures to obtain audit evidence in accordance with the requirements of with ISA (UK) 330 (Revised July 2017) (Updated May 2022) and ISA (UK) 500 (Updated May 2022). The objective of the auditor under ISA (UK) 505 (Updated May 2022) is to design and perform external confirmation procedures to obtain relevant and reliable audit evidence.

Computer-assisted audit techniques and digital audit

37.3 "Computer-assisted audit techniques" or 'digital audit techniques' describes a variety of methods of using information technology in audits, ranging from simple automation of checks such as casting of totals through to sophisticated analyses of entire populations which would not be practical otherwise.

37.4 The use of computer-assisted audit techniques ("CAATs") may enable 100% analyses of electronic transactions and account files to be performed efficiently. This may be particularly useful in responding to significant risks.

37.5 NAO auditors have access to MS Excel, AIMS and (upon email request to the ATS Core Team) to IDEA to support the analysis of data

37.6 The Audit Technology Services pages on Sharepoint contain guidance on how to perform a number of common CAATs using IDEA. Guidance on the use of AIMS applications that can also be used to perform CAATs is also available on Sharepoint.

37.7 Evidence about accuracy and completeness of information used in performing an audit procedure can be obtained concurrently as an integral part of the audit procedure itself, by testing controls (which may be IT dependent and reliant upon indirect General IT controls) over the preparation and maintenance of the information, or by additional audit procedures such as two-way testing or reconciling to a known, reliable source

37.8 ***Table 37A*** below provides a non-exhaustive set of circumstances where CAATs may be applicable.

Table 37A: Circumstances where CAATs may be applicable

Journals testing	Engagement teams are required to test journal entries as part of the response to the pervasive risk of fraud through management override of controls. This requirement is discussed in Chapter 17: Risk assessment and response planning. When automated procedures are used to maintain the general ledger and prepare financial statements, journal entries may exist only in electronic form. It may therefore be most effective and efficient to use CAATs to test journal entries. ***Consultation required*** All engagement teams should use the most recent version of the AIMS Journals App for auditing journals. Where an engagement team does not believe they will be able to use the most recent journals analytic tool, they should consult FAPQ.
Profiling	CAATs are usually necessary when profiling is used as a sampling technique for tests of detail. Profiling is a sampling technique which can be used where it is possible to identify characteristics of items within the population which would indicate whether or not they are likely to be of audit interest. Profiling involves stratifying population into items requiring differing levels of testing, focusing testing on the items most likely to be of audit interest while reducing the overall extent of the procedures performed.
Benford's Law analyses	Benford's law states that there is a natural pattern to the distribution of the each of the digits making up the values / numbers within a population (for example, the last digits of numbers have a typical frequency of occurring). Unusual frequencies of particular digits of the values / numbers within a population may indicate manipulation of the underlying data. A Benford's law analysis can be prepared using IDEA or other software packages. The AIMS Journals App contains Benford's law analysis.

37.9 Other examples of possible uses of CAATs include:

- identifying duplicate payments through a purchase-to-pay (PTP) business process analytic;
- checking numeric/date sequences for gaps;
- comparing addresses or other information to identify employees that are also suppliers (PTP);
- comparing addresses or other information to identify possible ghost employees;
- identifying suppliers with only PO Boxes as addresses;
- sorting payments by value to identify transactions that fall just under authorisation limits;
- identifying unusual items such as:
    - employees working unusually high hours or at unusual rates;
    - unusually high or frequent expense claims;
    - unusual patterns in the level of usage of suppliers (PTP); and/or
    - large round-sum items;

- checking data logs for modifications to master files;
- checking for slow-moving inventory;
- Analysing dates that leavers were removed from systems vs the date they left employment to identify weaknesses in the leaver controls;
- Analysing users roles to identify segregation of duty conflicts;
- Analysing supplier configurations to confirm they were all subject too the correct matching policies; and
- performing a 100% payroll recalculation based upon master HR data and amounts actually paid via BACS.

37.10 The work performed should be documented in sufficient detail to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the procedures performed and their results. This will usually include at least:

- the data source used;
- the procedures performed over the accuracy and completeness of the data;
- how the test was performed, including any modifications made to the data to facilitate analysis;
- the results of the procedures performed; and
- quality assurance procedures performed over bespoke analytics.

37.11 The NAO's overall policy regarding quality assurance (QA) of data analytics tools is as follows:

- Where a central data analytics tool is used in the audit, evidence of the QA process applied to that tool is held centrally and is not required to be documented on individual audit files.
- Where a bespoke data analytics tool is used for a particular audit, evidence of the QA performed over that tool, as well as any QA over coding, must be documented on the Apex audit file for that audit.

37.12 ***Consultation required*** Engagement team members should make use of digital audit techniques, also called CAATs where they judge it would be an effective substitute for equivalent manual procedures. Common tools available are IDEA and MS Excel. AIMS Applications are available including approved analytic tools such as for manual journals analysis, business process analytics (such as purchase to pay and payroll) and the Financial Audit Data Analytics team within the Analysis hub (DART) may be able to assist with bespoke digital solutions. The engagement team should consult with DART if a CAAT involves macros, scripts or other forms of coding that have not been produced and approved by DART.

37.13 The engagement team may also use digital techniques as risk assessment procedures or to support the performance of audit procedures to obtain assurance over risks of material misstatement, including significant risks. Engagement teams should consider carefully which risks of material misstatement will be covered by such techniques and implement manual techniques to obtain coverage over all risks of material misstatement where necessary.

37.14 Any use of digital techniques is dependent upon handling electronic data and information produced by the entity. All team members should comply with the NAO's data protection policy (see the Sharepoint page on the management of data used for audit purposes).

37.15 Where the use of digital techniques involves using information produced by the entity, the engagement team should follow the requirements of paragraph 9 of ISA (UK) 500 (Updated May 2022) *Audit evidence* and the related application guidance to evaluate whether the information is sufficiently reliable for the auditor's purposes.

37.16 CAATs can be used in tests of regularity, such as in selecting items for testing when using profiling.

37.17 The use of CAATs is dependent upon access to appropriately-formatted audited entity data. Engagement teams will need to agree this access with management. The Central AIMS team (contact form available on the AIMS Support page on Sharepoint) is able to support in discussions with IT departments on appropriate file formats and data transfer protocols.

37.18 CAATs may involve the use of personal data. Where this is the case, the NAO's data protection policy requires that engagement teams communicate in writing to management and those charged with governance how the personal data obtained has been treated.

37.19 The data processing form must be completed to record how each item of personal or other sensitive piece of data collected during the course of the audit, as recorded on the form, has been treated: that is, whether it has been retained, destroyed or returned to the audited entity.

37.20 ***Consultation required*** CAATs can be complex to design. The engagement team must consult with relevant IT audit or data specialists to assist in performing the testing and to ensure that appropriate assurance is obtained over the reliability of the data.

External confirmations

37.21 Paragraph 6 of ISA (UK) 505 (Updated May 2022) sets out the following definitions which apply in respect of external confirmations:

- External confirmation – Audit evidence obtained as a direct written response to the auditor, or by the auditor directly, from a third party (the confirming party), in paper form, or by electronic or other medium. Electronic or other medium could include auditors directly accessing information held by third parties through web portals, software interfaces or other digital means.
- Positive confirmation request – A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.
- Negative confirmation request[9] – A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.
- Non-response – A failure of the confirming party to respond, or fully respond, to a positive confirmation request, or a confirmation request returned undelivered.
- Exception – A response that indicates a difference between information requested to be confirmed, or contained in the entity's records, and information provided by the confirming party.

37.22 In accordance with paragraph 19 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) and the related application guidance, engagement teams should consider whether external confirmation procedures are to be performed as substantive audit procedures.

37.23 Engagement teams are encouraged to use external confirmations where considered appropriate, including cash, as confirmations from external parties received directly by the NAO may be more reliable evidence than evidence provided by the audited entity. In general:

- audit evidence is more reliable when it is obtained from independent sources outside the entity;
- audit evidence obtained directly by the engagement team is more reliable than audit evidence obtained indirectly or by inference; and

[9] The use of negative confirmations is prohibited in an audit conducted in accordance with ISAs (UK). Accordingly, the requirements and related application material in ISA (UK) 505 (Updated May 2022) relating to negative confirmations are not applicable.

- audit evidence is more reliable when it exists in documentary form, whether paper, electronic or other medium.

37.24 Therefore, external confirmations may be particularly appropriate in addressing significant risks or where it is otherwise difficult to obtain sufficient appropriate audit evidence.

37.25 As well as ISA (UK) 505 (Updated May 2022), other ISAs (UK) also suggest external confirmations can provide important audit evidence. Examples are given in paragraph 3 of ISA (UK) 505 (Updated May 2022).

37.26 External confirmations provide more relevant evidence for certain risks of material misstatement than others. In particular, confirmations typically provide less relevant evidence about valuation: for example, a receivable confirmation will not necessarily provide sufficient evidence of recoverability, as although a debtor may acknowledge that they owe the money they may still be unable to repay the debt. Further, if they believe they owe a greater sum than that requested in the confirmation, the debtor may be reluctant to advise differently.

37.27 Factors to consider in determining whether to use external confirmations include:

- the confirming party's knowledge of the subject matter – responses may be more reliable if provided by a person at the confirming party who has the requisite knowledge about the information being confirmed;
- the ability or willingness of the intended confirming party to respond – for example, the confirming party:
    - may not accept responsibility for responding to a confirmation request;
    - may consider responding too costly or time consuming;
    - may have concerns about the potential legal liability resulting from responding;
    - may account for transactions in different currencies; or
    - may operate in an environment where responding to confirmation requests is not a significant aspect of day-to-day operations. In such situations, confirming parties may not respond, may respond in a casual manner or may attempt to restrict the reliance placed on the response; and
- the objectivity of the intended confirming party - if the confirming party is a related party of the entity, responses to confirmation requests may be less reliable.

37.28 Examples of when positive external confirmations may be the only way to obtain sufficient appropriate audit evidence in respect of a risk may include where:

- the information available to corroborate management's assertion(s) is only available outside the entity; and/or
- there are fraud risk factors, such as the risk of management override of controls, or the risk of collusion which can involve employee(s) and/or management, prevent the engagement team from relying on evidence from the entity.

37.29 A number of major frauds have involved management intercepting or influencing the confirmation process. If appropriate control is not maintained over confirmations, they may no longer represent reliable audit evidence.

37.30 Where frauds have occurred involving confirmations, they have often involved subverting the confirmation process by providing the engagement team with incorrect address details. It is therefore important (as discussed further below) to check the validity of a sample of addresses as part of the confirmation process.

37.31 The NAO has templates for a number of common types of confirmations, including bank, receivable and payable confirmations and legal letters.

37.32 The design of a confirmation request may directly affect the confirmation response rate, and the reliability and the nature of the audit evidence obtained from responses. Factors to consider when designing confirmation requests include:

-
- the identified risks of material misstatement, including fraud risks;
- the layout and presentation of the confirmation request;
- prior experience on the audit or similar engagements;
- the method of communication (for example, paper, electronic or other medium);
- confirming parties may only be willing to respond to a confirmation request containing management's authorisation; and
- the ability of the intended confirming party to confirm or provide the requested information, such as the individual invoice amount versus the total balance.

37.33 There is a risk that a confirming party may reply to the confirmation request without verifying that the information is correct. Engagement teams can reduce this risk by using positive confirmation requests that do not state the amount (or other information) on the confirmation request and ask the confirming party to fill in the amount or furnish other information.

37.34 Use of this type of "blank" confirmation request may result in lower response rates because additional effort is required of the confirming parties.

37.35 The reason for obtaining evidence that management's reasons are valid and reasonable is because a refusal to allow a confirmation request may be an attempt to disguise fraud or error.

37.36 The alternative audit procedures performed may be similar to those appropriate for a non-response as set out in paragraphs 12 and A18 to A19 of ISA (UK) 505 (Updated May 2022).

37.37 It may help to categorise the results of individual external confirmation requests as:

- a response by the appropriate confirming party indicating agreement with the information provided in the confirmation request, or providing requested information without exception – this provides the planned assurance;
- a response deemed unreliable – this does not provide the planned assurance and further testing will be required;
- a non-response – this does not provide the planned assurance and further testing will be required; or
- a response indicating an exception – this requires follow-up.

37.38 All confirmation responses carry some risk of interception, alteration or fraud, regardless of whether the reply is by post or electronically. Factors that may indicate doubts about the reliability of a response include that it:

- was received indirectly (such as via the audited entity); and/or
- appeared not to come from the originally intended confirming party.

37.39 A response to a confirmation request may contain restrictive language regarding its use. Such restrictions do not necessarily invalidate the reliability of the response as audit evidence. Engagement teams should consider and document our assessment of the impact of any restrictive language on the assurance obtained.

37.40 Teams may choose to verify the source and contents of a response to a confirmation request by contacting the confirming party. For example, when a confirming party responds by e-mail, engagement teams may telephone the confirming party to determine whether the confirming party did, in fact, send the response. When a response has been returned to the engagement team indirectly – for example, because the confirming party incorrectly addressed it to the entity rather than to the NAO – engagement teams may request the confirming party to respond in writing directly.

37.41 Fewer responses to confirmation requests than anticipated, or a greater number of responses than anticipated, may indicate a previously unidentified fraud risk factor that requires evaluation in accordance with ISA (UK) 240 (Revised May 2021) (Updated May 2022). When several external confirmations are sent – for example, for a receivables or payables test – it is unusual to achieve a 100% response rate. If fraud were taking place, the individuals involved might ensure that all confirmation requests were replied to in order to avoid suspicion. If the engagement team identifies any new fraud risk factors or indications of fraud as a result of these considerations, they should, as appropriate, revisit the Engagement Team Discussion on Risk and Fraud and reflect any new risks within the Risk Assessment in Apex and/or the Regularity Testing Plan.

37.42 Exceptions noted in responses to confirmation requests may indicate misstatements or potential misstatements in the financial statements. When a misstatement is identified, engagement teams should evaluate whether the misstatement is indicative of fraud. Exceptions may provide a guide to the quality of responses from similar confirming parties or for similar accounts. Exceptions also may indicate deficiencies in the entity's internal control over financial reporting.

37.43 Some exceptions do not represent misstatements. For example, the engagement team may conclude that differences in responses to confirmation requests are due to timing, measurement, or clerical errors in the external confirmation procedures.

37.44 External confirmations may not be appropriate for obtaining assurance over regularity due to concerns over the objectivity of responses. For example, confirmation from a grant recipient to the engagement team that their expenditure has been in line with the purposes of the grant is potentially weak audit evidence. Where confirmations are used, teams should document the rationale for the approach adopted.

37.45 The confirmation work performed should be documented in sufficient detail to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the procedures performed and their results. This would include documenting:

- what risk of material misstatement the procedures are planned to address;
- what information is to be confirmed/requested;
- how the sample of items to be confirmed has been selected;
- who confirmations have been requested from and, where relevant, why they are the appropriate confirming party;
- how engagement teams have determined that the requests are appropriately addressed;
- whether responses were received directly by the NAO and the NAO's response if this was not the case;
- the detail of responses;
- any judgements made and procedures performed in response to issues around reliability of responses, non-responses, or exceptions;
- any further details which are necessary to understand the approach adopted and judgements made.

37.46 The ISAs (UK) emphasise the role that external confirmations can play in obtaining high quality audit evidence. External confirmations may be particularly appropriate in providing evidence in respect of significant risks, in particular where there is a risk of fraud. Engagement Directors and Engagement Managers should therefore consider carefully where confirmations should be used on audits.

37.47 When engagement team members are carrying out confirmation procedures, a properly controlled process is key to performing tests which provide reliable audit evidence. Where frauds have occurred involving confirmations, they have often involved subverting the confirmation process by providing the engagement team with incorrect address details. It is therefore important to check the validity of a sample of data as part of the confirmation process.

37.48 If 100% confirmations are not possible, any judgement at the planning stage to move away from a 100% circulation needs to be grounded in risk, using the principles set out in ISA (UK) 505 (Updated May 2022). This would also be a matter of significant audit judgement to be recorded on file and should be included in the Letter of Representation as appropriate. The engagement team may decide to consult FAPQ in these circumstances.

37.49 In some circumstances, positive external confirmations may be the only way to obtain sufficient appropriate audit evidence in respect of a risk. If this is the case, teams should perform external confirmation procedures and where these are not possible, the team should consider the implications for the opinion.

37.50 In planning and performing external confirmation procedures, it is critical to maintain control over the process and the external confirmation requests and the engagement team should do this by following the requirements of paragraph 7 of ISA (UK) 505 (Updated May 2022) and the related application guidance.

External confirmations – management refuses to allow the auditor to send a confirmation request

37.51 As set out in paragraph 8 of ISA (UK) 505 (Updated May 2022), if management refuses to allow the engagement team to send a confirmation request, the engagement team should:

- enquire as to management's reasons for the refusal, and seek audit evidence as to their validity and reasonableness;
- evaluate the implications of management's refusal on the auditor's assessment of the relevant risks of material misstatement, including the risk of fraud, and on the nature, timing and extent of other audit procedures; and
- perform alternative audit procedures designed to obtain relevant and reliable audit evidence.

37.52 As set out in paragraph 9 of ISA (UK) 505 (Updated May 2022), if the engagement team concludes that management's refusal to allow the engagement team to send a confirmation request is unreasonable, or the engagement team is unable to obtain relevant and reliable audit evidence from alternative audit procedures, the engagement team should communicate with those charged with governance in accordance with paragraph 16 of ISA (UK) 260 (Revised November 2019) (Updated May 2022). The engagement team should also determine the implications for the audit and the auditor's opinion in accordance with ISA (UK) 705 (Revised June 2016).

External confirmations – cash and cash equivalents

37.53 Teams should consider the following factors when designing responses to risks of material misstatement associated with cash and cash equivalents:

- the important role bank accounts have to play in-year;
- cash and cash equivalents appear as a balance on a primary statement;
- the cash and cash equivalents balance forms a key component of the Statement of Cash Flows. For example, if cash is a confirmed figure, it provides strong audit evidence against which other working capital movements and transactions can be corroborated within the Statement of Cash Flows.

37.54 Considering the susceptibility of cash to fraud, as well as the important role banks have of recording all transactions and other facilities/securities they may be providing to entities, engagement teams are expected to obtain confirmations for non-Government Banking Service (non-GBS) accounts when re-performing the bank reconciliation.

37.55 Many banks now participate in, prefer and some insist on using online confirmations via confirmation.com, to which the NAO has subscribed. Confirmation.com enables any NAO auditor to request non-GBS bank confirmations for multiple audited entities up to 90 days before the period end date, to receive the confirmations very soon after the period end date.

37.56 The ATS Core Team administers the confirmation.com service. For example, where a confirmation requestor from the NAO moves teams or jobs, ATS can reassign the confirmation to another registered NAO user. Engagement teams can and should facilitate this themselves by adding additional auditors to the confirmation.com job. Guidance on using confirmation.com is available on the ATS pages on Sharepoint.

37.57 If the audited entity's non-GBS accounts are outside of the BBA (for example, overseas banks), the banks may not provide details of all other facilities, securities and accounts the audited entity may operate other than the ones of which management has made the engagement team aware. This presents an additional risk surrounding completeness.

37.58 The engagement team should ask management for a facilities letter from each bank, which should list all services provided to the audited entity by that bank. Engagement teams can then obtain further details form management and send confirmation letters using those details

37.59 If a facilities letter is not available, the engagement team should ask management what facilities the banks provide and use professional scepticism on the integrity of management, judgement and additional procedures to determine whether this is a complete disclosure, adding to the Letter of Representation.

37.60 Depending on the outcome of risk assessment procedures, the engagement team should consider whether confirmation is needed in relation to additional information such as trade finance transactions and balances or information about guarantees and other third-party securities, in addition to the confirmation of balances and other banking arrangements usually provided in such a request.

External confirmations – Government Banking Service accounts

37.61 In accordance with paragraph 19 of ISA (UK) 330 (Revised July 2017) (Updated May 2022), the NAO has considered centrally whether external confirmation procedures are to be performed as substantive procedures in respect of bank accounts held by audited entities with the Government Banking Service (GBS) and concluded that external confirmation procedures are not required for these accounts. This judgement is informed by an assessment that the inherent risk associated with GBS accounts is low, because the scope of services provided by the GBS to each audited entity is

limited and potentially higher-risk facilities (such as loans and securitisations) are not provided by the GBS. FAPQ confirms these arrangements with contacts at HM Treasury and the GBS on an annual basis; this confirmation was last received in April 2023.

37.62 The GBS is not considered to be a service organisation in scope of ISA (UK) 402 (Updated May 2022) *Audit considerations relating to an entity using a service organisation*. Whilst the GBS provides a single banking service across government, it does not undertake any banking or operate any controls surrounding banking accounts operated by government entities, which each individually retain a direct relationship with the individual providers of GBS bank accounts (i.e., banking institutions). Paragraph 8(e) of ISA (UK) 402 (Updated May 2022) defines a service organisation as a third-party organisation (or segment of a third-party organisation) that provides services to user entities that are part of those entities' information systems relevant to financial reporting. The services that are part of the information systems relevant to financial reporting of entities with GBS accounts are provided by the banks with which the accounts are held, rather than GBS itself, which merely has an oversight and facilitation role for government cash management. Those banks are themselves not service organisations, since paragraph 5 of ISA (UK) 402 (Updated May 2022) specifies that the standard does not apply to services provided by financial institutions that are limited to processing, for an entity's account held at the financial institution, transactions that are specifically authorised by the entity.

37.63 As a result of the risk assessment set out above, direct bank confirmations are not required for accounts managed by the GBS. Evidence to confirm year end balances is available from the year end statements and online facilities provided by the banks. Online statement facilities have the functionality to provide statements at a specified point in time and all audited entities have the ability to access these online facilities.

37.64 The GBS does not provide loans or require securitisations as part of their banking relationships. Authorised overdraft facilities are only provided in exceptional circumstances where it has been explicitly authorised by HM Treasury. The GBS has exchequer management processes in place to ensure action is taken to review any set of accounts that is in a net overdraft position (which may be, for example, because of bank charges applied to the account or delays in receipt of funds from the sponsor department), as paragraph A5.6.7 of Managing Public Money requires that public sector organisations should never go overdrawn. In the event of a very high value overdraft, Government Banking Service staff work with departmental and HM Treasury contacts to bring the account back into credit and put in place measures to prevent a reoccurrence (which may include penalty interest charges levied by HM Treasury). These processes are described in more detail in the following paragraph. Engagement teams therefore have inherent assurance that GBS balances are complete and there are no other interactions with these accounts which require reporting in the financial statements.

37.65 The GBS's exchequer management processes are described in more detail below:

- A report is taken at the beginning of every banking day to confirm all customer and Government Banking control/journal accounts are overdrawn. The whole report is referred to Government Banking leadership team members.
- If an overdrawn account is part of an agreed departmental set of accounts which is in a net credit position, then no action is taken.
- If an overdrawn account is part of an agreed departmental set of accounts which is in a net debit position, or is not part of an agreed departmental set of accounts, then the following action is taken:
    - All overdrawn amounts are reviewed and specific actions are taken. Amounts below £100 are typically made up of account charges applied by the bank.

- The Government Banking Customer Team will investigate reason by telephoning the customer to establish a satisfactory reason or escalate within customer or department depending on scale (see Vote account exception below).
- These actions are reported back to the Customer Leadership Team and the Senior Risk Lead and picked up the following day by monitoring to confirm clearance.
- Exceptionally, an account may be overdrawn more than a day because of a delay in receipt of central funds from the parent department. Where this happens, the Government Banking Customer Relationship Manager will monitor activity and manage the issue directly with the customer, keeping the Customer Leadership Team and the Senior Risk Lead apprised.
- In the event that there is a very high value overdraft and the Customer Relationship Manager is unable to contact the department, a senior member of the Government Banking team will approach their equivalent in the department to understand and resolve the debt. High values are usually a result of an accounting error rather than actual spend.
- In the event that the overdrawn account is a Vote (Supply) account, the Government Banking Customer Team will refer the position to HM Treasury for their immediate follow up. HM Treasury will arrange for the account to urgently be brought back into credit and request an explanation as to what caused the overdraft and what measure can be implemented prevent a reoccurrence. HM Treasury can charge penalty interest on overdrawn positions in accordance with paragraphs A5.6.7 and A5.6.8 of Managing Public Money.

- Government Banking Control/Journal accounts are reviewed by Government Banking personnel multiple times per day and at the start of each day. These reviews are performed by confirming that the balances are equal and opposite to those shown in Bank of England accounts. Any discrepancy (either debit or credit) is investigated and specifically reported to the Senior Risk Lead, who then oversees action to correct the discrepancy.

37.66 Teams auditing year-end GBS accounts should:

- obtain a listing of bank accounts held by the audited entity at the year-end date;
- observe the audited entity logging in to those accounts using their online access and confirm there are no other accounts showing online and note down the balances as at the period end date;
- enquire and corroborate with others at the audited entity as to whether the list of accounts provided covers all banks providing GBS services that are used by the entity (this could involve ensuring, for instance, that the list does not include only Citibank accounts if the entity also has GBS accounts with another bank);
- vouch year-end bank balances recorded in the bank reconciliation to the year-end statements provided by GBS for all accounts held;
- vouch the information in the GBS statement to online statements for Citi and RBS accounts; and
- re-perform the year-end bank reconciliation (if adopting a substantive approach).

External confirmations – negative confirmations

37.67 In most circumstances where confirmations are appropriate, they should be positive confirmations. Negative confirmations are only appropriate in limited circumstances which are uncommon among the NAO's audit portfolio.

37.68 Engagement teams should not use negative confirmation requests as the sole substantive audit procedure in respect of an assertion unless all of the conditions set out in paragraph 15 of ISA (UK) 505 (Updated May 2022) apply.

37.69 Any decision to use negative confirmations should be made by the Engagement Director and the justification for doing so clearly documented within the audit file. In particular, the audit

documentation should set out clearly how each of the preconditions in paragraph 15 of ISA (UK) 505 (Updated May 2022) are met.

External confirmations – management refuses to allow the auditor to send a confirmation request

37.70 Paragraphs 8 and 9 of ISA (UK) 505 (Updated May 2022) and the related application guidance set out how the auditor should respond where management refuses to allow the auditor to send a confirmation request, including where the auditor concludes this refusal is unreasonable.

37.71 The engagement team may conclude based upon these procedures that it is necessary to revise the assessment of the risks of material misstatement.

External confirmations – evaluating evidence obtained

37.72 Paragraphs 10 to 14 and 16 of ISA (UK) 505 (Updated May 2022) and the related application guidance set out how the engagement team should evaluate the results of external confirmation procedures, including whether the results of the external confirmation procedures provide relevant and reliable audit evidence, or whether further audit evidence is necessary.

37.73 An oral response to a confirmation request does not meet the definition of an external confirmation because it is not a direct written response to the NAO. It is usually possible to request a confirming party who has given an oral response to put the response in writing directly to the NAO.

37.74 If the engagement team is unable to obtain a written confirmation, they should seek other audit evidence to support the information in an oral response.

37.75 If there are doubts about the reliability of information intended to be used as audit evidence, the engagement team should determine whether to modify or add procedures to resolve those doubts.

37.76 If the team determines that a response to a confirmation request is not reliable, evaluate the implications on the assessment of the risks of material misstatement, including the risk of fraud, and on the related nature, timing and extent of other audit procedures (ISA 505.11). This may lead to the identification of additional significant risks or modification of planned procedures in response to other risks.

37.77 The engagement team should consider whether non-responses are indicative of previously unidentified risks of material misstatement, and if so revise the audit plan accordingly, reflecting this in the Risk Assessment in Apex and other planning documentation as appropriate.

37.78 The engagement team should consider carefully the relevance and reliability of the evidence provided before planning to use confirmations to obtain assurance over regularity.

37.79 The engagement team should document the decision of whether to use external confirmations, and the basis for the decision. The confirmations themselves should, where practicable, be saved within the Apex audit file.

Inventory

37.80 Inventories include:

- materials or supplies to be consumed in the rendering of services;

- stockpile goods and military reserve inventories;
- confiscated, seized and forfeited property;
- goods held under price support programmes;
- assets held for sale in the ordinary course of business;
- assets in the process of production for such sale;
- materials or supplies to be consumed in the production process; and
- development property stock.

37.81 Paragraphs 4 to 8 of ISA (UK) 501 (Updated May 2022) and the related application guidance include requirements for the auditor to obtain sufficient appropriate audit evidence regarding the existence and condition of inventory; they cover matters relating to physical inventory counting, alternative procedures and circumstances where inventory is under the custody and control of a third party. Where the engagement team is unable to attend the year-end physical inventory count due to unforeseen circumstances, they may perform a count at an alternative date and follow the procedures set out in paragraphs 5 and A9 to A11 of ISA (UK) 501 (Updated May 2022).

37.82 Where engagement teams rely on controls over ownership, they will need to evidence how they are satisfied the control was effective in providing assurance that counted inventory did not include items owned by third parties. Engagement teams will also need to evidence how the control relied on covers all inventory items.

37.83 The matter of difficulty, time, or cost involved is not in itself a valid basis to omit an audit procedure for which there is no alternative or to be satisfied with audit evidence that is less than persuasive.

37.84 Engagement Directors and Engagement Managers should consider carefully whether the engagement team members (including contractors) attending physical inventory counts have the necessary skills, knowledge and experience to perform the planned procedures, especially when inventory is specialised in nature. The engagement team should consider appointing an NAO expert to assist in the audit of complex inventory balances (see Section 12: Use of experts).

37.85 The nature of inventory means that there are particular challenges over obtaining sufficient, appropriate audit evidence, in particular with respect to existence and valuation.

Inventory – attending physical inventory counts and performing test counts

37.86 Paragraphs A1 to A8 ISA (UK) 501 (Updated May 2022) set out how the auditor should obtain sufficient appropriate audit evidence regarding the existence and condition of inventory by attendance at physical inventory counting, unless impracticable, in accordance with paragraph 4(a).

37.87 The engagement team may decide to employ a rotational approach to visiting the entity's sites to attend the stocktakes by visiting different locations in different years. Where such an approach is adopted, the engagement team will need to evidence why they are satisfied the control operated effectively across all sites, including sites not tested or sites that are maintained by different entities.

37.88 Where a sampling approach is used in testing valuation, the engagement team will need to consider how the sample represents the population across all sites and can be used to draw conclusions on the valuation of inventory as a whole.

37.89 If valuation is only tested at sites visited on a rotational basis, some items may not have a chance of selection and may be excluded for the population used to select a sample. Where an audit sampling approach is adopted, each item should have a chance of selection in order to provide the engagement team with a reasonable basis on which to draw conclusions about the entire population.

Inventory – physical inventory counting conducted other than at the date of the financial statements

Paragraphs A9 to A11 of ISA (UK) 501 (Updated May 2022) set out how the auditor should respond where the physical inventory counting may be conducted at a date, or dates, other than the date of the financial statements.

Inventory – attendance at physical inventory counting is impracticable

37.90 ***Consultation required*** Paragraphs A12 to A14 of ISA (UK) 501 (Updated May 2022) set out how the auditor should respond where attendance at physical inventory counting is impracticable. The engagement team should consult FAPQ if such a situation arises.

Inventory – inventory under the custody and control of a third party

37.91 Paragraphs A15 to A16 of ISA (UK) 501 (Updated May 2022) set out how the auditor should obtain assurance over inventory that is under the custody and control of a third party.

Inventory – other matters regarding inventory

37.92 Depending upon the nature and complexity of the inventory and inventory system in an entity, the engagement team may need to test the operating effectiveness of IT systems used as part of controls over existence and valuation of inventory.

37.93 The quality of the audit assurance obtained from attending inventory counts is increased through:

- performing analytical procedures to identify anomalous stock holdings or patterns, and following up on these through the physical inventory counts;
- assigning more experienced staff to higher risk inventory balances;
- planning testing to incorporate an element of unpredictability as to which locations will be visited (to reduce the risks of counts being performed particularly carefully at locations the engagement team visit);
- avoiding informing management (or allowing them to identify) which stock lines have been counted (to avoid the risk of fraudulent adjustments to stock lines which have not been counted by the engagement team); and
- ensuring that the contents of boxes, crates, etc. are inspected (to ensure that they are genuinely full).

Litigation and claims

37.94 Paragraphs 9 to 10 of ISA (UK) 501 (Updated May 2022) and the related application guidance set out how the auditor should design and perform audit procedures in order to identify litigation and claims involving the entity which may give rise to a risk of material misstatement and, where necessary, either seek direct communication with the entity's external legal counsel or perform alternative audit procedures.

37.95 Audit evidence about the status of litigation and claims up to the date of the C&AG's report may be obtained by inquiry of management, including in-house legal counsel, responsible for dealing with the relevant matters. In some instances, the engagement team may need to obtain updated information from the entity's external legal counsel.

37.96 In accordance with paragraph 11 of ISA (UK) 501 (Updated May 2022), the CA&G's audit report would be modified if:

- management refuses to give the engagement team permission to communicate or meet with the entity's external legal counsel, or the entity's external legal counsel refuses to respond appropriately to the letter of inquiry, or is prohibited from responding; and
- the engagement team is unable to obtain sufficient appropriate audit evidence by performing alternative audit procedures

37.97 Payments arising from litigation and claims are generally not in accordance with Parliamentary intention, and so may be irregular. Engagement teams should consider whether the expenditure is irregular, and whether the irregular transaction has crystallised at the reporting date.

37.98 The engagement team should enquire of management and those charged with governance whether there are any material litigation or claims and communicate with management and those charged with governance in respect of significant litigation and claims as part of communications about significant accounting estimates and fair value measurements.

37.99 The letter of representation should include representations about the completeness of liabilities reflected in the financial statements, and about the significant assumptions used in valuing any litigation and claims.

37.100 Litigation and claims can be complex and highly judgemental. Engagement Directors and Engagement Managers should ensure that the team members auditing these areas have the appropriate skills, knowledge and experience to do so. The Engagement Director and Engagement Manager will also typically be involved in discussions with management, those charged with governance and potentially external legal counsel about material litigation and claims.

37.101 ***Consultation required*** Where appropriate, the NAO may need to consult with the Office's own legal counsel with respect to litigation and claims. Engagement teams should initially consult FAPQ if they consider that this might be required, and if necessary obtain legal advice through the Legal and Policy team.

37.102 The nature of litigation and claims means that there are particular challenges over obtaining sufficient, appropriate audit evidence, in particular with respect to completeness of liabilities. Liabilities for litigation and claims are usually accounting estimates.

37.103 Depending on the circumstances, the engagement team may judge it appropriate to examine related source documents, such as invoices for legal expenses, as part of the team's review of legal expense accounts.

37.104 Other information it may be appropriate to consider includes:

- media reports;
- general public and stakeholder feedback;
- other information obtained by regulators, officials, public prosecutors, or other investigative agencies;
- information from complaints officials and whistleblowers; and

- outcomes of wider NAO reports.

37.105 Direct communication with the entity's legal counsel assists in obtaining assurance over both the completeness of the liabilities, and whether management's estimates of the financial implications, including costs, are reasonable.

37.106 However, this will usually not be the engagement team's sole source of assurance. The valuation of liabilities for litigation and claims should be assessed in accordance with the guidance in Chapter 36: Accounting estimates.

37.107 If management has provided for a liability on the basis of the advice from their lawyers (acting as management's expert), the engagement team should consider whether their work represents sufficient appropriate audit evidence.

37.108 In some circumstances, engagement teams may need to use our own lawyers as an NAO expert to evaluate their work, which can be arranged through the Legal and Policy team. Engagement teams may initially consult with FAPQ if believe this audit approach is necessary.

37.109 In the UK, solicitors typically will only respond to specific inquiries, following guidance from the Law Society. A letter making specific inquiries should include:

- a list of litigation and claims;
- where available, management's assessment of the outcome of each of the identified litigation and claims and its estimate of the financial implications, including costs involved; and
- a request that the entity's external legal counsel confirm the reasonableness of management's assessments and provide the engagement team with further information if the list is considered by the entity's external legal counsel to be incomplete or incorrect.

37.110 In certain circumstances, the engagement team also may judge it necessary to meet with the entity's external legal counsel to discuss the likely outcome of the litigation or claims. This may be the case, for example, where:

- litigation or claims have been identified as a significant risk;
- the matter is complex; and/or
- there is disagreement between management and the entity's external legal counsel.

37.111 Ordinarily, such meetings require management's permission and are held with a representative of management in attendance.

37.112 Although unlikely to apply in the UK, if law, regulation or the respective legal professional body prohibits the entity's external legal counsel from communicating directly with the NAO, the engagement team should perform alternative audit procedures.

Segmental information

37.113 Paragraph 13 of ISA (UK) 501 (Updated May 2022) and the related application guidance include requirements on the auditor to obtain sufficient appropriate audit evidence regarding the presentation and disclosure of segment information in accordance with the applicable financial reporting framework, while also ensuring that the segmental information is not materially inconsistent with the rest of the accounts.

37.114 The FReM requires the presentation and disclosure of segmental information. The objective of IFRS 8 is to require an entity to disclose information to enable users of its financial statements to

evaluate the nature and financial effects of the business activities in which it engages and the economic environment in which it operates. IFRS 8 applies in full for entities applying the FReM. ISA (UK) 501 (Updated May 2022) requires specific procedures to audit these disclosures.

37.115 The procedures performed are only required to provide assurance in the context of the financial statements as a whole: i.e. that it is in line with the applicable financial reporting framework and not materially inconsistent with other areas of the accounts – the engagement team do not need to obtain sufficient assurance to form an opinion on the segment information on a standalone basis.

37.116 The application of methods used by management in determining segment information can be tested by selecting some items (groupings of transactions and balances) within the segmental information and ensuring they have been classified reasonably.

37.117 The segmental information should reconcile to the underlying accounting records, i.e. the TB, and explanations obtained and assessed for reasonableness where there are reconciling items.

37.118 Usually, the information will be that presented to the senior management or other relevant decision makers in a public sector context.

37.119 Analytical procedures may involve, for example, summing all income / expenditure lines in the segmental disclosure and comparing with income / expenditure lines in the primary statements and notes. Examples of other procedures include:

- comparisons with budgets and other expected results: for example, operating profits as a percentage of sales;
- the allocation of assets and costs among segments; and
- consistency with prior periods, and the adequacy of the disclosures with respect to inconsistencies.

37.120 For departments, engagement teams should be aware that inappropriate allocation of income or expenses between segments could potentially disguise a breach of a voted control total.

37.121 The FReM follows IFRS 8 in requiring segments to be defined in accordance with how an entity's operations are managed in practice. Engagement teams should consider whether any of the following circumstances apply where relevant to identifying the reportable segments:

- only one operating segment is reported, but the group appears to be diverse with different businesses or with significant operations in different countries;
- the operating analysis set out in the narrative report differs from the operating segments in the financial statements;
- the titles and responsibilities of the directors or executive management team imply an organisational structure which is not reflected in the operating segments; and/or
- the commentary in the narrative report focuses on non-IFRS measures whereas the segmental disclosures are based on IFRS amounts.

37.122 Teams may also wish to assess the following questions in auditing segmental disclosures:

- What are the key operating decisions made in running the business?
- Who makes these key operating decisions?
- Who are the segment managers (per IFRS 8) and whom do they report to?
- How are the group's activities reported in the information used by management to review performance and make resource allocation decisions between segments?
- Is any proposed aggregation of operating segments into one reportable segment supported by the aggregation criteria in the standard, including consistency with the core principle?
- Is the information about reportable segments based on IFRS measures or on an alternative basis?

- Have the reported segment amounts been reconciled to the IFRS aggregate amounts?
- Do the accounts describe the factors used to identify the reportable segments including the basis on which the company is organised?
- Do the reported segments appear consistent with their internal reporting and, if not, why not?

37.123 No exemption is given from any aspect of IFRS 8 on the grounds that disclosure would be commercially prejudicial.

Section 10: Contracted-out work

Chapter 38: Contracting with partner organisations

Relevant standards and guidance

38.1 Paragraphs 1-7 to 1-11 of Practice Note 10 (Revised 2022) *Audit of financial statements* and regularity of public sector bodies in the United Kingdom provide guidance on applying ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* to contracted-out engagements in the public sector.

38.2 Paragraph 1-207 of Practice Note 10 (Revised 2022) provides guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* to reports by contracted-out auditors to national audit agencies.

Scope of this Section

38.3 The NAO's contracting-out arrangements typically follow one of three models:

- Partner organisations support the NAO by carrying out audit assignments on the NAO's behalf, providing the NAO with an audit opinion on the financial statements, or other outputs as agreed at the commencement of the engagement;
- Partner organisations provide expertise in a range of specialist audit or accounting issues as part of audit assignments, but do not provide an audit opinion on a complete set of financial statements; and
- Partner organisations provide staffing resources who are either experts in matters other than audit or accounting or audit practitioners who can supplement the NAO's own in-house teams at critical points in the audit cycle.

38.4 This Section of the FAM principally contains NAO policies and procedures covering the first two circumstances described in the preceding paragraph.

38.5 This Section also addresses the respective responsibilities for work under the NAO's arrangements with Audit Scotland, Audit Wales and the Northern Ireland Audit Office (NIAO) in circumstances where staff from Audit Scotland, Audit Wales or the Northern Ireland Audit Office (NIAO) are undertaking an audit engagement on behalf of the C&AG using a model similar to that which is applied to contracted-out audit arrangements.

38.6 Where NAO staff are performing an audit engagement on behalf of Audit Scotland, Audit Wales or the Northern Ireland Audit Office, they should follow the policies and procedures set out within this Manual with the exception of the certification process, where the Certification Journal is sent to the relevant Office rather than the C&AG. Letters of Engagement for such arrangements should be included within or as Annexes to the relevant Memoranda of Understanding agreed with these bodies.

38.7 Policies and procedures for situations where external organisations provide the NAO with an expert in a matter other than audit or accounting are set out in Section 12: Use of experts.

38.8 Policies and procedures for situations where other audit organisations audit a component of a group audited by the NAO are set out in Chapter 25: Group audit procedures.

Contracted-out engagements

38.9 Paragraph 1-7 of Practice Note 10 (Revised 2022) defines a contracted-out engagement as an engagement where, although responsibility for issuing the audit report remains with the statutory auditor, all or some of the audit assignment is undertaken by another firm or auditor under contract or agreement. In some cases, the contractor firm or auditor provides a fully ISA-compliant audit report to the statutory auditor. For example, the C&AG contracts out audit work on some statutory appointments but is still responsible for signing the audit certificate and report.

38.10 The NAO's arrangements to contract out a proportion of its work were originally recommended as part of the Sharman review of the NAO in 2001. Since then, the NAO has refined this model over 20 years to contract out a significant proportion of audits to supplier firms that meet quality and service standards defined by the NAO.

38.11 Guidance on current contracting arrangements is available on the Financial Audit Contract pages on Sharepoint.

38.12 Guidance on managing contracted-out audits in Financial Force is available on Sharepoint here.

Quality management for contracted-out engagements

38.13 The NAO has agreed overarching contracts and protocols with contractor firms and other public sector auditors, covering responsibilities and high-level quality management arrangements. The NAO's contract management process considers and addresses quality management matters affecting contractor auditors.

38.14 For contracted-out engagements, responsibility for quality remains with the NAO as statutory auditor. This includes:

- ensuring that the contractor auditor has sufficient personnel with the competencies, capabilities and commitment to ethical principles necessary for compliance with relevant standards;
- confirming that the contractor auditor meets the relevant ethical standards, including independence, on appointment and periodically thereafter;
- ensuring that there are policies and procedures in place to identify and resolve potential conflicts;
- considering whether an internal consultation and the appointment of an engagement quality reviewer is necessary for contracted-out engagements;
- applying NAO-wide quality management arrangements (including, for example, the NAO's quality risk assessment process, governance and leadership responsibilities, relevant ethical requirements and resourcing) to contracted-out engagements;
- including contracted-out engagements within the scope of the NAO's overall quality management arrangements and requirements for direction and supervision of the audit: for example, by:

- the Engagement Director, in the role of Engagement Partner, carrying out appropriate direction, supervision and review and taking overall responsibility for managing and achieving quality (see Chapter 5: Direction and review of the engagement);
- referring technical queries and judgements through the NAO's formal consultation processes where appropriate (see Chapter 6: Technical support and consultation); and
- including contracted-out audits in the scope of audits that are considered for whether they require an engagement quality review (see Chapter 7: Engagement Quality Review), hot review or post-certification inspection review ("cold review") (see Chapter 4: Quality monitoring);

- reporting any deficiencies identified as a result of monitoring a contracted-out engagement to the contractor auditor undertaking the assignment; and
- establishing policies and procedures designed to provide reasonable assurance that complaints and allegations relating to quality are dealt with appropriately (in this context, the relevant policies and procedures are those set out in the section of Chapter 4: Quality monitoring entitled 'Quality monitoring', concerning complaints on the standard of audit work).

38.15 This does not absolve contractor auditors of responsibility for systems of quality management within their organisations. The contractor auditor is considered to be a service provider for the purpose of ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements*. In this context, the contractor auditor may agree to provide the NAO with a report on the system of quality management within their firm (a 'service provider report') to inform the NAO's understanding of the impact of using the service provider on the achievement of its quality objectives. In practice, the NAO either obtains assurance over quality from its contractors or may undertake procedures to confirm that its contractors' systems of quality management are working effectively.

38.16 In considering contractor auditors as service providers under ISQM (UK) 1, FAPQ reviews publicly available information on the quality of the contractor firms (for example Transparency Reports, main Audit Quality Review team (AQR) reports issued by the Financial Reporting Council (FRC), Major Local Audit AQR reports and any outputs from the ICAEW's Quality Assurance Division (QAD). Where relevant matters arise for teams to consider, these will be highlighted to teams using the firms on the Quality Management pages on Sharepoint.

38.17 If the contractor auditor identifies deficiencies in any of its public sector assignments that fall within the remit of the NAO, these are communicated, along with the action undertaken, to the NAO. If the NAO identifies deficiencies in the performance by the contractor auditor of any of its contracted-out assignments, the NAO communicates these to the contractor auditor and determines what actions are required to address these, which may include additional work being performed by the contractor auditor.

Financial Audit Contract and Specialist Audit Services Framework

38.18 The NAO has agreed overarching contracts and protocols with contractor firms and other public sector auditors, covering responsibilities and high-level quality control arrangements.

38.19 The current Financial Audit Contract with relevant firms, signed in Autumn 2021 and covering the 2021-22 cycle onwards, will be in place for a minimum of 3 years, with the option to extend for a further 2 years.

38.20 A Specialist Audit Services Framework is also in place, covering digital, pensions and property expertise.

38.21 ***Consultation required*** If the engagement team considers they require expertise outside the areas covered by the Specialist Audit Services Framework, they should consult FAPQ and the Financial Audit Operations team to discuss options, except that requests for specialist expertise relating to financial instruments should initially be directed to the Financial Instruments Centre of Expertise (who will engage with FAPQ and the FA Operations team as appropriate).

Queries and advice on contracting-out arrangements

38.22 Queries regarding contracting-out arrangements should be directed to the Financial Audit Operations team in the first instance. The Central Procurement Team can also provide advice on contracting issues.

Avoiding conflicts of interest when using contractors for audit work

38.23 Contractors are required to declare any conflicts of interest prior to entering into an engagement under the Financial Audit Contract, the Specialist Audit Services Framework, or another arrangement. The contractor is required to provide a declaration of any conflicts of interest prior to an award being made as part of the procurement process.

38.24 The Financial Audit Contract requires contractor auditors to disclose to the NAO any conflicts of interest which arise, along with their own ethical assessment of the conflicts. In addition to this, contractor firms provide a quarterly declaration of any new conflicts at contract management meetings.

38.25 ***Consultation required*** Any proposals by contractors to provide non-audit services to NAO audited bodies must be discussed with the Director, Audit Operations prior to being submitted to the audited body. Contractor auditors must provide their own ethical assessment of the proposed service to the Director, Audit Operations. In these instances, the engagement team should consult the Ethics Function.

38.26 As part of the engagement team's review of the contracted-out audit file, they should review the ethical section of the contractor's file.

38.27 Conflicts or perceived conflicts of interest should be analysed objectively to see if they can be managed. A conflict or perceived conflict should not necessarily rule out an otherwise attractive contractor firm, because their experience can mean that they are very well placed to carry out effective work for the NAO. For example, in assessing the value for money of a public private partnership, the NAO might seek technical support from a consultant who did work for such partnerships and might therefore be perceived to have an interest in promoting a positive view of them.

38.28 ***Consultation required*** An Engagement Director who wishes to accept and manage an actual or perceived conflict must be prepared to make a robust defence of those situations where they are able to manage a conflict. They should consult with FAPQ, who will advise on the appropriate safeguards to mitigate any actual or perceived conflict of interest.

38.29 In their working relationships with contractors and audited bodies, engagement teams should monitor whether new conflicts are emerging or whether known, managed conflicts are becoming problematic. Equally, engagement teams should be aware of the risk that new conflicts may arise during the contract. During an assignment, and where appropriate for an agreed period of time afterwards, a contractor firm must obtain the NAO's consent before seeking work that would give rise to a conflict. The NAO and contractor firms are obliged to work together to resolve a conflict that emerges. Where a conflict cannot be resolved to the NAO's reasonable satisfaction, the NAO may require the contractor auditor to withdraw from the assignment, or the contractor auditor can decide to withdraw.

38.30 Where contractor auditors engage sub-contractors, they are expected to manage these relationships according to the arrangements set out the contractor auditor's contract with the NAO and to provide the NAO with assurance that they are doing so.

Chapter 39: Role of the contractor auditor

Relevant standards and guidance

39.1 Paragraphs 1-7 to 1-11 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* to contracted-out engagements in the public sector.

39.2 Paragraph 1-207 of Practice Note 10 (Revised 2022) provides guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* to reports by contracted-out auditors to national audit agencies.

Contractual responsibilities of the contractor auditor

39.3 The contractual relationship between the contractor firm and the NAO is set out in the overall Financial Audit Contract or the Specialist Audit Services framework, supplemented where necessary with contractual documentation written specifically for the assignment.

39.4 The contractual responsibilities agreed in one of the ways described above may cover a full audit of financial statements, providing staff to form part of an engagement team, or other specialist support.

Protocols document

39.5 The protocols document sets out the baseline expectations from contractor firms and NAO engagement teams.

39.6 The protocols document for each engagement should be tailored according to the risk profile of the audit and the preferences of the contractor firm and the NAO engagement team. It is recommended that the NAO engagement team, including the NAO Engagement Director, discusses and agrees the protocols document with the firm prior to the start of the audit.

39.7 The document must be signed by the firm's Partner and the NAO Engagement Director at the start of the audit.

39.8 The template protocols document contains matters which te NAO Engagement Director must review to discharge their responsibility as the Engagement Partner. These comprise the minimum items that the NAO Engagement Director should review for the purpose of compliance with ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*.

Key responsibilities of the contractor auditor on a contracted-out financial statements audit

39.9 The contractor auditor is responsible for carrying out a high-quality audit in accordance with the ISAs (UK) and, where relevant (for example, for audits including a regularity opinion), Practice Note 10 (Revised 2022).

39.10 The work should cover all elements of the C&AG's true and fair and, where relevant, regularity opinions, unless agreed otherwise.

39.11 The contractor auditor will draft reports for those charged with governance, including an Audit Planning Report and Audit Completion Report. These should be drafted using NAO templates and be shared with the NAO engagement team for review on a timely basis. The NAO Engagement Director remains responsible for all communications with those charged with governance.

39.12 The contractor auditor is expected to meet the agreed timetable and client engagement approach, which will have been set out in the audit protocols document during planning. Delays outside the contractor firm's control should be discussed with the NAO engagement team and the Financial Audit Operations team.

39.13 The contractor auditor should raise any significant issues identified on the audit with the NAO engagement team at the earliest possibility.

Responsibility for the audit opinion

39.14 Each contractor firm should identify a 'responsible individual' who is the senior representative of the firm, responsible for delivery of the product and for signing the shadow audit opinion provided to the C&AG. In the case of audit firms, this will invariably be the Partner and in the case of other organisations, this will be at Director-equivalent level.

39.15 At the end of the assignment, the 'responsible individual' should provide the Engagement Director with a draft "shadow audit opinion", an Audit Completion Report, Management Letter and other documentation as per the agreed contractual responsibilities (see the section earlier in this Chapter entitled 'Contractual responsibilities of the contractor auditor'). The "shadow audit opinion" issued by the contractor auditor should be based on the relevant audit certificate template and mirror the wording of the audit certificate or report the NAO engagement team propose to issue. The shadow opinion may include a "bannerman" style paragraph on the firm's liability. It should be clearly marked as a shadow certificate (for example, by using the firm's letterhead). The shadow opinion may be signed electronically by the relevant person at the contractor firm.

39.16 In accordance with the arrangements described in paragraph 1-207 of Practice Note 10 (Revised 2022), the contract with the contractor firm (i.e. the Financial Audit Contract) may specify that the firm issues an audit report to the NAO (the "shadow audit opinion"). Under these circumstances, the shadow audit opinion is outside of the scope of ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* and the reporting arrangements will be defined by the contract between the firm and the NAO. The shadow audit opinion issued by the contractor auditor to the NAO reflects the scope of the engagement under the terms of the contract.

39.17 ***Consultation required*** In light of the contractual requirements relating to shadow audit opinions described in the preceding paragraph, the NAO engagement team should consult FAPQ if the contractor auditor proposes to deviate from the standard NAO templates when preparing their shadow opinion, unless the deviation has been previously agreed between FAPQ and the contractor firm.

Contractor firm asked to sign a "hold harmless" letter

39.18 ***Consultation required*** If the audited entity has contracted out the internal audit function to an audit firm, the firm may request that the NAO's contractor firm sign a "hold harmless" letter prior to sharing working papers with them. The NAO engagement team should consult FAPQ in these cases to ensure that the wording of any such letter does not imply a restriction of the C&AG's statutory powers. Further guidance may be found in Section 12: Use of experts.

Chapter 40: Role of the NAO engagement team in contracted-out audits

Relevant standards and guidance

40.1 Paragraphs 1-7 to 1-11 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISQM (UK) 1 *Quality management for firms that perform audits or reviews of financial statements, or other assurance or related services engagements* to contracted-out engagements in the public sector.

40.2 Paragraph 1-207 of Practice Note 10 (Revised 2022) provides guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* to reports by contracted-out auditors to national audit agencies.

Responsibility for the audit opinion

40.3 In all cases of contracted-out audit arrangements, the C&AG retains overall responsibility for the audit of the financial statements and will sign the audit certificate/opinion and report. The NAO Engagement Director, acting on the C&AG's behalf, operates as the 'Engagement Partner' as defined in the ISAs (UK) (in particular, paragraph 12(a) of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*). The engagement team is a joint team consisting of all NAO and contractor firm staff working on the audit engagement.

40.4 It is important for the NAO engagement team to ensure through their involvement and review that, as with any audit, they are satisfied that the work performed supports the C&AG's audit opinion. Although contractor firms may use different methodologies:

- the scope of the NAO engagement team's discussions with the contractor auditor on the audit approach for the entity; and
- the NAO Engagement Director's review of the contractor auditor's file

should be sufficient to determine that the contractor auditor has conducted an ISA-compliant audit. In particular, the NAO Engagement Director must perform a second stage review directly on the firm's audit file with the same scope as if it were an in-house audit following the policies set out in Chapter 5: Direction and review of the engagement. This review should be document within the NAO Apex file which has been set up for the engagement.

40.5 ***Consultation required*** In certain circumstances, the signature of the certificate and report may be delegated to a named NAO Engagement Director. Delegated signature arrangements require approval by the C&AG on the recommendation of the Director, Audit Quality. Further guidance may be found in Chapter 12: Roles, delegations and licences.

40.6 The NAO Engagement Director must ensure they maintain appropriate links with both audited entity and the contractors during the audit, to ensure that the NAO Engagement Director can fulfil their role as the 'Engagement Partner', under the ISAs (UK); in particular, with regard to the direction, supervision and performance of the audit.

40.7 The NAO engagement team should seek to actively engage with both the audited entity and contractors during outsourcing (even on smaller audited entities), both so that there is no ambiguity

that the C&AG and the NAO remains the actively appointed external auditor and so that information can be easily collected for cross-discipline areas of work such as client insight. This should, however, be balanced by an efficient approach.

Responsibilities to be undertaken by the NAO engagement team

40.8 As the Engagement Partner, as defined in the ISAs (UK), the NAO Engagement Director should discharge the key responsibilities of that role. In particular, the NAO Engagement Director has the following responsibilities:

- performing a second-stage review of the contractor auditor's audit file, including within the scope of the review the matters identified as requiring second-stage review as set out in Chapter 5: Direction and review of the engagement, in the same manner as for a review of an in-house audit file, and documenting within the NAO's Apex file evidence that they have discharged these review responsibilities. The Contracted-out Audits Director Review Template sets out the minimum areas which the NAO Engagement Director must review on the contractor firm's file. This template should be used by the NAO Engagement Director to evidence their review of the contractor's file;
- NAO business risk management, including if applicable, audited entity acceptance risks;
- reviewing annually the risks associated with the audited entity and its business, including changes to the engagement risk profile, management integrity and other factors that might impact on the risk assessment and audit responses;
- establishing an NAO engagement team with appropriate skills and experience to manage the contracted-out audit (this includes consideration of roles and responsibilities, as well as the extent and timing of deployment); and
- engaging with the contractor auditor and agreeing protocols for the relationship.

40.9 At the start of each engagement, the Engagement Director should undertake and document an assessment of the level of engagement required by NAO staff. A template form is available to document this assessment. The level of direct NAO involvement will vary from engagement to engagement. This assessment must be informed by:

- a robust understanding of the business and of the results of previous audits;
- knowledge of the key engagement risks and audit risks arising;
- an awareness of the strengths of the contractor auditor's engagement team (however, this should not negate the need for the contractor auditor to provide a suitable team); and
- maintaining regular contact with the audited body.

40.10 Whilst the level of NAO involvement will vary from engagement to engagement, there are a number of procedures that are required to be carried out by the Engagement Director. These are:

- completing the Engagement Risk Assessment Audit Form;
- attendance at the main audit planning meeting and the engagement team discussion on risk and fraud;
- approving the significant risks identified and the audit responses to these;
- consideration of the need for an Engagement Quality Review;
- agreement of the Audit Planning Report (or equivalent) and Audit Completion Report (or equivalent) prepared by the contractor auditor;
- agreement of protocols for client management, including attendance at audit committees;
- performing a second-stage review of the contractor auditor's audit file, as described above;
- review of the annual report and financial statements (which should take into consideration the detailed points raised by the contractor auditor); and

- agreement of conclusions.

40.11 The template protocols document contains matters which the NAO Engagement Director must review to discharge their responsibility as the Engagement Partner. These comprise the minimum items that the NAO Engagement Director should review for the purpose of compliance with ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*. The NAO Engagement Director should include evidence of the NAO Engagement Director's personal review of the contractor auditor's file within the Contracted Out Audits - Review of firm audit work Audit Response Group in Apex.

40.12 In addition to the mandatory NAO Engagement Director procedures, there are a number of other procedures that may be completed for each contracted-out audit. The NAO Engagement Director, having considered their responsibilities and the risks associated with the audit (including the results from the Engagement Risk Assessment Audit Form) and the assessed level of NAO involvement required, should determine and document the timing and level of NAO involvement and the extent of the NAO Engagement Director's review. This should be completed during the planning stage of the audit and should be continually reassessed during the course of the audit; the assessment should be documented in the relevant template.

40.13 The NAO engagement team should aim to focus their input on the more significant aspects of the audit, particularly significant risks and areas such as regularity with which contractor firms' staff may be less familiar. The NAO engagement team should not repeat the contractor auditor's detailed first-stage review.

40.14 Contractor firms engaged under the Financial Audit Contract should be familiar with the requirements for the audit of regularity. However, as this is a less common feature of the work for those firms than for the NAO, Engagement Directors may wish to consider the work performed on regularity more closely than other testing.

40.15 The NAO Engagement Director should ensure that they review significant judgements made by the contractor auditor and challenge of these, including the risk assessment process and the evidence obtained for significant estimates. The contractor auditor's audit file should contain sufficient evidence for the significant judgements. The NAO Apex file should evidence the NAO Engagement Director's challenge of the contractor auditor's judgements.

40.16 ***Consultation required*** The NAO Engagement Director is required to consider the need for an Engagement Quality Review in accordance with Chapter 7: Engagement Quality Review. The NAO Engagement Director cannot fulfil that role, as they are not independent. An EQR may be required even if the contractor firm has employed an independent partner review. In the event an NAO Engagement Director considers that an EQR is required, they should consult FAPQ. The NAO engagement team and the contractor auditor should each make their own determination of whether an EQR would be an appropriate response to quality risks on a contracted-out engagement. A relevant consideration for both the NAO and the contractor auditor in making this determination is whether the other party plans to appoint an EQR for the engagement. The NAO engagement team should therefore discuss with the contractor auditor their respective proposals for any EQR, with a view to a single EQR being appointed for the engagement.

40.17 ***Consultation required*** The NAO Engagement Director should use the same criteria as for an audit performed by NAO staff when deciding whether it is necessary to consult with FAPQ. Even if the contractor auditor has consulted their firm's technical team, consultation with FAPQ is still required where it would be for an in-house audit. If the contractor auditor has consulted their firm's technical team, FAPQ will take this into account when providing advice. If the contractor auditor or NAO Engagement Director are considering proposing a modified audit certificate or report, the NAO engagement team should consult FAPQ. Where the NAO engagement team consults FAPQ, the query submitted should reflect the consensus view of the engagement team (i.e., NAO staff and the contractor firm as a joint team), having been agreed with the contractor firm and after any internal consultation process considered appropriate by the contractor auditor partner. If there is an irreconcilable difference of opinion between the NAO engagement team and the contractor auditor, the submission to FAPQ should describe the situation and include specific details of the NAO engagement team's attempts to reach a joint position.

40.18 The contractor firm must first discuss with the NAO Engagement Director before consulting on any matters outside of the engagement team. The nature and scope of any such consultation with those outside of the engagement team must be agreed with the NAO Engagement Director before the contractor firm undertakes the consultation.

40.19 The NAO Engagement Director should confirm with the contractor auditor that they have complied with relevant ethical standards and whether there are any reportable matters under ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements* and/or ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector*. If there are any such reportable matters, the NAO engagement team should refer to Chapter 31: Consideration of laws and regulations and reporting to regulators.

Liaison between the NAO engagement team and the contractor auditor

40.20 ***Consultation required*** If substantive differences arise between the NAO engagement team and the contractor auditor that cannot be resolved, the NAO engagement team should consult FAPQ.

40.21 The NAO engagement team should liaise with the contractor auditor at regular points throughout the audit.

40.22 ***Consultation required*** At the end of the process, the NAO Engagement Director should meet with the 'responsible individual' to review the performance of the audit and to identify lessons learned for the NAO and for the contractor auditor. Performance issues should also be communicated to the Director, Audit Operations and the Director, Audit Quality in a timely manner and prior to settlement of the final invoice.

Contractor auditor responsible for a component of the overall audit

40.23 ***Consultation required*** Any proposal by the NAO engagement team to amend the scope of the contractor auditor's work such that the contractor auditor would be completing less than a full ISA-compliant audit (i.e., scoping out elements of the engagement) should be submitted to FAPQ for

approval. FAPQ may approve such an arrangement on an ongoing basis or subject to re-assessment for each reporting period.

40.24 Where an NAO engagement team is relying on a contractor auditor to undertake work on a component of an audit or to test specific areas, the responsibility for the audit remains with the Engagement Director.

40.25 Where the contractor auditor is testing a geographical or operational component of an overall audit, the NAO engagement team should:

- agree clearly the contractor auditor's role in the engagement;
- ensure that the NAO engagement team have discussed with the contractor auditor staff the significant risks and other information relevant to their work, including the outcome of the engagement team discussion on fraud;
- set the scope of their work as part of our audit plan;
- supervise them as the engagement team would supervise any other NAO team performing testing at a discrete location/component;
- the NAO Engagement Director should directly review the work of the contractor firm on their file and evidence this review within the NAO's Apex file.

40.26 Where a contractor auditor is responsible for the audit of, for instance, a non-departmental public body being consolidated into a department's accounts, the paragraph above is not applicable to the group audit. ISA (UK) 600 (Revised September 2022) *Special considerations – audits of group financial statements (including the work of component auditors)* and Chapter 25: Group audit procedures apply in these circumstances.

40.27 Where the contractor auditor is performing testing in specified areas, the NAO engagement team should:

- clarify with the contractor auditor what the NAO engagement team wishes to achieve from their work;
- discuss with the contractor auditor the significant risks and other information relevant to their work;
- agree a clear scope of work which is mutually agreed to achieve the planned assurance;
- review the findings of work done; and
- ensure that the scope of the work done by NAO engagement team reflects the scope of the contractor auditor's work.

Communication and documentation requirements

40.28 The level of the NAO engagement team's expected or planned involvement should be made clear to both the audited entity and to the contractor auditor at the outset. It is particularly important to keep the audited entity informed of the arrangements and to ensure that they have a clear understanding of the respective responsibilities and lines of communication. It is also important to ensure that the audited entity fully understands that the C&AG remains as the appointed auditor and that the contractor auditor is working on behalf of the NAO.

40.29 All formal written communication with the audited entity, such as the Audit Planning Report, Audit Completion Report and Management Letter, should be presented in the standard NAO formats and be approved by the Engagement Director. It may be jointly badged. Written representations

should be addressed to the C&AG and must include all representations contained within the NAO template, although firms may elect to include further representations as appropriate.

40.30 The Apex workflow for contracted-out audits contains Audit Responses designed to ensure that the NAO's own documentation demonstrates that the NAO Engagement Director has undertaken appropriate direction, supervision and review of the engagement. The Contracted-out Audits – Director Review Template sets out the minimum areas of the contractor's file which must be reviewed by the NAO Engagement Director.

40.31 The NAO engagement team should include the contractor auditor's shadow opinion within the certification journal, either as a physical copy or electronically.

40.32 Paragraph 6(b) of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* defines the 'audit file' as one or more folders or other storage media, in physical or electronic form, containing the records that comprise the audit documentation for a specific engagement. For contracted out audits, the audit file consists of the combined contents of the NAO's Apex audit file and the contractor auditor's working papers – these combined constitute the folders containing the records that comprise the audit documentation for the engagement. The Apex audit file should also document the work performed by the NAO engagement team to support the C&AG's audit opinion.

40.33 The contractor auditor's working papers and the NAO audit file should, between them, contain sufficient and appropriate documentation to understand the work performed by the contractor auditor and the NAO respectively.

40.34 Taken together, the contractor's file and the NAO audit file will evidence the engagement team's compliance with the requirements of the ISAs (UK). The contractor auditor's working papers should not be duplicated on the NAO's Apex file.

40.35 As the NAO Engagement Director fulfils the role of the Engagement Partner for contracted-out audits, the nature, timing and extent of their involvement should be sufficient to fulfil the Engagement Partner's obligations, including appropriate direction, supervision and review of the engagement. The NAO Engagement Director's personal review should extend to:

- the determination of materiality under ISA (UK) 320 (Revised June 2016) (Updated May 2022) *Materiality in planning and performing an audit;*
- documentation of decisions made surrounding the deployment of resources, including any judgements surrounding whether significant expertise is required on the audit;
- the decision to involve an auditor's expert, include the scoping of the work of such expert and the output of their work;
- the contractor firm's evaluation of the work of auditor's experts and the conclusions drawn therefrom;
- the contractor firm's risk assessment process, including situations where consideration of inherent risk factors and the assessment of inherent risk requires significant judgment by the contractor firm;
- the contractor firm's consideration of related party relationships and transactions and disclosures;
- the results of any detailed testing relevant to significant risks;
- the contractor firm's consideration of any significant judgments (including any requests by the contractor firm's team to consult technical teams, or equivalent, within the contractor firm);
- the results of testing on any accounting estimates with significant estimation uncertainty;

- the results of the firm's consideration of going concern;
- the results of the firm's review of the entity's accounting policies;
- the results of the firm's consideration of any new accounting standards;
- the results of testing on any particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements, for which the engagement team has determined the materiality level or levels to be applied in accordance with paragraph 10 of ISA (UK) 320 (Revised June 2016) (Updated May 2022);
- (for group audits):
    - the proposed group audit strategy and group audit plan;
    - decisions about the involvement of component auditors, including how to direct and supervise them and review their work, including, for example, when there are areas of higher assessed risk of material misstatement of the financial information of a component; and
    - the evaluation of work performed by component auditors and the conclusions drawn therefrom;
- the results of the firm's review of the annual report and financial statements;
- any ethical matters considered by the contractor auditor;
- evidence of partner review by the contractor auditor;
- a copy of any overall summary of the audit work performed; and
- the overall evaluation of identified misstatements.

40.36 The Contracted-out Auditors – Director Review template will assist the NAO Engagement Director in documenting their review of these matters. This template sets out the matters that the NAO Engagement Director must perform a second stage review upon as a minimum in order to fulfil their responsibilities for review under ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*.

40.37 Where the contractor auditor is undertaking specified testing on behalf of the NAO, their working papers are formally part of the audit file..

Section 11: Specialist areas

Chapter 41: Parliamentary Supply

Relevant standards and guidance

41.1 Paragraph 2-35 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* includes guidance that, in the context of regularity in central government in the United Kingdom, the auditor may consider material any expenditure incurred in excess of the amounts authorised by Parliament.

41.2 Chapter 34 of Erskine May's treatise on the law, privileges, proceedings and usage of Parliament (25th edition, 2019) sets out Parliamentary procedures relating to public expenditure and supply.

Background

41.3 The supply process is the link between the financing of central government and the annual financial statements produced by government departments. The government requests funds annually in Supply Estimates for each department in line with the current Spending Review; Parliament then votes on these Supply Estimates and the key elements of the Estimates are embodied in law in Supply and Appropriation Acts. In doing so, Parliament sets the spending limits in different categories for each department which are known as voted control totals. Parliament also approves the purposes for which resources, capital and cash may be used by approving the ambit of each department.

41.4 Departmental financial statements include a Statement of Outturn against Parliamentary Supply (SOPS) which reports the outturn for the financial year against each of the voted control totals. The SOPS is derived from the other financial statements within departmental financial statements, such as the Statement of Comprehensive Net Expenditure (SoCNE). It is the key statement for financial accountability purposes with Parliament. As such there are additional considerations when auditing departmental financial statements or other accounts of Parliamentary Supply.

41.5 To support the SOPS summary tables, a number of additional notes are produced, including:

- SOPS1: Analysis of net outturn by Estimate Subhead, in two parts:
    - SOPS1.1: Analysis of net Resource outturn by Estimate Subhead, showing separately Administration and Programme gross expenditure and income, and compared to the Voted and Non-voted amounts in the Estimate plus virements; and
    - SOPS1.2: Analysis of net Capital outturn by Estimate Subhead, showing separately gross expenditure and income, and compared to the Voted and Non-voted amounts in the Estimate plus virements;
- SOPS2: Reconciliation of net Resource outturn to net operating expenditure;
- SOPS3: Reconciliation of net Resource outturn to Net Cash Requirement;

- SOPS4: Analysis of income due to the Consolidated Fund, in two parts:
    - SOPS4.1: Analysis of amounts payable to the Consolidated Fund, consisting of income outside the ambit of the Estimate and excess cash surrenderable to the Consolidated Fund (required only if non-budget income has arisen during the year); and
    - SOPS4.2: Disclosure of income collected by the entity as an agent of the Consolidated Fund (required only if such income has been collected and the entity does not prepare a Trust Statement).

Parliamentary control totals set as part of the Supply and Estimates process

41.6 The format of the SOPS includes the totals voted by Parliament for a given department. The voted control totals are as follows:

- the net Resource Departmental Expenditure Limit (DEL) requirement;
- the net Capital DEL requirement;
- the net Resource Annually Managed Expenditure (AME) requirement;
- the net Capital AME requirement;
- the net Non-budget requirement; and
- the Net Cash Requirement for the Estimate as a whole.

41.7 These totals can be found in the relevant Supply and Appropriation Act. They are supported by the Estimates themselves, which contain further details including limits imposed by HM Treasury in addition to the Voted control totals.

41.8 As the totals voted by Parliament are on a net basis, it is possible for them to be negative. That is, a department may be expected to generate a level of income in excess of its gross expenditure.

The annual Supply process

41.9 In summary form, the annual cycle of Supply and Appropriation for a typical financial year is as follows:

- April: Government departments' spending plans (Main Estimates) are published.
- June/July: Supply resolutions authorising the Main Estimates are approved; Supply and Appropriation (Main Estimates) Bill passed.
- July: Government departments lay their Annual Reports and Accounts (for the financial year ending the previous March) before Parliament.
- October/November: the Budget is presented, which can include proposed spending changes for the current or future financial years.
- February: Government departments' revised spending plans for the current financial year (Supplementary Estimates) are published.
- February/March: Supply resolutions authorising Supplementary Estimates, Votes on Account for the next financial year, Defence Votes A for the next financial year and Excess Votes for the previous financial year are approved; the Supply and Appropriation (Anticipations and Adjustments) Bill is passed.

41.10 ***Table 41A*** below summarises the key steps in the annual cycle covering spending for a single financial year. Each of the Estimates is given effect through a Supply and Appropriations Bill.

Table 41A: Annual Supply process

Action	Timing	Example timing in respect of 2021-22 Supply	Description
Vote on Account (VoA)	Around February immediately before the financial year.	February 2021	Parliament provides interim funds to cover the first few months of the year. Parliament does not authorise expenditure for which authority is sought by the Main Estimates until after the start of the financial year to which the Main Estimates relate. It is therefore the established practice, during one financial year (usually in February), to seek authority for some provisional allocation of amounts for the financing of the public service during the next financial year, pending Parliamentary approval of the corresponding Main Estimates. Accordingly, special Estimates are presented seeking 'Votes on Account', which comprise total amounts for resources and cash to cover the needs of the Government and the independent services, for the first three or four months of the financial year, until final authority can be given by the passage into law of the Supply and Appropriation (Main Estimate) Act. The Votes on Account for the coming year normally contain a standard provision to advance amounts equivalent to 45% of the resources and cash which were previously voted for each Estimate for the current year. Greater or lesser amounts may be sought where there has been a transfer of responsibility between departments, where allocation of resources and cash is expected to be significantly different in the early months of the coming financial year, or where expenditure will be incurred for a new service.
Main Estimates	First and second quarters of the financial year.	April to September 2021	Parliament provides formal approval of funds for the whole financial year. The Main Estimates set out the use of resources and the grants of cash which will, during the financial year to which the Estimates relate, be required to make financial provision for the civil and defence services, and five independent services (the House of Commons Administration, the National Audit Office, the Electoral Commission, the Independent Parliamentary Standards Authority and the Local Government Boundary Commission for England).

			Each Ministerial and non-Ministerial department has a single Estimate, but they are all presented in a single volume (other than those of the independent services). Departmental Estimates include the spending plans of the relevant government department and also those of any other central government body (such as NDPBs) for which the department has responsibility.
Supplementary Estimates	Fourth quarter of the financial year.	February to March 2022	Parliament approves changes requested by departments (this is the last opportunity to change a department's control totals for the financial year). A substantive Supplementary Estimate may be presented either: • for authorisation of further amounts in respect of an existing service, in addition to the amounts already sought for the current financial year; or • for authorisation of further amounts required for a fresh object of expenditure the requirement for which has arisen since the presentation of the Main Estimates, such as the costs of providing a service newly provided for in statute, or the requirement to deal with an unexpected emergency. Supplementary Estimates contain the ambit of the Estimate affected, amended as necessary to take account of any new services, together with a statement of the changes to the spending limits for which authorisation is sought. Supplementary Estimates may also seek to reduce previously agreed spending limits where it is known that funding previously requested is no longer required.
Committee of Public Accounts (PAC) report on excess amounts	If possible, in February or early March of the financial year following that in which the excess occurred, but in any case after the accounts	February to March 2023	Following completion of the audit, Government seeks Parliament's retrospective approval for any breaches of control totals. The need for an Excess Vote arises when a department has incurred expenditure or other use of resources upon an existing service beyond the amounts authorised for it during the financial year in question, or where there is no proper parliamentary authority for the service. When the exact amount of the excess expenditure or other use of resources has been ascertained on completion of the audit, the C&AG makes a report to the House of Commons (the audit report published along with the departmental accounts). The findings come before PAC,

	are laid before Parliament		which, after an examination of the explanation provided by the relevant department, submits its own report to the House, setting out the reasons and stating the objections (if any) to the excess being approved.
Statement of Excesses	As soon as possible after the report from the Committee of Public Accounts has been agreed.	March 2023	HM Treasury presents a Statement of Excesses, which takes the form of a combined request for amounts of resources and cash to make good the aggregates of excess expenditure or other excess use of resources on the various Estimates affected.
Supply and Appropriation (Anticipations and Adjustments) Bill	Following presentation of the Statement of Excesses.	March 2023	Parliament authorises and appropriates individual excess amounts.

41.11 The Supply and Appropriation (Main Estimates) Act provides legal authority to spend provision included in the Main Estimates. The Act is passed after the start of relevant financial year, normally in the summer prior to Parliamentary recess. Provision for the early months of the financial year is provided through a 'Vote on Account' which is customarily set as 45% of the prior year control total. In theory, departmental spending should not exceed the resource, capital and cash limits set out in the 'Vote on Account' until the Main Estimate gives legal authority for further spending. However, if a department did exceed these limits, the excess spending would be regularised retrospectively by the subsequent Estimate – this would therefore only be an issue for the regularity opinion in the highly unlikely event that Parliament failed to provide authority for any further spending under the subsequent Estimates.

41.12 During the financial year, departments may seek amendment to voted control totals by way of a Supplementary Estimate. There is only one Supplementary Estimate per financial year and this receives legal authority, together with the 'Vote on Account' for the next financial year, shortly before the financial year-end in the Supply and Appropriation (Anticipation and Adjustments) Act.

41.13 Departments do not recognise a receivable in their accounts in respect of amounts included in the Vote on Account that are expected to be received in the following financial year. This is because:

- the future receipts of cash that such a receivable would relate to will not be recognised as income, but rather will be credited to the General Fund (a component of taxpayers' equity) in accordance with the FReM (paragraph 7.5.2 of the 2022-23 FReM); and
- there is uncertainty associated with the future receipts: the Vote on Account provides authority for spending (meaning such spending will be in accordance with the framework of authority and therefore regular) but is not a cash allocation for the period and there is no certainty that the

department will draw down the full amount of the Vote on Account. UK-adopted international accounting standards do not envisage recognition of a contingent asset unless the realisation of 'income' is 'virtually certain' (paragraphs 31 and 33 of IAS 37) and the Vote on Account does not meet the definition of a financial asset (paragraph 11 of IAS 32) as it does not give rise to cash, equity instruments or contractual rights on the part of the department.

41.14 Main and Supplementary Estimates in respect of future years that are published before financial statements are authorised for issue are not treated as adjusting events after the reporting period under IAS 10, since they do not provide evidence of conditions that existed at the end of the reporting period. The Estimates for future years are not published until the financial year they relate to (as the Vote on Account covers the initial months of the year – see the preceding paragraph) and no authority is given to spend under these Estimates until Parliament has approved them. There is no income or receivable to recognise in respect of future years for the same reasons as with the Vote on Account, and since the Estimates give authority for spending in the year they are published, they do not give rise to expenditure or payables relating to the preceding financial year, which would be that subject to any adjustment for an event after the reporting period.

41.15 Parliament also has other means of authorising expenditure in limited circumstances, including the Contingencies Fund, Votes of Credit and exceptional grants.

Other control totals set as part of the Supply and Estimates process

41.16 The Supply Estimate also includes subhead detail which disaggregates the voted limits (on a net basis) by category, by gross expenditure and income. The Resource element of the Departmental Expenditure Limit is also split into administration and programme limits. The sum of all the administration subheads is the Administration Cost Limit, which is disclosed on the SOPS.

41.17 Each individual subhead i.e. each cell in Part II of the Supply Estimate, is an individual limit. A limit has been exceeded if the outturn figure is greater than the estimate figure. This means that failing to meet an income figure in the estimate is a breach of that individual limit. Departments have been delegated the authority to perform virement of the expenditure budget in certain circumstances. These are detailed in the Supply Estimates Manual.

Consequences of exceeding limits set in the Supply process

41.18 The audit of the SOPS and associated notes is particularly relevant to the opinion on regularity. If the SOPS has been properly prepared from the underlying records, it will be evident whether any control totals have been breached (either voted totals or totals subject to HM Treasury control, breaches of both of which result in irregular expenditure).

41.19 However, at the time of certification, the excess expenditure remains irregular. The C&AG qualifies his regularity opinion for all breaches of voted totals, regardless of the amount of excess.

41.20 If a department exceeds its Administration Cost Limit it is usually treated in the same way as a breach of a voted total. Although the Administration Cost Limit is not in itself voted by Parliament, HM Treasury does not have delegated authority to reallocate voted resources to increase it. Any breach will, therefore, be reported to Parliament through the Statement of Excesses when Parliament will be asked to either grant additional provision or to vire from an underspend elsewhere.

The C&AG will therefore usually qualify his regularity opinion for a breach of the Administration Cost Limit.

The ambit

41.21 The ambit of a vote is a description of the services or purposes to which expenditure and income can be applied. It can be found in Part I of the Supply Estimate. It is included in the relevant Appropriation Act and is therefore subject to Parliamentary control.

41.22 Any expenditure or income of a department which is not included within the ambit is outside Parliament's authority and therefore irregular. Spending on services or activities outside a department's ambit should result in Parliament being asked to regularise the amount of irregular expenditure by a subsequent vote. If spending on services or activities outside a department's ambit is material (considering context as well as value) it will lead to a qualification of the C&AG's opinion on regularity.

41.23 Ambits can be varied as part of a Main Estimate or a Supplementary Estimate. There are many reasons for these changes, but the most common are to recognise formal and on-going departures from the Consolidated Budgeting Guidance, to recognise new activities or to allow HM Treasury to exercise control over specific types of transactions within a department. Ambits are also amended following a Machinery of Government change to departmental responsibilities.

Main responsibilities

41.24 The engagement team should obtain sufficient appropriate audit evidence that the SOPS and its related notes are properly prepared and presented in accordance with the FReM. This includes the reclassification of transactions and specific adjustments for known misalignments between budgets, estimates and accounts, following the principles set out in the Consolidated Budgeting Guidance and the Supply Estimates Manual.

41.25 The engagement team should review the reported results against the voted limits authorised by the Supply and Appropriation Acts for that year and consider the reporting implications should any limit be exceeded. Excess Votes will normally result in the qualification of the regularity opinion.

41.26 The engagement team should consider whether transaction streams are within the ambit of the department; any resource expenditure, capital expenditure or income which is not included in the ambit is irregular. The ambit of the vote also covers the expenditure of Arm's Length Bodies within the departmental boundary as defined by the latest Government Resources and Accounts (Estimates and Accounts) Designation Order.

41.27 ***Consultation required*** Any potential qualification arising from a breach of a voted limit or transactions occurring outside the ambit of the vote must be evaluated and referred to FAPQ.

Planning procedures

41.28 Planning procedures should include documentation of the skills and experience of the team in relation to Supply. Sufficient consideration should be given to the need for further training or

support the team may require to complete the engagement in line with our engagement risk management practices.

41.29 As a minimum, engagement team members auditing or reviewing completed work on the SOPS should be familiar with the NAO Disclosure Guide, Resource Accounts Consistency Checklist and the relevant HM Treasury guidance (including the Consolidated Budgeting Guidance and the Supply Estimates Manual).

41.30 Following the process set out in Chapter 17: Risk assessment and response planning, engagement teams for departmental audits should use the Risk Assessment in Apex to identify the risks of material misstatement associated with the following classes of transactions, account balances and disclosures (COTABDs) relating to Supply:

- transactions related to drawdowns of Supply from the Consolidated Fund or of amounts issued from the Contingencies Fund or from the National Loans Fund, which are credited to the General Fund, as shown in the Statement of Changes in Taxpayers' Equity;
- year-end payable or receivable balances relating to Supply issued from the Consolidated Fund and/or amounts issued from the Contingencies Fund and/or the National Loans Fund;
- Consolidated Fund Extra Receipts (CFER) and the associated year-end receivable or payable balances; and
- amounts disclosed in the Statement of Cash Flows relating to Supply issued from the Consolidated Fund and/or amounts issued from the Contingencies Fund and/or the National Loans Fund and those relating to CFERs.

41.31 Because the SOPS is included within the Accountability Report and is not part of the financial statements, it is treated as part of the Statutory Other Information, the responsibilities relating to which are set out in ISA (UK) 720 (Revised November 2019) (Updated May 2022) *The auditor's responsibilities relating to other information* and Chapter 32: Other information and other reporting responsibilities. Consequently, in relation to the preparation of the SOPS (as distinct from Supply-related COTABDs, which are covered in the preceding paragraph), the engagement team is not required to undertake the risk assessment process under ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* that is set out Chapter 17: Risk assessment and response planning.

41.32 The engagement team should consider the risk of breaching voted or Treasury totals and how this affects the overall risk assessment performed within the Risk Assessment in Apex. The potential for limits to be breached, resulting in a qualified regularity opinion, will almost certainly affect the assessment of the risk of management perpetrating financial statement fraud through the override of management controls. Fraud risk factors, which are Generic Inherent Risk Factors within the Risk Assessment in Apex, address these considerations – further guidance on identifying fraud risk factors is provided in Chapter 30: Fraud responsibilities.

41.33 Other Generic Inherent Risk Factors within the Risk Assessment in Apex that are applicable to audits of departmental accounts reflect the potential complexity and subjectivity associated with judgements around the classification of transactions that may impact outturn against control totals reported in the SOPS.

41.34 The standard Apex content for departmental accounts include Audit Responses that address risks that the SOPS is not properly prepared, such as the risk of improper reconciling items between

comprehensive net expenditure and net resource outturn and risks associated with complex models used to derive figures reported in the SOPS.

41.35 Group engagement teams should consider how they will obtain sufficient, appropriate audit evidence from components to support the departmental SOPS. The Group Audit Instructions should include the procedures component auditors are expected to perform on consolidation submissions and details about how any potential issues impacting supply should be communicated to the departmental engagement team. If the group team has identified a significant risk relating to Supply or if particular control total issues or treatments are a concern, then this information should also be communicated to component audit teams.

Audit procedures

41.36 The SOPS is a derived statement, based upon the same financial reporting data that is assured through normal audit procedures on the financial statements.

41.37 As illustrated by ***Figure 41B*** below, the NAO's standard testing approach relies upon the assurance gained from the financial statement testing and builds upon it to provide assurance over the SOPS and the related notes.

Figure 41B: Derivation of the SOPS and NAO assurance

41.38 Similarly, to evaluate the impact of misstatements, errors in the financial statements need to be considered for their impact on the SOPS, along with any misstatements identified during SOPS-specific testing.

41.39 The main elements of SOPS testing are set out below in the order the engagement team may wish to approach them.

- The department will have a process for mapping trial balance data into the format of the SOPS and related notes. The engagement team should ensure that this mapping process correctly classifies income and expenditure (including capital) against the correct Parliamentary control total and Estimate sub-line. This may be a combination of budget holder or cost centre and accounts codes as well as manual adjustments. This process results in the detail presented in SOPS1.1 and SOPS1.2.
- The mapping process will require manual adjustments to account for the differences in treatment between accounts and Estimates. These adjustments should be audited and checked for completeness against the list of known misalignments in the FReM.
- The SOPS compares Estimate amounts with outturns. The engagement team should confirm that the Estimate amounts accurately reflect the format and contents of the Supplementary Estimate.
- Other procedures can then be completed on the related SOPS notes in line with the standard testing procedures in Apex and the key requirements of the Resource Accounts Consistency Checklist, ensuring completeness and consistency with the financial statements.

41.40 ***Consultation required*** The engagement team should consult FAPQ where they consider that modifications to Apex content specific to departmental accounts may be required to provide substantive assurance over the classification and regularity of transactions for SOPS purposes.

41.41 The engagement team should complete the NAO FReM Disclosure Guide, which contains detailed advice on the disclosure issues associated with the proper presentation of the SOPS and its related notes. It must be completed for each departmental resource account.

41.42 The engagement team should evaluate the explanations of variances between outturn and estimate as presented in the SOPS and the section outturn note (SOPS1) to confirm whether the explanations are appropriate and meaningful.

Breaches, errors and reporting

41.43 ***Consultation required*** Breaches of a voted control total are irregular because they breach Parliamentary authority. Subsequently, Parliament will be asked to retrospectively regularise the expenditure by a vote in an Appropriation Act. The engagement team should refer all breaches or potential breaches to FAPQ.

41.44 A department may exceed more than one control total. Where this is the case, the C&AG's qualified regularity opinion will refer to all of the totals which have been breached and Parliament will be asked to regularise each individual excess by voting on the relevant Appropriation Act.

41.45 ***Consultation required*** Where unadjusted misstatements have been identified that, if adjusted, would cause an Excess Vote, engagement teams should consult FAPQ. Whilst the SOPS may be properly prepared based on a set of true and fair financial statements, such errors may be indicative of management override of controls. Therefore, whether such situations would result in a modified regularity opinion is a matter of judgement for the C&AG. The C&AG would also consider on a case-by-case basis whether misstatements that are potentially indicative of management override of controls should be treated as material for the purpose of the true and fair opinion on the financial statements in light of the qualitative considerations arising from management's actions: i.e., the implications of such actions for the perceived integrity of management may influence the decisions taken by users of the financial statements.

41.46 In addition, where a Parliamentary control total has been exceeded, requiring a subsequent Excess Vote, the engagement team should inform the Exchequer Section within the NAO.

41.47 Where there is a breach of control total, this will need to be reported to those charged with governance with the engagement team's assessment of the cause of the breach. Individually significant SOPS misstatements should also be reported.

Other considerations

41.48 Restatements of the SOPS and related notes are rare. Restatements should only be undertaken where a material machinery of government change has occurred and both departments are undertaking a restatement. Immaterial SOPS restatements should not be undertaken: these are not compliant with the Consolidated Budgeting Guidance. Prior period adjustments to the financial statements that have an impact on Supply outturn should be reflected in in-year Non-Budget Expenditure, rather than through a restatement of the SOPS prior year comparatives.

41.49 The engagement team should document the work performed in sufficient detail to enable an experienced auditor, having no previous connection with the audit, to understand the nature, timing and extent of the procedures performed and their results.

41.50 FAPQ may select and review resource accounts as part of a central quality process which will include a review of the SOPS and related notes. Central FAPQ reviews of accounts are covered in more detail in Chapter 54: Overall conclusions and preparing the certificate or report under the section entitled 'Quality assurance processes during completion'.

Chapter 42: Companies

Relevant standards and guidance

42.1 Parts 16 and 42 of the Companies Act 2006 include provisions on the audit of companies and on statutory auditors.

42.2 The Companies Act accounting rules are set out in the following Statutory Instruments, as amended by subsequent regulations:

- for small companies, the Small Companies and Groups (Accounts and Directors' Report) Regulations 2008; and
- for large and medium-sized companies, the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

Background

42.3 The C&AG is able to audit companies under Section 1226 of the Companies Act 2006. The companies audited by the C&AG fall into two categories:

- Those bodies listed on a legislative order made by HM Treasury under the Government Resources and Accounts Act 2000 (GRAA), which has the effect of appointing the C&AG as auditor. Section 482 of the Companies Act exempts companies listed on such an order from the Companies Act audit regime, provided that they are not-for-profit entities and that the balance sheet contains a statement by the directors above the signature that the company is exempt from the requirements of Part 16 of the Companies Act under Section 482 (as required by Section 475 of the Act). Whilst the C&AG signs under the authority of the GRAA, the rest of the Companies Act still applies.
- Those companies that are responsible for deciding who to appoint as their auditors and are agreement audits acquired either as the result of a successful tender or a request from the company. Sections 1226-1238 of the Companies Act make the C&AG eligible for appointment to audit any company under the standard statutory audit regime, but on the condition that individuals responsible for conducting work on the C&AG's behalf are qualified as statutory auditors in the normal way. In practical terms, in the reserved area of audit, this means the relevant Director holding a Practicing Certificate from their accountancy institute.

42.4 The first category (GRAA company audits) are usually performed under the relevant client director, and the audit report is signed by the C&AG. In most respects these audits are similar to our audits of standard NDPBs and, of the two types of company, a regularity opinion is most likely to be provided on these entities.

42.5 The second category of company audits generally have a greater number of differences compared to other NAO engagements and, therefore, this Chapter covers these specific differences (i.e., it is primarily for the performance of audits governed solely by the Companies Act).

42.6 A listed entity is defined as an entity whose shares, stock or debt are quoted or listed on a recognised stock exchange or are marketed under the regulations of a recognised stock exchange or other equivalent body. In the UK, this includes any company in which the public can trade shares, stock or debt on the open market, such as those listed on the London Stock Exchange (including those admitted to trading on the Alternative Investments Market) and ISDX Markets. It does not

include entities whose quoted or listed shares, stock or debt are in substance not freely transferable or cannot be traded freely by the public or the entity.

The company register

42.7 Companies House is an essential source of information for company audits, including annual returns, the company memorandum and articles of association, the details of directors' company directorships, certificates of incorporation and share capital and the company's registered address. Information from the company register can be viewed on the Companies House website. However, as it is the act of a company itself filing with Companies House that effects any changes, the company register alone is not an adequate source of audit evidence.

Accepting a company audit for the first time

42.8 Chapter 9: Engagement acceptance (statutory and non-statutory) contains detailed guidance on the NAO's business risk management policy for taking on new audit audited entities and engagements and should be considered together with this Chapter. This risk management framework is supported by various required due diligence procedures. However, there are particular distinctions in the process for Companies Act audits of which engagement teams should be aware.

42.9 For Companies Act audits, the directors or members of the company appoint the C&AG and, in doing so, they will need to agree to the terms set out in the letter of engagement. Where prospective audit entities request significant modification to the terms set out in the NAO's letter of engagement template, the engagement team should consider the implications for the conduct of the audit and whether or not to accept the engagement. Where appropriate, the engagement team may consult FAPQ.

42.10 The directors of a company may approach the NAO to tender for appointment as auditors. The NAO would consider submitting a tender when;

- the company audit fits with the NAO strategy;
- there are available resources, for the length of the appointment, to take on the audit;
- the NAO is competent and ethically fit to perform the audit; and
- acceptance of the engagement does not expose the NAO to inappropriate risk.

42.11 The engagement team should complete key due diligence procedures before submitting a tender, making an informed decision about the likelihood of accepting the audited entity and engagement before submitting a tender. These should include specifically:

- checking, through review of the accounts and audited entity interviews, that there are no specialist account areas beyond the NAO's competence;
- determining whether any previous audit opinion was modified and what risks any underlying issues pose for the following period's audit;
- reviewing other available information, including the Companies House annual return, published information and company articles in order to gather standing information on the company's key shareholders, connected companies, employees, customers and suppliers, and determining the impact of this information on the engagement risk;
- ***Consultation required*** if a regularity opinion has been requested, discussing the implications with the line director and FAPQ; and

- contacting the predecessor auditor (in accordance with ISA (UK) 300 (Revised June 2016) (Updated May 2022) *Planning an audit of financial statements*) to ensure that they have formally resigned, and obtaining information on the circumstances around their resignation, including whether there are any relevant matters of which the NAO should be aware before accepting the engagement.

42.12 The engagement team should complete the additional due diligence considerations required for Companies Act audits relating to money laundering regulations (see Chapter 30: Fraud responsibilities).

42.13 The engagement team should ensure that all risks identified through engagement risk management are addressed as the audit, if accepted, is planned and performed.

42.14 If the company also meets the definition of a Public Interest Entity, the engagement team should refer to Chapter 45: Public Interest Entities for the additional requirements in respect of the audit.

Engagement acceptance for company audits

42.15 When the NAO are accepting a new company audit, the relevant Engagement Director and Engagement Manager should consider carefully what the engagement team wish to learn from a review of the predecessor auditor's files, and what they plan to do with the information obtained.

42.16 While review of predecessors' files can be informative, it is important that the engagement team consider the acceptability of the entity as an audited entity and the risks of material misstatement in the audit based upon the NAO's own work.

42.17 Further considerations relating to engagement acceptance are set out in Section 5: New engagements and standing information.

Performing a company audit for the first time

42.18 If applicable, the engagement team should request access to the predecessor auditor's working papers. The Companies Act requires auditors to grant access to, but not copies of, working papers to their successor. Review of a predecessor auditor's working papers can:

- inform the due diligence work required before formally accepting an audited entity;
- inform the risk assessment procedures during planning; and
- inform the engagement team's work to gain assurance over opening balances.

42.19 The engagement team should consider requesting copies of working papers in respect of low risk audited entities, as this may be more cost-efficient than visiting the predecessor auditor's offices to access this information.

42.20 If predecessor auditors charge the direct costs of extracting and providing access to relevant working papers, the NAO should pass such costs onto the audited entity. Predecessor auditors may not include a profit element in such charges.

42.21 Where it becomes necessary to make a formal request under the Companies Act, the engagement team may contact FAPQ.

42.22 The engagement team should enquire with the predecessor auditor if they are aware of any identified or suspected instances of non-compliance with laws and regulations of which they should be aware.

42.23 When taking on an engagement for the first time and this is not the first period of account, the engagement team should gather sufficient appropriate evidence in respect of opening balances, following the requirements of ISA (UK) 510 (Revised June 2016) *Initial audit engagements – opening balances*. Further guidance is available in Chapter 29: Comparative information.

42.24 Where appropriate, the engagement team should take assurance from the work of the predecessor auditor to obtain evidence over opening balances. The engagement team should apply judgement in assessing whether further work is required, which may be appropriate if, for example, there are concerns over the previous auditor's integrity, competence or objectivity, or the previous auditor issued a modified audit opinion.

42.25 Where the prior year financial statements were unaudited, the engagement team should, in accordance with paragraph 6(c) of ISA (UK) 510 (Revised June 2016) *Initial audit engagements – opening balances* and the associated application guidance, either evaluate whether audit procedures performed in the current period provide evidence relevant to the opening balances or perform specific audit procedures to obtain evidence regarding the opening balances (which should include reconciliation to the opening position, review of accounting records, and review of deeds or third-party confirmations). Paragraphs A6 and A7 of ISA (UK) 510 (Revised June 2016) provide further guidance on procedures that may be appropriate.

Licences, training and support

42.26 Under the NAO's engagement risk management procedures, Engagement Directors are responsible for ensuring that the appointed team is capable and competent to carry out the audit. Due to the specialist nature of company accounts, the Engagement Directors and Engagement Managers auditing these accounts are required to apply for a Companies Act licence on an annual basis, following the process set out in Chapter 12: Roles, delegations and licences. This applies to both companies audited under the GRAA and those audited under the Companies Act. For audits of charitable GRAA companies, a Charities SORP licence should be applied for instead of a Companies Act licence. Staff signing off Companies Act audits as the Senior Statutory Auditor must be appointed as a Responsible Individual by the ICAEW.

42.27 The Engagement Director and Engagement Manager should also consider as part of establishing the overall audit strategy whether it is necessary to provide particular training or support to engagement team members to enable them to perform an efficient and effective audit of a company.

Key legal and governance context for companies

42.28 A company is defined as an association of people for common objects which, following registration under the Companies Act, acquires a separate legal personality from that of the individuals that carry out its business.

42.29 As a result of this separation, the legal liability of a company's members (for example, in the event of the company being wound up) is described as "limited". Companies can be limited:

- "by shares", so that the members' maximum liabilities on winding-up would be the amount remaining unpaid on their issued shares; or
- "by guarantee", where the maximum liability consists of a nominal amount agreed by the members on incorporation.

42.30 Companies limited by guarantee are not normally able to distribute profits to their members, so are usually not-for-profit organisations.

42.31 Companies with share capital can be bought and sold and can distribute profits as dividends to their shareholders from eligible reserves. This structure is therefore more suitable where a company operates with a view to profit.

42.32 Companies can be set up by Departments or subsidiary public bodies either as "limited by guarantee" or "limited by shares".

42.33 Subject to satisfying certain criteria, companies limited by guarantee can also be registered charities. In addition to complying with the Companies Act, companies registered as charities should, as required by the Charities Act 2011, apply the Charities SORP. Chapter 43: Charities provides guidance on the audit of charities.

42.34 Section 482 of the Companies Act only allows not-for-profit companies to be made subject to compulsory C&AG audit by GRAA orders. HM Treasury has deemed that only companies limited by guarantee can be designated as not for profit and therefore be eligible for inclusion on such orders. These companies will usually be audited by teams under the relevant client directors on the authority of the GRAA, though in all other respects the company remains subject to the Companies Act.

42.35 Government companies limited "by shares", as well as all those limited by guarantee not included in the GRAA order, are not obliged to engage the C&AG as their auditor but may do so. The Companies Act, rather than the GRAA, is the basis for such audits.

42.36 For private companies, the directors appoint the first auditor, and the shareholders (also known as 'members') can appoint or reappoint an auditor each year. They can do so at a meeting of shareholders, or by ordinary resolution, within 28 days of the directors sending the accounts to the members. If members do not exercise this right, the auditor remains in office until a resolution is passed to remove or reappoint them. This does not apply if the auditors were appointed by the directors or if the company's articles require an annual appointment.

42.37 Members can appoint auditors at their discretion as long as the auditor is eligible for appointment: i.e. the auditor is a member of relevant supervisory body (such as the ICAEW) and is eligible for appointment under the rules of that body. Following from this, there is a requirement for the senior individual on audits performed under the Companies Act to hold a Practicing Certificate. Therefore, all NAO audits of non-GRAA companies are performed under one of the Companies Act

directors, who must be eligible for appointment as a statutory auditor to perform the audit on the C&AG's behalf, in accordance with Section 1227 of the Companies Act. These directors sign the audit report "for and on behalf of the C&AG" as senior statutory auditor, the term applied by Section 504 of the Companies Act to the individual responsible for signing on the firm's behalf (analogous to engagement partners in private firms). The C&AG is then referred to as the statutory auditor, where a private sector auditor would insert the firm's name on the audit report. For GRAA companies, the C&AG will sign the audit report personally as statutory auditor, for which appointment he is eligible under Section 1226 of the Companies Act.

42.38 Under the Companies Act, the board of directors is the collective authority for the running of the company. Directors' powers are subject to restriction by the articles of association and by specific action taken by the members.

42.39 Directors are also subject to a series of statutory duties; in addition to various specific duties, they must discharge a set of general duties now fully codified in Sections 170 to 181 of the Companies Act. The engagement team should keep these duties in mind when undertaking the overall risk assessment. If the directors breach any of these requirements, the engagement team should consider what action is required, including the impact on the engagement team's assessment of inherent risk factors and their understanding of the entity and its environment and system of internal controls. Teams should also consider the need to report on non-compliance with laws and regulations where it is in the public interest to do so under ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements*. Further guidance may be found in Chapter 31: Consideration of laws and regulations and reporting to regulators.

42.40 The Companies Act specifies that the board of directors approve the annual accounts which should be signed by a director of the board on their behalf.

42.41 If the sponsoring department (or other party) appoints an Accounting Officer to the company, engagement teams should note that, as an officer established by HM Treasury with no basis in the Companies Act, an Accounting Officer cannot sign:

- the balance sheet of the financial statements of a company, unless they are also a director of the company; or
- the director's report, unless they are also a director of the company or the company secretary

42.42 Often, where companies are consolidated into a departmental group account, the Principal Accounting Officer at the department will appoint an officer of the company to be an Accounting Officer. It is not necessarily the case that if an Accounting Officer is appointed then the company is required to comply with Managing Public Money. The Accounting Officer appointment letter should be explicit about the conditions and requirements attached to the appointment so that the framework of authorities for the entity is clearly understood.

42.43 A company's articles, passed by special resolution, initially on incorporation, specify its governance framework beyond the high-level provisions of the Companies Act itself. They form, to the extent allowed by the Act, an agreement between the company and its members which is binding on both parties under contract law. The combination of these articles and the company's memorandum of association (sometimes referred to as "Mem & Arts") with all extant resolutions passed in general meetings is referred to as the company's constitution.

42.44 A copy of the articles should be:

- kept as standing information on the Apex audit file;
- kept up to date for any amendments, which can be made at any time by special resolution of the company's members; and
- kept in view by the engagement team, as these contain the key details of the reporting and regulatory framework which applies to the company.

42.45 It is quite possible that the parent entity will have specified some non-standard terms in the articles, such as instructions on how the Board must be constituted or modifications to the default division of powers between shareholders and directors.

42.46 The company's articles may affect how the engagement team engage with management and those charged with governance, as well as potentially informing the risk assessment (for example, determining whether any liability might arise as a result of a breach and thus affect the 'true and fair' opinion).

42.47 Since the articles are, in effect, a legal contract, the engagement team should consider them in the context of ISA (UK) 250A (Revised November 2019) (Updated May 2022).

Key financial reporting context for companies

42.48 Company directors must prepare accounts for the company for each of its financial years unless the company is exempt. Subject to certain conditions, a company is exempt from preparing accounts for a financial year if:

- it is itself a subsidiary undertaking;
- it has been dormant throughout the whole of that year; or
- its parent undertaking is established under the law of any part of the United Kingdom.

42.49 Company directors must also prepare a directors' report for each financial year of the company. However, some of the statutory requirements on content do not apply to companies qualifying for the small companies regime.

42.50 Section 395 of the Companies Act provides a choice to prepare accounts, including disclosure notes, either:

- under UK-adopted international accounting standards; or
- in accordance with Companies Act accounting rules, as laid out in Section 396 of the Companies Act and the supporting statutory instruments:
    - for small companies, the Small Companies and Groups (Accounts and Directors' Report) Regulations 2008; and
    - for large and medium-sized companies, the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

42.51 Companies should present their financial statements in accordance with either:

- IAS 1 *Presentation of financial statements* (for accounts prepared under IFRS);
- one of the permitted formats in Schedule 1 of Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 (for accounts of small companies prepared under Companies Act accounting rules); or

- one of the permitted formats in Schedule 1 of Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (for accounts of non-small companies prepared under Companies Act accounting rules).

42.52 Although companies have a choice of accounting frameworks, and may adopt accounting policies appropriate to their circumstances, some will be consolidated into their sponsoring department's accounts prepared under the FReM. Sponsoring departments may, therefore, request that companies keep a second set of accounting records under IFRS, the FReM and parent department accounting policies.

42.53 Where the Companies Act rules are followed, audited entities should prepare their accounts in accordance with UK GAAP and should explicitly state this in their accounting policies and ensure that the disclosure rules form the relevant statutory instrument are adhered to.

42.54 Under the Companies Act, there is no requirement to adopt IFRS. Company audited entities may choose to adopt IFRS as the basis for preparing their accounts, in some cases in response to shareholder requirements for consolidation accounting.

42.55 Due to the distinct statutory regime applicable to companies, HM Treasury has no direct influence over companies and so the FReM does not apply.

42.56 Although companies may choose to apply the FReM, sometimes at the request of their shareholders, the requirements of the Companies Act will still take priority over the FReM, so only a limited number of FReM adaptations will be applicable. Management must take care to ensure there is an accurate description of the accounting framework in the accounting policy note.

Key financial reporting context for companies – small companies regime

42.57 Company audited entities may be subject to the small companies regime in their first year if they meet certain qualifying criteria (which are set out in Sections 381 to 384 of the Companies Act and summarised in the following paragraph), and in subsequent years if they:

- have met either the prevailing or current qualifying criteria last year and meet the current criteria this year; or
- have met both the prevailing and current qualifying criteria last year (regardless of last year's status).

42.58 The small companies regime applies to a company for a financial year in relation to which the company:

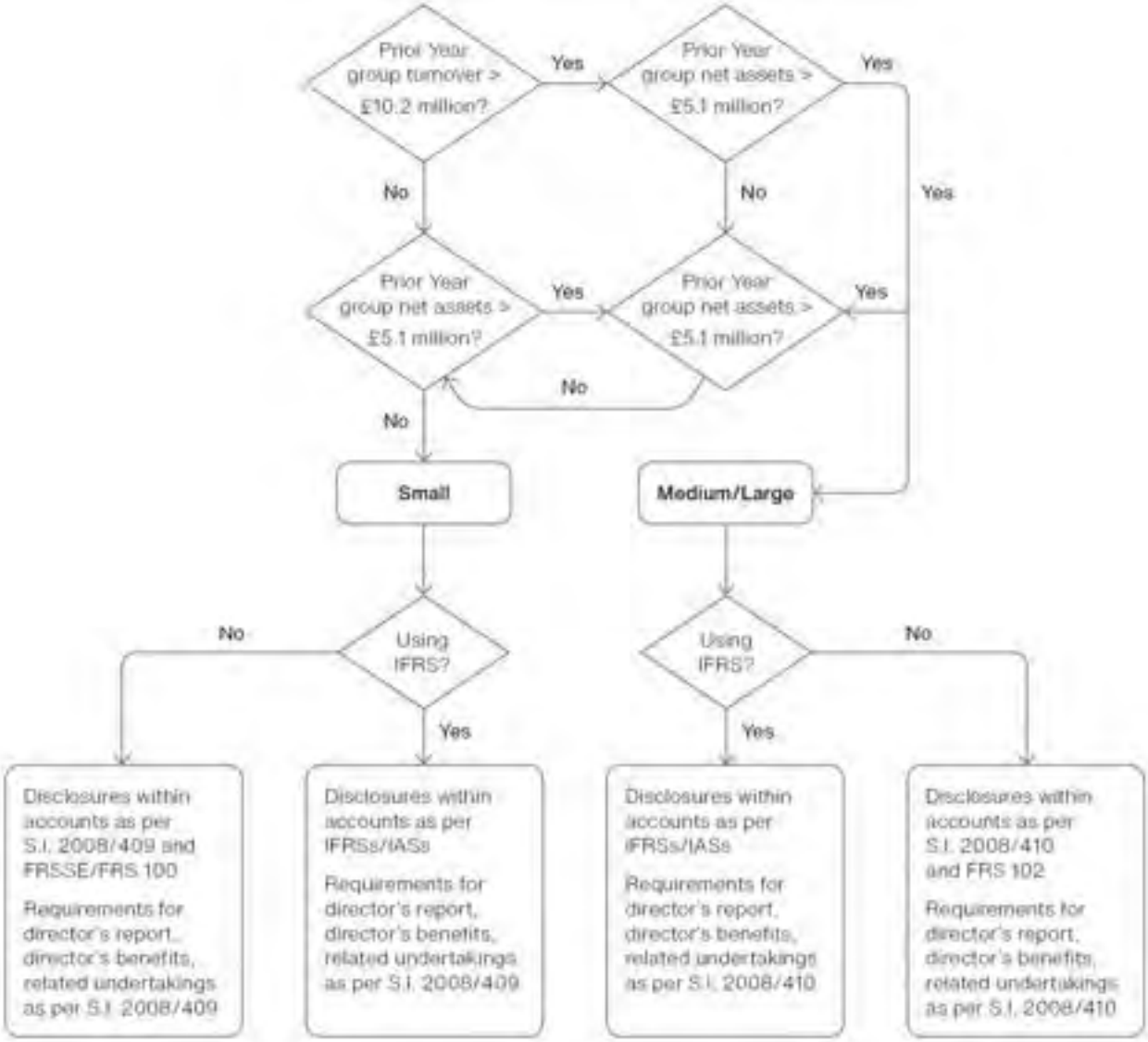
- meets two or more of the following qualifying conditions:
    - the company's turnover is not more than £10.2m (proportionately adjusted if the financial year is not twelve months long);
    - the aggregate of the amounts shown as assets in the company's balance sheet is not more than £5.1m; and
    - the average number of persons employed by the company in the year is not more than 50; and
- is not excluded from the regime by being any of: a public company; a company that is an authorised insurance company; a banking company; an e-money issuer; an MiFID investment firm; a UCITS management company; a company that carries on insurance market activity; or a scheme funder of

a Master Trust scheme within the meanings given by Section 39(1) of the Pension Schemes Act 2017 or Section 39(1) of the Pension Schemes Act (Northern Ireland) 2021; or a member of an ineligible group.

- A parent company qualifies as a small company in relation to a financial year only if the group headed by it qualifies as a small group – the qualifying conditions are set out in Section 383 of the Companies Act.

42.59 If a company qualifies as small and does not apply IFRSs, its minimum disclosure requirements are set out in the Small Companies and Groups (Accounts and Directors' Report) Regulations 2008 and FRS 102 (January 2022) *The financial reporting standard applicable in the UK and Republic of Ireland*. The minimum disclosure requirements for differently sized companies are summarised in ***Figure 42A*** below.

Figure 42A: Minimum accounting and disclosure requirements for companies according to size



Key financial reporting context for companies – directors' report

42.60 Regardless of whether a company follows IFRS or the Companies Act accounting rules, the statutory instruments referred to above contain the minimum requirements for the disclosures included in the directors' report and regarding directors' benefits.

42.61 The Companies Act requires companies to disclose directors' remuneration in the notes to the financial statements. Unlisted companies need not prepare a remuneration report, although if companies do prepare a remuneration report there are differences to the format required by the FReM.

42.62 The disclosure of the director's remuneration in the notes to the financial statements may differ from the disclosure of director's remuneration in the remuneration report due to differences in the definition of director's remuneration between the guidance under which these statements are prepared. Where such a difference occurs, it should be clearly set out and the reasons for it explained within the remuneration report.

42.63 Unlisted companies are not subject to the UK Corporate Governance Code, unless they apply it voluntarily, so the directors are not required to prepare a governance statement under the Companies Act.

42.64 Companies may elect to prepare a remuneration report and a governance statement, or they may be required to produce these reports at the request of a parent department, or other members, as part of preparing FReM-compliant accounts.

Key financial reporting context for companies – applicability of FReM requirements

42.65 Where companies choose to apply the FReM, the following are key differences in terms of allowable accounting policies as compared with the majority of the NAO's audited entities. Breach of any of the following would put the audited entity in breach of the requirements of the Companies Act and might, if judged material, lead to a modification of the audit report:

- Companies cannot recognise and measure assets on the basis of service provision alone; the key consideration per FRS 102 (January 2022) and the Conceptual Framework for Financial Reporting 2018 is whether assets will generate future economic benefits. For example, a company may only capitalise development costs incurred in creating a new database which gives the public access to its services if fees are charged for that service.
- Companies may not recognise notional expenditure.
- Companies must disclose historical cost carrying amounts as per IAS 16 *Property, plant and equipment* or FRS 102 (January 2022) as the exemption under the FReM cannot be exercised.
- The interpretations and adaptations in the FReM around related party transaction disclosures (such as not disclosing the detail of transactions with other government bodies) are not available to companies.
- HM Treasury discount rates hold no authority, such as when discounting provisions of when measuring the fair value of a financial instrument using future cash flows.

42.66 Where companies do not choose to apply the FReM, they gain certain freedoms arising from the fact that they are able to interpret UK GAAP/IFRS without restriction, as follows:

- the 'historical cost less depreciation and impairments' measurement option in IAS 17 *Leases*, FRS 102 (January 2022) and IAS 38 *Intangible assets* is restored
- there is no need to discuss changes in depreciation policies with sponsor bodies or HM Treasury
- the requirement to expense borrowing costs connected to assets held as fair value falls away, so such costs are capitalised if they satisfy the eligibility criteria in IAS 23 *Borrowing costs* and FRS 102 (January 2022); and
- all approaches to the recognition of actuarial gains and losses under IAS 19 *Employee benefits* are available, including the corridor approach and recognition through the performance statement.

42.67 Only a limited number of FReM interpretations are compatible with the Companies Act. The starting point is that accounting standards should be applied without adaptation. However, the following adaptations are allowed, since they do not conflict with the Companies Act:

- Companies may include a Governance Statement.
- Companies may include a full Remuneration Report in accordance with HM Treasury guidance, or in accordance with Companies Act requirements had the company been listed, provided that it also provides all the information required by the Companies Act and it cross-references from the financial statements.

- Companies may prefer the valuation basis for fixed assets over the historical cost method.
- Companies may account for actuarial gains and losses through the Statement of Recognised Gains and Losses or the Statement of Comprehensive Income/Expenditure as an accounting treatment for pensions.
- Companies can credit supply from government bodies directly to the income and expenditure reserve

42.68 Additionally, some FReM interpretations provide detail on how to apply very specific accounting concepts in GAAP, such as determining an asset's value-in-use. In cases where such guidance provides additional detail rather than adapting GAAP, there is no impediment to their use.

Regularity

42.69 The concept of regularity reflects Parliament's concern that public money is used only for those purposes approved by Parliament. The preparation of financial statements by bodies carrying out a public function is an important means by which they are accountable for the use of public funds made available to them by Parliament. Parliament has a reasonable expectation that the transactions included in the financial statements for bodies directly accountable to Parliament will be in accordance with the framework of authorities. The engagement team should therefore determine whether a regularity opinion should be provided for such companies, in accordance with the guidance in Chapter 10: Determining the form of opinion.

42.70 ***Consultation required*** Issuing a regularity opinion on the financial statements of GRAA companies is at the NAO's discretion. Due to the nature of these entities, a regularity opinion will normally be required, but engagement teams are still required to make a formal assessment and recommendation to FAPQ.

42.71 Non-GRAA companies do not lay their accounts before Parliament and their accounts are prepared and audited under the Companies Act. It is beyond the scope of the statutorily-required audit work on a company to provide an opinion on regularity.

42.72 Non-GRAA companies, or their sponsoring departments, may request a regularity opinion in some circumstances. This is particularly the case where a non-GRAA company sits within a sponsoring department's consolidation boundary and the department requires assurance over the regularity of transactions entered into by the company.

42.73 ***Consultation required*** In accordance with the policies above, Engagement Directors on Companies Act audits should make an assessment of such requests, based principally on the extent to which the audited entity is funded by government grant or performs a public function. A recommendation should then be made to FAPQ and the final judgement recorded on the audit file.

42.74 As with all audited entities, there are sometimes difficult judgements involved in determining whether a transaction is not in accordance with Parliament's intention. However, many Companies Act audited entities are established by a form of authorising legislation and, therefore, Parliament's intention can be described in terms of compliance with the authorising, or governing, legislation.

42.75 For example, companies which perform a public function often have governing legislation which allows them to raise fees to deliver their statutory objectives. When an entity earns income

outside of these objectives it may be irregular, in addition to being non-compliant with laws and regulations and could have a material impact on the financial statement disclosures.

42.76 A company audited under the Companies Act whose accounts are consolidated into its sponsor department's financial statements, will not necessarily be subject to HM Treasury or related spending controls or the requirements of Managing Public Money – this will depend on the specific framework of authorities applicable to the company (for example, any framework agreement with a sponsor department). If not prevented by its own framework of authorities, the company can make ex-gratia severance payments to staff without the need for Treasury approval. There is no regularity impact for transactions that are in accordance with the company's framework of authorities when consolidated into the group financial statements, even though the parent is subject to the approval requirements within Managing Public Money.

42.77 As part of the preliminary engagement activities, the engagement team should assess whether it is appropriate for a regularity opinion to be given on the company's financial statements, basing this assessment on the extent to which the body provides a public function, is funded from public monies and is directly accountable to Parliament. Consideration should also be given of the entity's framework of authorities and whether it is an appropriate framework against which to audit.

42.78 ***Consultation required*** The engagement team should provide to FAPQ an evidence-based recommendation on whether a regularity opinion should be provided and then retain the final decision in the audit file.

42.79 Where it is agreed to give a regularity opinion this will, by definition, be discretionary. The engagement team should consider and agree the criteria for what constitutes an irregular transaction under such circumstances and document this on the Apex audit file, as well as setting this out in the Letter of Engagement, as there may be a significant 'expectations gap' between the audited entity's understanding of the NAO's work and what the engagement team is able to provide.

42.80 The engagement team should tightly define relevant reference points for the regularity opinion in liaison with the audited entity and the sponsor department (if any), referring, where relevant, to authorising and governing legislation, as well as any framework document issued by the sponsor department containing specific requirements on how public money should be used. The documented criteria for what constitutes an irregular transaction should establish clearly that a breach of the company's articles of association would not, in itself, constitute a qualification issue, since the articles are easily amended and are not an indication of Parliamentary intention.

42.81 When company accounts are consolidated into a parent entity's group financial statements, there can only be one framework of authorities for each transaction; the same transaction cannot be regular in one set of financial statements and irregular in another. The parent body's framework of authorities does not apply to the company unless made a condition of ownership in the memorandum and articles of association or associated framework document.

42.82 Where provided, the regularity opinion should be stated on the face of the audit report. However, for Companies Act audits, no further report may be provided in support of a qualification.

Going concern

42.83 FRS 102 (January 2022) and IFRS both require directors to satisfy themselves that it is appropriate to prepare financial statements on a going concern basis before approving them. The board is initially responsible for assessing the entity's going concern status; audit procedures should follow-on from the work management performs, as set out in ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern* and Chapter 27: Going concern.

42.84 The risk of an inappropriate use of the going concern is more significant for companies that for other NAO audited entities because:

- most companies are trading entities and are reliant on generating sufficient revenue to remain a going concern, whereas other government bodies often have the guarantee of sponsor department funding or are established on a statutory basis; and
- the arm's length nature of companies makes them potentially transient in nature, so they are more likely to be dissolved than central government bodies established in statute, especially if they are seen to perform poorly.

42.85 Where government companies are wound-up but their functions continue through a machinery of government change, there may be scope to apply the principles of the FReM interpretation of IAS 1, which directs bodies to adopt the going concern basis in such circumstances. For example, if the company is established in statute and have a statutory funding mechanism, the principles of the continued provision of service approach, as described in Practice Note 10 (Revised 2022) and Chapter 27: Going concern, can be applied in the circumstances.

42.86 The engagement team should perform and document a robust planning assessment of the extent of the risk that the entity will adopt the going concern basis inappropriately, which should include enquiring with suitable senior staff at the audited entity and, where applicable, its ultimate parent.

42.87 The engagement team should also consider the events or conditions that may cast significant doubt on the entity's ability to continue as a going concern outlined in paragraph A3 of ISA (UK) 570 (Revised September 2019) (Updated May 2022).

42.88 For all Companies Act audits, the engagement team should:

- address specific items of uncertainty in respect of the going concern assumption in the Letter of Representation;
- where appropriate, obtain a signed letter of comfort from the company's main source of grant or credit that they have no plans to withdraw funding by the date up to which going concern is being considered; and
- where such confirmations are obtained, consider their suitability as audit evidence in light of information from other procedures and wider knowledge of the business.

42.89 Where appropriate, the engagement team should consider modifications to the audit report, following the processes set out in Chapter 27: Going concern and Chapter 55: Modified certificates and reports, which set out the implications for the audit report in different circumstances, including where the going concern basis has not been adopted, where there is uncertainty or where the going concern assumption has been applied inappropriately. The engagement team is advised to consult FAPQ at an early stage.

42.90 Gathering evidence on an audited entity's ability to continue its business can create difficult situations: for example, if management communicates an uncertainty of which staff are not aware. The engagement team should act with the utmost sensitivity and discretion, with due regard to the NAO's duty to uphold audited entity confidentiality.

42.91 ***Consultation required*** Directors retain responsibility for ensuring sound financial management regardless of the statutory basis of the entity. It would be illegal for the directors to continue operating a company when it is insolvent. Therefore, companies may disclose material uncertainties related to going concern even if the company was established by statute and therefore could not legally cease to operate. In such circumstances, the engagement team should consult FAPQ.

42.92 The responsibility for directors includes requirements for reporting to the relevant regulators. By extension, this requirement would require any concerns surrounding financial sustainability to be reported to the relevant regulator by the auditor under ISA (UK) 250A (Revised November 2019) (Updated May 2022). If this is the case, the Engagement Director must follow the protocol for reporting to regulators set out in Chapter 31: Consideration of laws and regulations and reporting to regulators.

42.93 Further considerations on going concern may be found in Chapter 27: Going concern.

Current and deferred tax

42.94 Many government-owned companies are within the scope of corporation tax and subject to the UK tax regime.

42.95 There is no requirement under ISAs (UK) to perform a line-by-line audit of the corporation tax return.

42.96 Under FRS 102 (January 2022) and IAS 12 *Income taxes*, companies have to make a number of disclosures whether or not they have a tax liability.

42.97 Assets and liabilities relating to deferred tax may arise where a company has a current tax liability or where there is a reasonable prospect of the payment of tax in the near future. The purpose of deferred tax is to ensure that tax charges and refunds are recognised on an accruals basis, rather than on the basis of which they fall due to HMRC as determined by legislation. For example, the capital allowances permitted by HMRC often write-down fixed assets at a faster rate than a company's depreciation policy. In this instance, a deferred tax liability is created to spread the tax allowance over the same period as the asset's useful economic life, to harmonise the accounting treatment of the asset and its tax effects. Deferred tax assets may arise where companies are loss-making and anticipate that they will be able to relieve current tax losses against future taxable profits. However, the relevant accounting standards set a high bar to the recognition of deferred tax assets where there is a history of losses. Where such companies do recognise tax assets, this should be disclosed as a key judgement in the notes to their financial statements as it may have a significant effect on a reader's interpretation of the financial statements.

42.98 All movements in deferred tax assets and liabilities will be matched by income and expenditure in the company's performance statement.

42.99 The engagement team should address the risk of taxation items giving rise to material misstatement of the financial statements, ensuring that the current tax charge and the resulting tax liability at the year-end are materially accurate.

42.100 The engagement team should include a working paper within standing information on the Apex audit file that explains the audited entity's tax position and any accounting implications and makes an assessment of the risks of material misstatement, which should also be reflected in the Risk Assessment in Apex. The engagement team should design procedures to address any risks of material misstatement associated with taxation, following the process set out in Chapter 17: Risk assessment and response planning.

42.101 Where the audited entity recognises deferred tax assets following a history of losses, the engagement team should challenge the evidence provided to support management's assessment of the recovery of a deferred tax asset. A high standard of evidence is required as to the existence of future taxable assets against which losses can be offset.

42.102 ***Consultation required*** Where non-compliance with tax legislation is identified, the engagement team should follow the processes set out in Chapter 31: Consideration of laws and regulations and reporting to regulators. Where a non-compliance with tax legislation is identified, this may result in a need to report to a third party in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements. The engagemen*t team's responsibilities in relation to the audit of the financial statements do not extend to determining that the entity has complied in every aspect with applicable tax legislation. Any instances of non-compliance with tax legislation which are identified must be referred to FAPQ.

42.103 When calculating the deferred tax asset or liability, companies should apply the tax rate expected to apply on the crystallisation of the tax liability based on the latest Finance Act.

Share capital and equity reserves

42.104 In addition to the principal accounting reserves, companies limited by shares will also have items in their Balance Sheet relating purely to equity. All companies limited by shares will have a share capital account, representing the nominal value of all ordinary shares issued by the company.

42.105 Some shares are more characteristic of debt than equity. For example, if the shares entitle a shareholder to an annual dividend of a fixed amount they are, in substance, a loan agreement with fixed interest payments. Such shares are often known as 'preference shares'.

42.106 Following incorporation, changes to government-owned companies' share capital are rare. The engagement team should review the share register to determine whether there have been any changes and determine whether any further procedures are required.

42.107 The engagement team should reconcile any changes in share capital and the shareholders to relevant legal documents and the annual return to Companies House. This information should be held as standing information on the Apex audit file, updated as necessary and considered for any additional impact on the audit.

42.108 Where a company issues new shares during the year, the engagement team should review documentation to determine whether the shares are more characteristic of debt or equity and determine whether the company's accounting policy for these instruments reflects the underlying characteristics of the shares, in line with the relevant financial reporting framework.

42.109 The engagement team should consider the completeness of share movements based on other procedures, such as the review of board minutes and their wider understanding of the company's business.

42.110 The engagement team may consult FAPQ if an audited entity recognises an equity reserve other than the share capital account and the revaluation reserve. Additional reserves should not arise in wholly government-owned companies.

Dividends

42.111 Companies limited by shares may distribute profits to shareholders as dividends. A dividend is simply a payment made by the company to its shareholders, whether they are ordinary shareholders or preference shareholders.

42.112 Under Section 830 of the Companies Act, dividends may only be made out of "profits available for the purpose" (i.e., the accumulated realised profits of the company since start-up less the accumulated realised losses – in accounting terms this usually equates to the balance of the main income and expenditure reserve). Dividends in excess of these are illegal.

42.113 Under both FRS 102 (January 2022) *The financial reporting standard applicable in the UK and Republic of Ireland* and IAS 10 *Events after the reporting period*, dividends are recognised only when declared, not just when they are proposed. The loss to the company is disclosed either at the base of the performance statement to arrive at a figure for retained profit (UK GAAP) or in the Statement of Changes in Equity (IFRS).

42.114 In many cases, directors will declare a dividend after the balance sheet date (but prior to the issue of the accounts). Where this is the case, dividends should be disclosed in both the directors' report and the post-balance sheet events (events after the reporting period) note.

42.115 Dividends on ordinary shares, with the characteristics of equity, are accounted for through reserves and are shown either in the notes to the financial statements or in the Statement of Changes in Equity, depending upon the applicable financial reporting framework.

42.116 Interim dividends are recognised when the payment is made, by debiting the income and expenditure reserve and crediting cash. Final dividends are recognised when formally approved in a written resolution or at a general meeting of the company. In such cases, there may be a creditor at the balance sheet date depending upon the date the dividend was approved.

42.117 Under civil law, companies may only pay dividends out of distributable reserves consisting of 'realised profits'. In practice, a company's realised profits will only be those in the main income and expenditure reserve; revaluation reserves and the share premium reserve are specifically excluded.

42.118 Further guidance on realised profits is available in the ICAEW's Technical Release Tech 02/10 *Guidance on the determination of realised and losses in the context of distributions under the Companies Act 2006*.

42.119 Where a company recognises a dividend, the engagement team should inspect bank statements to confirm payment and determine the appropriate accounting treatment. The engagement team should also inspect the minutes of board meetings and general meetings to gain assurance over the completeness of dividends.

42.120 The engagement team should assess whether dividends have been made out of realised profits, in accordance with the requirements of the Companies Act, in particular if the company pays dividends following any type of restructuring or complex transaction. The engagement team may consult FAPQ as appropriate.

42.121 Where an audited entity has paid a dividend in excess of distributable reserves, the engagement team should consider the requirements of ISA (UK) 250A (Revised November 2019) (Updated May 2022). In particular, the engagement team should assess the effect on the financial statements of any additional tax charge arising as a result of the excessive dividend.

42.122 A legal opinion has been obtained by the ICAEW that gift aid payments made by the trading subsidiary companies of charities meet the definition of distributions under Section 829 of the Companies Act. Therefore, any such payments made by trading subsidiaries which exceed their profits available for distribution constitute unlawful distributions. Such unlawful distributions are recoverable by the trading subsidiary and should be disclosed as such within their financial statements.

42.123 ***Consultation required*** Furthermore, where such unlawful distributions have been made, the engagement team should consider the regularity implications (where a regularity opinion is provided) and whether a report should be made to a third party in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022). Further guidance on non-compliance with laws and regulations can be found in Chapter 31: Consideration of laws and regulations and reporting to regulators. Any instances of such unlawful distributions being made must be referred to FAPQ.

42.124 As the gift aid payments made by trading subsidiaries to their charitable parents constitute distributions, they should be disclosed within equity. However, as these payments are still eligible for gift aid, they should be clearly disclosed as "Gift Aid Payments to Parents" rather than dividends, as dividend payments are ineligible for gift aid under Section 194(3) of the Corporation Tax Act 2010.

Related party transactions

42.125 The audit approach for companies' related party transactions is the same as for other audited entities. Depending upon the risk assessment there may be a greater risk of material misstatement arising from related party disclosures for company financial statements than for other audited entities.

42.126 The engagement team should be alert to circumstances where a director, or a close family member of the director, owns or has significant influence over another company. Where this is the

case, that company would be a related party. Significant influence may be through common directorships, as the owner of a business is likely to be a director.

42.127 Engagement teams should use the Companies House website to obtain information on directors and related parties.

42.128 The audit approach for companies' related party transactions is the same as for other audited entities, as set out in Chapter 28: Related parties.

Concluding, reporting and filing

42.129 Guidance on concluding, reporting and filing for companies is available in Chapter 60: Reporting to the members or shareholders of a company and filing with Companies House.

Non-audit services

42.130 Engagement teams are able to provide some non-financial audit services, such as grant certification assurance arrangements, but should only accept such work if it complies with the FRC's Revised Ethical Standard 2019. Further considerations may be found in Chapter 8: Ethical considerations.

42.131 The engagement team should treat any work additional to the financial statement audit as a separate engagement from the financial statement audit and subject it to the NAO's standard business risk management procedures, including the requirements for C&AG approval of new engagements set out in Chapter 9: Engagement acceptance (statutory and non-statutory).

Companies that choose to apply the FReM

42.132 Where the audited company chooses to apply the FReM, the engagement team should:

- ensure all disclosures, including those driven by the FReM, are consistent with audited accounts, knowledge gained during the audit and the negative consistency opinion in the audit report;
- ensure that the accounts are properly prepared under the Companies Act, that in all material respects, disclosures are complete, and the chosen accounting framework was correctly applied; and
- ensure that no disallowed adaptations from the FReM have been applied (see the section earlier in this Chapter entitled 'Key financial reporting context for companies').

Companies that are part of departmental and other groups

42.133 The engagement team should agree with the Group Engagement Team whether any procedures are required on records kept by the company for group reporting purposes and note any such procedures in the Letter of Engagement.

Exemptions from audit under the Companies Act

42.134 Where an audited body no longer requires an audit under the Companies Act, the C&AG may wish, or be asked, to withdraw from the Companies Act audit.

42.135 Chapter 1 of Part 16 of the Companies Act governs when a company is exempt from audit. In summary, a company may be exempt where:

- the group it is part of qualifies as a small under Section 383 of the Companies Act;
- it is a subsidiary whose parent undertaking prepared suitable group accounts and has provided a guarantee to the subsidiary; or
- the company is dormant.

42.136 The Charity Commission has ruled that for a charity to provide this guarantee to their commercial trading arms would be against the charity's objects. Therefore, charity subsidiaries are generally not able to use the subsidiary audit exemption.

42.137 HM Treasury has cautioned against the use of the subsidiary exemption in the public sector, although they are prepared to consider its use on a case-by-case basis.

42.138 Where engagement teams are concerned about the use of an exemption, they may consult FAPQ and potentially the Treasury Officer of Accounts (TOA) team.

Communicating with management and those charged with governance

42.139 The engagement team should ensure that communications and requests for representations are tailored to reflect the circumstances of a Companies Act audit including, as appropriate;

- discussion of, and representations regarding, significant risks from company audit issues such as taxation, dividends, going concern or the presumed risk of fraud in revenue recognition; and
- terminology, such as addresses and quoting, 'audit report' instead of 'audit certificate'.

Governance Statements

42.140 Where the company is required to prepare a Governance Statement in accordance with HM Treasury guidance, the engagement team's responsibilities towards this statement are consistent with the responsibilities towards non-company audited entities. Further guidance on review of such Governance Statements may be found in Chapter 32: Other information and other reporting responsibilities.

42.141 Where the company is required to prepare a Corporate Governance Statement as a result of adopting the UK Corporate Governance Code and this is included as a separate report, Section 497A of the Companies Act 2006 requires that the auditor considers whether the information given in the separate Corporate Governance Statement in compliance with rules 7.2.5 and 7.2.6 in the Disclosure Guidance and Transparency Rules sourcebook made by the Financial Conduct Authority (information about internal control and risk management systems in relation to financial reporting processes and about share capital structures) is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

42.142 Furthermore, where the company is required to prepare a Corporate Governance Statement as a result of adopting the UK Corporate Governance Code and this is included as a separate report, the auditor is also required to consider whether rules 7.2.2, 7.2.3 and 7.2.7 in the Disclosure Guidance and Transparency Rules sourcebook made by the Financial Conduct Authority (information about the company's Corporate Governance Code and practices and about its administrative, management and supervisory bodies and their committees) have been complied with.

Resignation, removal and expiry of the audit term

42.143 Through the Companies Act 2006, the Financial Reporting Council (FRC), as the appointed Independent Supervisor of the C&AG's Companies Act work, requires the NAO to comply with the C&AG Audit Regulations 2008 in respect of that work.

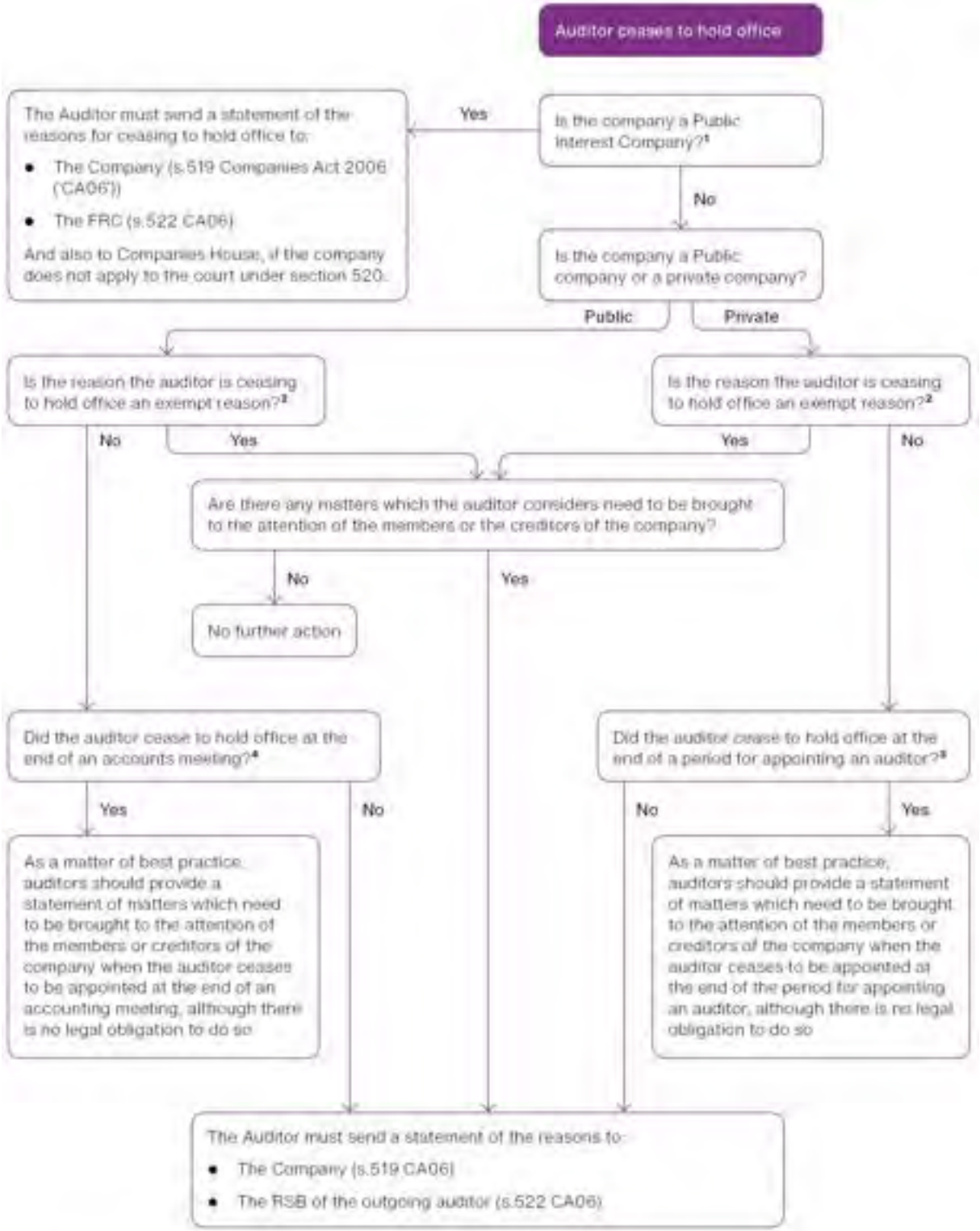
42.144 This requires that: "Where the C&AG ceases to hold an audit appointment in relation to any entity and another Registered Auditor (the "successor") is appointed, the C&AG must, if requested in writing by the successor, allow the successor access to all relevant information held by the C&AG in respect of the last audit report signed by the C&AG. Relevant information is the information in the audit working papers compiled to comply with auditing standards. Any information obtained by the successor is for the purposes of its audit and must not be disclosed to a third party unless required to do so by a legal or professional obligation."

42.145 When the C&AG ceases to act as auditor for a company audited entity, the engagement team should be sensitive to the handover arrangements, including the requirement to provide the successor auditor with access to relevant working papers. Note that, as set out in Chapter 9: Engagement acceptance (statutory and non-statutory), the procedures for sharing information with successor auditors are applicable to all NAO engagements, including non-company audits.

42.146 If the C&AG ceases to hold office as a company's auditor, the engagement team should send a notice to that effect to the company under Section 516(1) of the Companies Act. Under Section 516(3) of the Companies Act, the resignation is effective either on the date at which the notice of resignation is received by the company or on a later date specified in the notice of resignation.

42.147 Where the C&AG ceases to be the auditor of a company, a statement of reasons for ceasing to hold office may need to be sent to the company depending on the circumstances. ***Figure 42B*** below sets out the decision-making process.

Figure 42B: Flow chart for decision making as to whether to provide a statement of reasons for ceasing to hold office upon the C&AG ceasing to hold office as auditor



Notes

1 Section 519A of the Companies Act defines a Public Interest Company.

2 Section 519A(3) of the Companies Act defines 'exempt reasons'.

3 Section 485(2) of the Companies Act specifies the period for appointing an auditor for private companies.

4 Section 437(3) of the Companies Act defines an 'accounts meeting' in relation to a public company.

42.148 Chapter 4 of Part 16 of the Companies Act includes further provisions relating to statements by an auditor on ceasing to hold office. However, these provisions are not relevant to GRAA companies or other companies who are exempt from Part 16 of the Act.

42.149 Where the C&AG resigns or is removed by company resolution during his term and a statement of circumstances is sent to the company, the NAO must send notice of the C&AG ceasing to hold office, together with a copy of the statement of circumstances, to the Financial Reporting Council (auditorresignation@frc.org.uk), which represents the 'appropriate audit authority' referred to in Section 522 of the Companies Act 2006.

42.150 The engagement team should take prompt action with regards to the Companies House requirements when the C&AG ceases, for any reason, to act as a company auditor as failure to comply is an offence under the Companies Act and is punishable by a fine.

42.151 ***Consultation required*** Where the company is a regulated entity ("an entity subject to statutory regulation"), whether the auditor resigns, is removes or otherwise ceases to hold over, consideration should be given as to whether there are any relevant matters to report to the regulator in accordance with ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector.* Where such matters are identified, the team must notify FAPQ. Further guidance can be found in Chapter 31: Consideration of laws and regulations and reporting to regulators.

42.152 The engagement team may wish to withdraw from the engagement if they believe that the entity or an employee of that entity is engaged in money laundering or any other illegal act, particularly where a normal relationship of trust can no longer be maintained. Where the engagement team intends to cease to hold office there may be a conflict between the requirements under Section 519 of the Companies Act 2006 to deposit a statement at a company's registered office of any circumstances that the auditor believes should be brought to the attention of members or creditors and the risk of 'tipping off'.

42.153 Where such disclosure of circumstances may amount to 'tipping off', the engagement team may consult FAPQ and the MLRO. The MLRO will seek to agree the wording of the statement of circumstances with the relevant law enforcement agency and, failing that, will seek legal advice. The MLRO may, as a last resort, need to apply to the court for direction as to what is included in the statement of circumstances.

42.154 In response of his statutory obligation under the Companies Act, the C&AG must comply in full with the requirement to provide access to relevant information to successor auditors of company audited entities. The NAO choose to follow the same principles in respect of all other engagements.

42.155 The requirements to provide access to working papers do not apply to:

- changes of contracted-out auditor (the C&AG remains the appointed auditor and owns the working papers generated in support of these audit opinions, whether they are prepared by the NAO or a partner firm); or

- requests for access from the first-time auditors of entities formed as the result of privatisations or Machinery of Government changes. Any requests for information in such circumstances may be referred to FAPQ.

42.156 The engagement team should not provide access to working papers until:

- the audited entity has confirmed that it has formally appointed a successor auditor; and
- the C&AG has received, by e-mail or post, a formal request for access from the successor auditor. If successor auditors are unclear on the form of such a request, the engagement team should direct them to Appendix B of ICAEW Technical Release AAF 01/08 *Access to information by successor auditors*.

42.157 ***Consultation required*** Once the conditions for access have been satisfied, the engagement team should consider the logistics of granting access with a view to minimising time and cost requirements for all parties. In most circumstances, a member of the successor engagement team will visit NAO premises to access working papers on a standalone laptop. It may also be possible to arrange to share working papers remotely using MS Teams. Where a successor auditor suggests that working papers are shared using an alternative technology, the engagement team should consult FAPQ.

42.158 The engagement team should consider whether it is appropriate to recharge the direct costs of providing access to the successor auditor. This will only be appropriate in unusually complex cases where redaction and sharing of the file would otherwise represent an unnecessary and unreasonable burden. Any recharge should:

- include direct/incremental costs only (i.e., staff time at 'direct' rates rather than 'fee' rates); and
- be agreed in writing with the successor, subject to a maximum price cap.

42.159 Successors may choose to recharge these costs back to the audited entity, who may be unwilling to pay. Engagement teams may refer cases of significant dispute to FAPQ to ensure that the C&AG discharges his statutory responsibilities to respond to successors' requests in a timely manner.

42.160 Having concluded on the issues above, the engagement team should issue a formal response to the predecessor's request, by e-mail or post, copying FAPQ and the audited entity into the correspondence.

42.161 Before the successor auditor attends NAO premises, the engagement team should:

- follow the relevant aspects of the process set out on the Sharepoint page linked here for providing access to Apex files to external parties;
- make all redactions to working papers required by the NAO's policy on the management of data used for audit purposes;
- where working papers held off the main audit file constitute information relevant to the previous year's audit, (for instance, documents specifically referenced in order to support the opinion) grant access to these documents;
- redact the audit file to remove any information not relevant to the opinion;
    - Information and documents required by NAO policy, but not an ISA requirement, should be removed. In practice this is likely to mean the areas of the file covering engagement and risk management and administrative planning, but engagement teams should review this on

a case by case basis and remove any information which is commercially sensitive, such as staff budgets.

- remove any information subject to legal or professional privilege asserted by the audited entity or a third party, such as internal audit reports and legal advice;
    - The engagement team should contact the audited entity to check whether they are content for the successor auditor to access such information and, where they are not, notify the successor that some information has been omitted for this reason, but not disclose the nature of that information.
- remove any information generated by the NAO or its legal advisers over which the NAO may wish to assert legal or professional privilege.
    - ***Consultation required*** Where such information exists, legal advice should be obtained from the NAO's Legal and Policy team over whether it should be shared with the successor.

42.162 The relevant Information Asset Owner should ensure that appropriate redactions are made and that the revised file does not contain personally sensitive information or information which is potentially compromising to the NAO or the audited entity.

42.163 The engagement team should be prepared to answer questions that successors have about working papers, whilst minimising the NAO's exposure to legal and reputation by being aware that:

- the engagement team are not normally obliged to answer queries which are not relevant to the audit work undertaken between the beginning of the last financial year under audit and the date on which the C&AG officially ceased to act;
- explanations to successor queries should be given a factual or evidential reference point; and
- where queries are either sensitive or highly numerous, it may be wise to exchange written notes in relation to some or all of those queries.

42.164 Upon the end of a term as auditor of a company, the Engagement Director should ensure that the successor auditor is aware of all relevant facts and information concerning non-compliance with laws and regulation that they consider they should be aware of in deciding whether to accept the appointment as auditor.

42.165 The offence of 'tipping off' may cause a conflict with the need to communicate with the prospective successor auditor in accordance with legal and ethical requirements relating to changes in professional appointment. Under anti-money laundering legislation, this would not constitute 'tipping off' if it was done to prevent the successor auditor from committing a money laundering offence. Further guidance on anti-money laundering responsibilities may be found in Chapter 30: Fraud responsibilities.

42.166 Engagement teams may consult FAPQ in case of any doubt on the appropriateness of responses in particular situations.

42.167 There is no obligation to allow successor auditors to take or retain copies of NAO working papers. Where the successor has a genuine interest in specific working papers for the purpose of planning or assurance over opening balances, the NAO allows electronic copies to be made.

42.168 Where the predecessor engagement teams deem it necessary to deviate from the standard arrangements, the engagement team may consult FAPQ, explaining the issue and their proposed course of action.

42.169 All written documentation relating to the handover should be stored in Sharepoint.

General meetings of the company

42.170 The auditor has the right to attend any general meetings of the company and be heard on any part of the business at such meetings which concerns them in their role as auditor.

42.171 Whilst it may not always be appropriate for the Engagement Director to attend general meetings of the company, the engagement team may wish to consider whether there are circumstances where it is appropriate to do so in order to address the members of the company. For example:

- The Engagement Director may make a statement concerning facts which have been discovered subsequent to the date of the auditor's report which have not been appropriately reflected in the financial statements.
- Where the financial statements have not yet been laid before the members and those charged with governance do not intend to make an appropriate statement at the general meeting concerning this, the Engagement Director may wish to make such a statement.
- Where the engagement team considers that those charged with governance may not adequately discharge their duties to bring relevant matters surrounding the financial statements and the audit to the attention of the members, the Engagement Director may wish to make a statement concerning this.

Chapter 43: Charities

Relevant standards and guidance

43.1 Chapter 3 of Part 8 of the Charities Act 2011 includes provisions relating to the audit or examination of charity accounts.

43.2 Practice Note 11 (Revised) *The audit of charities in the United Kingdom* provides guidance on applying ISAs (UK) to the audit of financial statements of charities in the United Kingdom.

43.3 Further guidance is also available on the websites of the Charity Commission, the Office of the Scottish Charity Regulator, the Charity Commission for Northern Ireland and the Republic of Ireland's Charities Regulator.

Background and overview of charity accounts

43.4 The charities which are directly subject to NAO's certification audit each year are a diverse group of organisations. While many have much in common with other NDPBs in the public sector, others are more similar, in terms of their corporate governance arrangements, with non-public sector charities. Under the GRAA, the C&AG can be, and has been, appointed the statutory auditor of charitable companies.

43.5 The guidance that is contained in this Chapter relates to where the C&AG is the auditor of the charity. Where grants are awarded by government entities to charities, the normal rules of audit will apply and engagement teams should apply the other relevant Chapter(s) in the FAM.

43.6 Registered charities are required to comply with the relevant legislation which outlines the requirements for the form and content of charities' accounts and annual reports, including group accounting and reporting. The legislation registered charities are required to follow is:

- for charities registered in England and Wales, the Charities Act 2011;
- for charities registered in Scotland, the Charities and Trustee Investment (Scotland) Act 2005 and the Charities Accounts (Scotland) Regulations 2006;
- for charities registered in Northern Ireland, the Charities Act (Northern Ireland) 2008; and
- for charities registered in the Republic of Ireland, the Charities Act 2009.

43.7 ***Consultation required*** If an audited entity is registered with another regulator not listed above, the engagement team should inform FAPQ.

43.8 Charitable companies also need to comply with the annual report and accounts requirements contained within the Companies Act 2006.

43.9 Under legislation applicable in England and Wales, Scotland, Northern Ireland and the Republic of Ireland, registered charities apply the Charities SORP, which contains detailed requirements, to prepare their accounts. There are also some entities which are analogous to charities which, for good practice purposes, are directed by their sponsor departments to apply the Charities SORP to prepare their accounts.

43.10 For charities registered in Scotland, there are additional reporting requirements.

The Charities SORP

43.11 As required by the Charities (Accounts and Reports) Regulations 2008, registered charities in the United Kingdom that prepare their accounts on an accruals basis, should, in all but exceptional circumstances where a true and fair override is appropriate, follow the recommendations set out in the Charities SORP. The accounting recommendations in the Charities SORP are based on FRS 102 (2022), and provide detailed guidance and clarification on their application within the charities sector.

43.12 Charitable public bodies, such as Charitable NDPBs, are generally directed to apply the FReM, usually through accounts directions. The FReM states that government bodies with charitable status should follow the SORP, as well as providing any additional disclosures that are required by the FReM, where these disclosures go beyond the SORP's requirements.

Financial reporting framework

43.13 Charities are required to prepare their financial statements in accordance with the Charities SORP. In selecting accounting policies and making accounting judgements in accordance with the Charities SORP, the majority of charities will be required to follow the hierarchy set out in paragraph 10.5 of FRS 102 (2022). This states that in making accounting judgements, management shall refer to and consider the applicability of the following sources in descending order:

- the requirements and guidance in an FRS or FRC Abstract dealing with similar and related issues;
- where an entity's financial statements are within the scope of a Statement of Recommended Practice (SORP) the requirements and guidance in that SORP dealing with similar and related issues; and
- the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses and the pervasive principles in Section 2 of FRS 102.

43.14 Where the charity does not prepare its financial statements in accordance with an Accounts Direction or does not have a separate statutory requirement for preparation of the financial statements, the above hierarchy should be followed in making accounting judgements.

43.15 The majority of the NAO's audited charities will prepare their financial statements in accordance with an Accounts Direction, usually set by the charity's sponsor department, which may require them to prepare their financial statements in accordance with the Charities SORP. In such circumstances, the Charities SORP, rather than FRS 102 (2022), may sit at the top of the hierarchy for making accounting judgements. Such an Accounts Direction is only binding on the charity if it has been issued in accordance with the legislation that requires the entity to prepare financial statements – a non-statutory Accounts Direction would be advisory only.

43.16 The majority of the NAO's charity audited entities are also required to prepare their financial statements in accordance with the FReM. Where this is the case, the FReM itself directs charities to prepare their financial statements in accordance with the Charities SORP, but to include the disclosures required by the FReM which are over and above the requirements of the Charities SORP.

43.17 Guidance on the key additional disclosures applicable to charitable entities applying the FReM are incorporated each year into the NAO's Charities SORP disclosure checklist. Engagement teams should ensure the accounts disclosures are complete with reference to both this checklist and elements of the FReM disclosure guide which may be relevant in the context of the charity's financial reporting framework.

43.18 The engagement team should ensure that they fully understand and document the financial reporting framework particular to the charity as part of their work in understanding the entity and its environment, as set out in Chapter 15: Gathering entity initial information.

Key differences between charity and non-charity accounts

43.19 There are some key accounting differences between charity and non-charity accounts which are highlighted below:

- Recognition of incoming resources: The Charities SORP has a separate definition for the recognition of incoming resources in charity accounts which depends on three factors being met: entitlement, probable and measurement. This differs from the standard recognition criteria for income recognition.
- Disclosure of resources expended: charities are required to allocate support and governance costs between the core activities of generating funds and charitable activities. The bases for apportionment for the support costs should be appropriate and clearly disclosed.
- The funds of the charity: there are clear definitions of unrestricted, restricted and endowment funds. It is important for engagement teams to have a clear understanding of this guidance, especially in respect of restricted funds, which can be restricted by the donor, have implied restriction (for example, through a public appeal) or have restriction created through a legal process.

Types of charity

43.20 A charity can be a company, usually limited by guarantee (i.e., a charitable company), or an unincorporated body. An unincorporated body may take the form of, for example, a trust, a Charitable Incorporated Organisation (CIO: a charity registered as a body corporate under the relevant charitable legislation), or a body (for example, charitable public bodies/NDPBs) incorporated by Royal Charter or special Act of Parliament but will generally fall into one of three categories.

- Registered: this is a charity that must register with the Charity Commission and falls under its supervision and regulation. All charities have to be registered unless exempt, excepted or small (charities with annual gross income less than £5,000). The charity may also be registered with other regulators, depending on where they operate.
- Exempt: charities legislation provides exemption from registration with the Charity Commission for certain, specified organisations. Exempt charities have a 'principal regulator' to regulate them as charities. Examples of these types of charities are certain universities, higher education corporations, academy trusts and various museums and galleries covered by the Museums and Galleries Act 1992. Many of the charities audited by the C&AG fall into this category. Exempt charities follow the accounting and reporting requirements that their principal regulator requires. Otherwise, the Charities Act 2011 only requires them to produce an income and expenditure account and a balance sheet.
- Excepted: these are charities that do not have to register with the Charity Commission, but in most other respects are regulated by the Charity Commission. Examples include charities (but not CIOs)

whose gross income is less than £5,000 per year, churches and chapels of certain religious charities and Scout and Guides groups.

Governance arrangements

43.21 The trustees of a charity are those who are responsible, under the charity's governing document, for controlling the management and administration of the organisation. In charitable government bodies, the trustees are appointed under the 'public appointments process' by the sponsor department. The trustees must operate effectively as a body; set the strategic direction of the charity; and delegate appropriate authority to management and keep this delegation under review. Detailed guidance on the role and responsibilities of trustees is given on the Charity Commission website.

43.22 While the main board of trustees retains, and is responsible for, the overall control of the charity, it is usual for them to delegate responsibility for the day-to-day running and management of the charity to a chief executive and senior management team (who may be remunerated), operating through various executive sub-committees. In such circumstances the executive sub-committees oversee the implementation of policy and make recommendations to the main Board of Trustees.

43.23 In the case of charitable government bodies, while the chief executive is appointed to the role by the board of trustees, he/she will usually also be appointed as the Accounting Officer for the organisation. As with other NAO audited entities, the Accounting Officer has specific, personal responsibilities under Managing Public Money. This joint responsibility between the Board of Trustees and the Accounting Officer should be reflected within the accounts of charitable government bodies through, for example, joint signature, of the balance sheet and the governance statement, by the Accounting Officer and a representative of the board of trustees, as well as a joint statement of the Accounting Officer and trustees' responsibilities. It should be noted that for charities, which are also companies, the Accounting Officer may only sign the balance sheet if they are also a director of the company – if they are not a director, then joint signature would not be appropriate.

Voluntary income

43.24 Charities often receive voluntary income in the form of cash or donations in kind. The engagement team should consider the adequacy of the controls in place to ensure the complete and accurate recording of this type of income as it is often:

- variable from year to year;
- unrelated to the charity's level of expenditure;
- unsupported by normal financial documentation; and
- collected by volunteers with no financial experience.

43.25 There is a presumed significant risk of fraud in revenue recognition under all engagements (see Chapter 17: Risk assessment and response planning). The engagement team should consider carefully the nature of any income received or receivable by a charity in identifying the nature of this risk on each engagement or determining whether the presumption of a significant risk can be rebutted.

Legacy income

43.26 Charities often receive significant legacies and bequests from donors. Engagement teams should consider the adequacy of the controls which the charity has in place to ensure the complete and accurate recording of this income as it is:

- often notified and monitored by individuals outside of the finance function; and
- variable from year to year

43.27 Legacy income should be recognised by the charity when the receipt is of such income is probable. This occurs when the executors are satisfied that there are sufficient assets in the estate, after settling any liabilities to pay the legacies, where the value of the legacy is measurable and where any conditions attached to the legacy have either been met or are within the control of the charity. This usually equates to the point at which probate has been granted but may occur earlier.

43.28 Charities should be aware that legacy income is recognisable at the point at which the charity could be reasonably expected to be aware of the legacy. Usually, this is interpreted as the point at which the charity or its legal advisors have been advised of the legacies.

43.29 Engagement teams should therefore consider circularising the charities legal advisors and performing procedures to ensure that any legacies notified to individuals in the charity outside of the finance function (for example, in a fundraising team) have been appropriately recognised within the financial statements.

Grants and donations income

43.30 When considering the timing of recognition of grants and donations income, the engagement team should ensure that they review all of the applicable terms and conditions under which the grants and donations have been issued. This would include any communications with the grant maker or donor in addition to formal documentation provided.

43.31 Entitlement to receive a donation usually only occurs upon receipt of the donation as the donor will normally be able to withdraw the donation at any point prior to the donation being made. However, some donations will also contain conditions which must be met in order for the charity to be entitled to the donation. For example, the donation may need to be returned to the donor if the conditions are not met.

43.32 Similarly, entitlement to grant will only normally be met when the formal funding offer letter setting out the amount of grant awarded is sent to the charity. However, some grants contain conditions which must be met for the charity to be entitled to the grant funding.

43.33 When reviewing the terms and conditions of grants and donations, engagement teams look to identify performance conditions which must be met in order for entitlement to the grant or donation to occur. Such conditions will normally provide specific deliverables or activities which must be achieved for the charity to be entitled to the grant or donation.

43.34 Administrative requirements such as returns would not constitute performance conditions. Similarly, restrictions on the use of funding to certain projects or categories of expenditure would indicate that the grant income should be restricted rather than providing an indication that there is a performance condition in place.

43.35 Donations income may also be highly susceptible to money laundering. Engagement teams should be alert to this risk and should follow the procedures set out in Chapter 30: Fraud responsibilities where they suspect that money laundering may have occurred.

Restricted funds

43.36 Restricted funds must only be used in the way and for the purposes specified by the donor. If they are not, then the trustees will have breached their duty. Restricted funds must also be accounted for, and disclosed, separately in the accounts. Engagement teams, therefore, need to consider the existence of restricted funds when planning and carrying out their audits. In particular, engagement teams will need to consider:

- how accounting records are properly and adequately maintained so that income received with a restriction is classified appropriately in the accounts; and
- the adequacy of controls in place to ensure that restricted funds are used only for their specific purposes.

43.37 The audit of restricted funds is a more sensitive area than the financial statements as a whole and teams may consider setting a lower materiality threshold.

43.38 Regardless of the level of materiality by value, the engagement team should judge the materiality of misstatements identified in restricted funds qualitatively, as they may be material in the context of other laws and regulations applicable to charities (see the section later in this Chapter entitled ‘Laws and regulations’).

Going concern

43.39 Practice Note 11 (Revised) provides useful guidance regarding circumstances where a charity may not be a going concern (paragraphs 158 to 174) and audit evidence engagement teams should obtain to support the going concern assumption (paragraphs 175 to 183).

43.40 ***Consultation required*** Trustees retain a responsibility for ensuring sound financial management regardless of the statutory basis of the audited entity. It would be illegal for the trustees to continue operating a charity when it is insolvent. Therefore, charities may disclose material uncertainties related to going concern even if the charity was established by statute and therefore could not legally cease to operate. In such circumstances, the engagement team should consult FAPQ.

43.41 The responsibility for trustees would include requirements for reporting to the relevant regulators. By extension, this requirement would require any concerns surrounding financial sustainability to be reported to the relevant regulator by the auditor under ISA (UK) 250A (Revised November 2019) (Updated May 2022) and the Charities Act 2011 as a ‘matter of material significance’. If this is the case, the engagement team must follow the protocol for reporting to regulators in Chapter 31: Consideration of laws and regulations and reporting to regulators.

Related party transactions

43.42 Appendix 1 *Glossary of terms* to the Charities SORP defines related parties in the context of the requirements of charity law, company law and FRS 102 (2022). The Charities SORP definition is broader than that under IAS 24 *Related party disclosures*.

43.43 Trustees are regarded as related parties. It is a fundamental principle of trust law that trustees should not benefit from their trust unless explicit authority exists for them to do so. Explicit authority comes either from the charity's governing document, or from express permission being granted from an appropriate authority (for example, the Charity Commission). This concept extends to remuneration, as well as other types of transaction, although trustees may be reimbursed for legitimately incurred expenses. Further guidance is available in the Charity Commission publication CC11 *Trustee expenses and payments*. The engagement team should consider these requirements when planning the audit approach, including the impact on materiality.

Trading issues and taxation

43.44 Although charities are not exempt from tax (including VAT), they do enjoy significant tax advantages, particularly in respect of income and capital gains in relation to their primary charitable objectives. In the event that income is not eligible for such reliefs, significant tax liabilities may accrue. Non-compliance with tax regulations may give rise to significant fines being incurred and in the event that income and gains are not applied for charitable purposes, any tax relief may be lost (meaning understatement of expenditure is a risk). The impact of fines or a tax assessment, potentially going back over a number of years, may give rise to a risk to the appropriateness of the going concern assumption. Engagement teams, therefore, need to have an adequate understanding of the relevant tax obligations and reliefs.

43.45 While the subsequent payment of tax due and penalties may not be irregular as a breach of general legislation, incurring a significant penalty would be considered an 'incident of material significance' that the charity should notify their regulator of (see the section later in this Chapter entitled 'Laws and regulations'). It may also be a matter which the engagement team should consider reporting to HMRC as the relevant authority if considered to be in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022). Further guidance is provided in Chapter 31: Consideration of laws and regulations and reporting to regulators.

Heritage assets

43.46 A number of the NAO's charitable audited entities hold significant portfolios of heritage assets. In some cases, proportions of these portfolios have not been recognised in the charity's Balance Sheet due to the fact that they have taken the exemption from recognition set out in paragraph 34.53 of FRS 102 (2022) that, where the information required to value them is not available and cannot be obtained at a cost which is commensurate with the benefits to users of the financial statements, the assets shall not be recognised in the Balance Sheet.

43.47 Where this is the case, the engagement team should consider whether they are aware either of any valuations which may be used to recognise such assets or whether they are aware of any information which would indicate that it would be possible for the charity to obtain a valuation of such assets at a reasonable cost, commensurate with the benefits to the users of the financial statements.

43.48 The specialist nature of heritage assets mean that they are often held on the Balance Sheet at a valuation obtained by a management's expert who is a leading expert in the field. In placing reliance on such experts, the engagement team should have regard for the guidance in Section 12: Use of experts and should also consider whether they possess the necessary skill and knowledge to be able to effectively challenge the work of the expert.

43.49 Obtaining assurance over the existence of heritage assets may be a challenge where such assets are on loan or not held at the charity's principal location. In such circumstances, it may be appropriate for the audited entity to provide photographic evidence of the existence of such assets, provided that such photos contain both the asset and evidence that the photograph was taken at a date on or after the reporting date. In reviewing such evidence, the engagement team should consider the reliability of the evidence and potential for management to manipulate photographic evidence.

Senior remuneration disclosures

43.50 ***Consultation required*** It may be the case that charities include disclosures of senior remuneration within the body of the financial statements rather than in the other information, either voluntarily or as a requirement of their accounts direction. If an audited charity proposes to do this, the engagement team should consult FAPQ on the implications for the audit approach: for example, the engagement team's risk assessment procedures carried out in accordance with ISA (UK) 315 (Revised July 2020) *Identifying and assessing the risks of material misstatement* would need to cover these disclosures.

Laws and regulations

43.51 Charities registered with the Charities Commission or exempt charities under a designated regulator are subject to regulation.

43.52 In accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022), the engagement team should obtain sufficient appropriate audit evidence regarding compliance with the provisions of those laws and regulations generally recognised to have a direct effect on the determination of material amounts and disclosures in the financial statements. Further guidance is provided in Chapter 31: Consideration of laws and regulations and reporting to regulators.

43.53 Users of the financial statements of a charity will reasonably expect that the transactions recorded within them are authorised by the governing document of the charity and are in furtherance of the charity's objects. In order to give a true and fair opinion, due regard needs to be given to disclosure of any significant non-compliance. Engagement teams should, therefore, confirm that transactions fall within the stated objects of the charity as part of their audit work to support the (true and fair) opinion on the financial statements.

43.54 In accordance with ISA (UK) 250B (Revised November 2019), the auditor of a regulated entity should bring information on a breach of regulation of which the auditor has become aware in the ordinary course of the audit to the attention of the regulator when it is relevant, and of material significance, to the regulator (i.e., in the context of the regulator exercising its regulatory functions).

43.55 Whilst ISA (UK) 250B (Revised November 2019) does not directly apply to the audit of charities, engagement teams are expected to follow the guidance set out within it when considering the need to exercise any statutory or other reporting duties to the Charity Commission, the Office of the Scottish Charity Regulator (OSCR) or the Charity Commission for Northern Ireland. Practice Note 11 (Revised) provides further guidance on this.

43.56 The legislative basis for the (registered) charity auditor's statutory duty to report is Sections 156 to 159 of the Charities Act 2011. There is also practical guidance on reporting issues for auditors on the Charity Commission website (links are provided in the following paragraphs). While there is no legal requirement on auditors of exempt charities to report to the principal regulator, the auditors of exempt charities are expected to apply the principles set out here in determining whether to report non-compliance to the regulator.

43.57 Trustees also have a duty to report 'serious incidents'. For example, Charity Commission guidance on reporting serious incidents notes that trustees should report an incident even if already reported to the police or another regulator. The guidance gives a guide that the Commission would expect any loss of funds or property should be reported where its value totals £25,000 or more, or totals less than £25,000 but is in excess of 20% of the charity's income.

43.58 Where matters would be reportable by trustees as a 'serious incident' it is expected that the matter would also be of 'material significance' for the auditor to report. The duty for the auditor to report applies whether or not the matter has already been notified by the trustees of a registered charity to the Charity Commission. However, if the trustees have reported the incident, it is likely that the auditor's report can be much less substantial (it might state that the engagement team is aware of the incident, referring to the fact that it has already been reported and that there are no further details to add, or that the engagement team are aware of inconsistencies in the trustees' report, if any).

43.59 The Charity Commission, the Office of the Scottish Charity Regulator (OSCR) and the Charity Commission for Northern Ireland have issued Matters of Material Significance reportable to UK charitable regulators: Guidance for auditors and independence examiners. This provides practical guidance on reporting matters of significance to the relevant charity regulator as well as setting the clear expectation and principle of "if in doubt, report it". This guidance also sets out the following nine matters of material significance which the regulators consider to be reportable:

- dishonesty and fraud;
- internal controls and governance;
- money laundering and criminal activity;
- support of terrorism;
- risk to charity's beneficiaries;
- breaches of the law or the charity's trusts;
- breach of an order or direction made by a charity regulator;
- modified audit opinion or qualified independent examiner's report; and
- conflicts of interest and related party transactions.

43.60 ***Consultation required*** If the engagement team believes a statutory report is needed, they should consult FAPQ for confirmation that the matter requires reporting. The 'Reporting Matters of Material Significance to Charity Regulators' section of Practice Note 11 (Revised) provides guidance for engagement teams to make such a report.

43.61 Chapter 31: Consideration of laws and regulations and reporting to regulators provides further guidance on factors to consider when considering making a report to a regulator (including the charities regulator) and the documentation requirements for this.

Charities and groups

43.62 Charities may have UK and/or overseas branches or the charity may have a group structure, including, for example, trading subsidiaries, joint ventures and associates. The engagement team are responsible for forming an opinion on all the charity's activities. Depending on the circumstances, engagement teams may, therefore, need to obtain evidence from, or place reliance on, the work of other audit firms to gain the assurance they need. For further details on using the work of another auditor, see Chapter 25: Group audit procedures.

43.63 Where charities have trading subsidiaries, it is common for their profits, or a proportion of their profits to be paid as gift aid to the parent charity. Under FRED 68, which has subsequently been incorporated into both FRS 102 (2022) and the Charities SORP, for accounting periods beginning on or after 1 January 2019, such gift aid income may only be recognised by the parent charity at the point at which there is a legal obligation on the trading subsidiary to make the gift aid payment to its parent.

43.64 ***Consultation required*** Such a legal obligation may exist through a formal deed of covenant or legal agreement to make the gift aid payment that is in place prior to the end of the reporting period. Where engagement teams find themselves in dispute with other firms – for example, the auditors of trading subsidiaries or contractor audit firms – surrounding accounting judgments on this issue, they should consult FAPQ.

43.65 A legal opinion has been obtained by the ICAEW that gift aid payments made by the trading subsidiary companies of charities meet the definition of distributions under Section 829 of the Companies Act. Therefore, any such payments made by trading subsidiaries which exceed their profits available for distribution constitute unlawful distributions. Such unlawful distributions are recoverable by the trading subsidiary and should be disclosed as such within their financial statements.

43.66 ***Consultation required*** Furthermore, where such unlawful distributions have been made, the engagement team should consider the regularity implications (where a regularity opinion is provided) and whether a report should be made to a third party in the public interest in accordance with ISA (UK) 250A (Revised November 2019) (Updated May 2022). Further guidance on non-compliance with laws and regulations can be found in Chapter 31: Consideration of laws and regulations and reporting to regulators. Any instances of such unlawful distributions being made must be referred to FAPQ.

Public interest

43.67 Charitable government bodies may be subject to greater levels of public interest than non-charitable bodies of equivalent size, by virtue of the fact that they may be in receipt of donations made directly by the public, as well as tax or lottery funding. The level of public interest should also be taken into account when materiality levels are considered from planning the audit onwards.

Regularity, the framework of authorities and related issues

43.68 The general elements of the framework of authorities for charitable public bodies will be the same as for other public bodies: i.e.: authorising legislation (the specific legislation, such as a Royal Charter, that sets the body up), governing legislation (regulations specific to the entity that state how it should carry out specific activities) and HM Treasury and related authorities (such as Managing Public Money). Further guidance is available in Chapter 11: Determining the framework of authorities.

43.69 Breaches of charities law may put a statutory duty on the auditor to report, but these are not irregular in themselves. For example, where a charitable NDPB makes transactions that do not fall within the stated objects of the charity, it will be the fact that public money should only be used for those purposes approved by Parliament that causes the income or expenditure to be irregular. Where the allowed activities for the entity, as set out in legislation, differ to those charitable objectives registered with the regulator, it is only to the extent that money has not been spent on allowed activities (i.e., not in accordance with authorising and governing legislation) that irregular transactions will arise.

43.70 Managing Public Money provides guidance relevant to charities such as Accounting Officers' responsibilities, regularity and propriety, novel and contentious payments, and losses and special payments.

Identifying those charged with governance

43.71 Those charged with governance in relation to a charity will include, at a minimum, the board of trustees who are collectively charged with governance.

Reporting to trustees and regulators

43.72 In addition to the normal requirements of ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance*, charity auditors notify trustees of all breaches of duties relevant to the administration of the charity identified during the course of their work. Breaches should be reported regardless of whether the matter gave rise to a statutory duty to report to the charity regulators. Such notification normally takes place in the course of assessing the consequences of each particular breach. However, engagement teams may also summarise such breaches in their report of audit matters to those charged with governance.

43.73 As set out in Chapter 31: Consideration of laws and regulations and reporting to regulators, the procedures and guidance in ISA (UK) 250B (Revised November 2019) should be adapted to circumstances in which the auditor of other types of entity (i.e. other than those in the financial services sector), such as charities, becomes aware of a suspected instance of non-compliance with laws or regulations which the auditor is under a statutory duty to report.

43.74 In forming an opinion, the engagement team will normally seek to reach agreement with the trustees on the circumstances giving rise to a report and to understand whether they intend to make a report. ISA (UK) 250B (Revised November 2019) also requires the auditor to bring the matter to the attention of the regulator as soon as practicable. However, ISA (UK) 250B (Revised November

2019) requires the auditor to report to the regulator without informing those charged with governance in advance, where the issue identified casts doubt on the integrity or competence of those charged with governance.

43.75 Additionally, in the case of money laundering suspicions, to ensure that "tipping off" does not occur, the engagement team cannot undertake to inform trustees in advance of every matter which it brings to the regulator's attention. Further guidance may be found in Chapter 30: Fraud responsibilities.

Licences, training and support

43.76 Under the NAO's engagement risk management procedures, Engagement Directors are responsible for ensuring that the appointed team is capable and competent to carry out the audit. Due to the specialist nature of Charities SORP accounts, the Engagement Directors and Engagement Managers auditing these accounts are required to apply for a Charities SORP licence on an annual basis, following the process set out in Chapter 12: Roles, delegations and licences.

43.77 The Engagement Director and Engagement Manager should also consider as part of establishing the overall audit strategy whether it is necessary to provide particular training or support to engagement team members to enable them to perform an efficient and effective audit of a charity.

Concluding, reporting and filing

43.78 The duty to file accounts and the trustees' annual report with the Charity Commission applies to all charitable incorporated organisations irrespective of income and to all other registered charities whose gross yearly income exceeds £25,000. Where possible, prior to the audited entity filing the accounts with the Charities Commission, the engagement team should compare the final audited accounts to version for filing. This comparison should ensure that the version to be filed is consistent with the audited version and that the version to be filed is of sufficient quality to be understandable when scanned in.

Chapter 44: Pension schemes

Relevant standards and guidance

44.1 Practice Note 15 (Revised) *The audit of occupational pension schemes in the United Kingdom* provides guidance on applying ISAs (UK) to the statutory audit of trust-based occupational pension schemes established under the Pensions Acts in the United Kingdom. Much of the guidance may also assist auditors of public sector pension schemes, although these schemes are subject to different financial reporting frameworks and different legislation.

44.2 Some of the guidance in Practice Note 15 (Revised) is not relevant to NAO audits: in particular, that relating to reporting on contributions to the pension scheme and on reporting to The Pensions Regulator, as the C&AG is not appointed under the Pensions Act 1995. However, the guidance on auditor reporting, reliance on third parties and going concern remain of central relevance to the NAO's work and the NAO is subject to other requirements which may require reporting to The Pensions Regulator. Specifically, ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector* deals with the circumstances in which the auditor of an entity subject to statutory regulation (a "regulated entity", which includes regulated pension schemes) is required to report direct to a regulator information which comes to the auditor's attention in the course of the work undertaken in the auditor's capacity as auditor of the regulated entity – further guidance on these requirements is provided in Chapter 31: Consideration of laws and regulations and reporting to regulators.

Background

44.3 Auditing pension scheme accounts and pension-related transactions and balances can be complex. The scope of the audit, the financial framework and applicable auditing guidance can vary. ***Figure 44A*** below shows how the engagement scope and financial reporting framework of pension scheme audits can differ depending on the type of scheme and the engagement team's role.

Figure 44A: Engagement scope and financial reporting framework for the auditor's role in auditing pension schemes

<table>
<tr><th colspan="3">Is the pension scheme audited as a separate engagement?</th></tr>
<tr><th colspan="2">Yes</th><th>No</th></tr>
<tr><th colspan="2">Does the pension scheme prepare Resource Accounts?</th><td rowspan="2">Audit of the accounts of an employer participating in a defined benefit pension scheme where the share of the assets liabilities can be separately identified</td></tr>
<tr><th>Yes</th><th>No</th></tr>
<tr><td>Pension scheme Resource Accounts</td><td>Other pension scheme accounts</td><td></td></tr>
<tr><td>Appointed under the Government Resources and Accounts Act 2000.

Financial reporting in line with the FReM.</td><td>Most are statutory appointments under specific legislation (the C&AG does not hold any audit appointments under the Pensions Act 1995).</td><td>Scope dependent on underlying engagement.

Financial reporting in line with IAS 19.</td></tr>
</table>

	Financial reporting in line with the FReM or the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom. Additional auditing guidance given in Practice Note 15 (Revised).	

Central review of GAD

44.4 The Government Actuary's Department (GAD) provides actuarial services for all pension scheme resource accounts. The Pensions Centre of Expertise commissions one of the firms on the Specialist Audit Services Framework to complete an annual, central review of the GAD, to allow teams to use the work of GAD as audit evidence. FAPQ and the Pensions Centre of Expertise jointly communicate the scope of this review to line teams in an annual FAB. The aim of the central review is to confirm that the GAD has the professional skills and expertise to provide IAS 19-compliant pension liability valuations and related disclosures to NAO clients.

44.5 The central review covers those aspects of considerations required under ISA (UK) 500 (Updated May 2022) which address the general work and procedures of the actuary as they apply to all schemes. For the main unfunded public sector schemes, the review also includes the application of the GAD's procedures to establish the data, methodology and assumptions required for the valuation of these specific schemes.

44.6 The engagement team should undertake procedures to gain assurance over those areas not included in the scope of the central review of GAD's work. These include the requirements covering the actions of scheme managers, communication with the actuary, consideration of significant changes to the pension scheme, and assessment of the disclosures in the accounts.

44.7 The engagement team should confirm that the source membership data used by GAD is complete and can be reconciled to the records held by scheme administrators. It will not normally be sufficient to rely solely on the central review. Although the latter considers the procedures undertaken by GAD to validate and assess the reasonableness of the scheme data, which involves a year-on-year comparison of the scheme data provided by the administrators, it does not include reconciling the data used by GAD back to source data.

Pension schemes producing accounts

44.8 The unfunded nationally-administered public service pension schemes are authorised by statute. The relevant Minister makes the rules for each scheme.

44.9 These schemes are 'unfunded', in that assets are not accumulated in advance of the benefits paid. Instead, they pay contributions to the Consolidated Fund and benefits are paid on an annual basis through the Supply Estimates process. In circumstances where there is a surplus of contributions in excess of benefits paid, that surplus is surrendered to the Consolidated Fund.

44.10 Unlike for private sector pensions, these schemes are not established under trust law and there are no trustees. The Principal Accounting Officer or delegated Accounting Officer for an Arm's Length Body with responsibility for the scheme appoints a Scheme Manager. Although the relevant departmental audit committee advises the Accounting Officer on scheme governance, all of the schemes also have a pension board, which is a statutory requirement and is responsible for scheme governance, as well as overseeing the administration and performance of the scheme, compliance with laws and regulations, Pensions Ombudsman cases and other matters.

44.11 These schemes prepare resource accounts in accordance with the FReM. Under the Government Resources and Accounts Act 2000, the C&AG is the statutory auditor of all the nationally-administered unfunded public service pension schemes.

44.12 The C&AG's audit certificate expresses an opinion on pension resource accounts in the same format as for other resource accounts. Unlike the opinion on pension accounts governed by the Pensions Act 1995, the C&AG is not required to provide a separate opinion on pension contributions.

44.13 Outside of central and local government, scheme auditors are generally appointed under the Pensions Act 1995. Under that legislation, auditors report whether, in their opinion, contributions have been paid in line with the scheme's payment schedule or schedule of contributions. In addition, auditors report whether, in their opinion, the accounts show a true and fair view and whether they contain specific information set out in law, and with guidelines set out in the Pensions SORP.

Auditing pension scheme resource accounts

44.14 Pension scheme arrangements, including for unfunded nationally-administered schemes that produce resource accounts, are often complex. The engagement team should engage early in the planning process to understand roles and responsibilities, assess the competence and objectivity of the actuary, and understand the communication channels and whether a different materiality applies to the actuary's work (further guidance on setting materiality for pension scheme accounts is provided in the section later in this Chapter entitled 'Materiality').

44.15 The engagement team should consider the risks in relation to the quality, completeness and supportability of the membership records on which the member benefits and scheme liabilities are based. This is particularly relevant for schemes with a multi-employer structure, such as the Teachers' Pension Scheme or the Civil Service pension arrangements, which presents a significant administrative challenge for scheme administrators in terms of obtaining accurate and timely employee data.

44.16 In order to gain the required level of assurance, the engagement team should:

- ensure the accuracy of the source (membership) data feeding into the calculation of the liability;
- review the major actuarial assumptions used to derive the estimate of the liability; and
- assess the consistency of the actuary's work in line with the engagement team's knowledge of the business and other procedures.

44.17 The engagement team should obtain sufficient, appropriate evidence to take assurance over the membership data used by the actuary. It is management's responsibility to gain assurance over the sufficiency, relevant and reliability of this data, and management should provide engagement

teams with the evidence required to support this data. Where there are deficiencies in this evidence, the engagement team should determine whether further procedures are required to gain the required level of assurance.

Auditing pension scheme accounts

44.18 The C&AG only acts as the auditor for a small number of pension schemes that do not prepare resource accounts.

44.19 NAO engagements are statutory, with the scope of the audit established in scheme specific legislation rather than in the Pensions Act 1995. Unlike auditors appointed under the Pensions Act 1995, therefore, the C&AG does not express an opinion on contributions.

44.20 Where the scope of the audit includes, or potentially includes an opinion on contributions, the engagement team may consult with FAPQ.

44.21 As set out in Chapter 12: Roles, delegations and licences, for audits where specialist licences are relevant (including audits of pension scheme accounts), holding the relevant licence (for pension scheme accounts, an Occupational Pension Scheme licence) is normally a requirement for Engagement Managers and Engagement Directors undertaking the assignment. The Engagement Manager should hold the relevant licence or be supervised by an Engagement Director with the licence.

Licences, training and support

44.22 Under the NAO's engagement risk management procedures, Engagement Directors are responsible for ensuring that the appointed team is capable and competent to carry out the audit. Due to the specialist nature of pension scheme accounts, the Engagement Directors and Engagement Managers auditing these accounts are required to apply for an Occupational Pension Scheme licence on an annual basis, following the process set out in Chapter 12: Roles, delegations and licences.

44.23 The Engagement Director and Engagement Manager should also consider as part of establishing the overall audit strategy whether it is necessary to provide particular training or support to engagement team members to enable them to perform an efficient and effective audit of a pension scheme account or pension-related transactions and balances.

Risk assessment and response planning

44.24 Pension scheme arrangements are often complex. The engagement team should engage early in the planning process to understand the roles and responsibilities of, and the communication channels between, the different parties.

44.25 The Risk Assessment in Apex incorporates risks of material misstatement relating to pension schemes and pension balances and disclosures in audited entities' accounts. The engagement team should incorporate these into their risk assessment and design appropriate responses, in line with the processes set out in Chapter 17: Risk assessment and response planning.

44.26 Engagement teams for audits of pension schemes or audits involving significant pension balances and disclosures should explicitly consider the need for specialist support in relation to pensions, in line with the processes set out in Section 12: Use of experts.

44.27 For contracted-out audits of pension schemes or of audited entities that have significant pension balances and disclosures, engagement teams should have regard to the pensions-related content in the Risk Assessment in Apex when reviewing the quality and sufficiency of risk assessment procedures performed by the contractor firm.

Defined benefit pension balances – assurance over scheme liabilities

44.28 In order to gain assurance over scheme liabilities, the engagement team should:

- gain assurance over the accuracy of the source data feeding into the calculation of the liabilities;
- review the major actuarial assumptions used to derive the estimate of the liabilities; and
- assess the consistency of the actuary's work in line with the engagement team's knowledge of the business and other audit procedures.

44.29 The engagement team should obtain sufficient, appropriate evidence to gain assurance over the source data behind the valuation of the liability. It is management's responsibility to gain assurance over the sufficiency, relevant and reliability of this data, and management should provide engagement teams with the evidence required to support this data. Where there are deficiencies in this evidence, the engagement team should determine whether further procedures are required to gain the required level of assurance.

44.30 Where the engagement team uses the work of a pension scheme auditor, they should consider the impact of the pension scheme auditor's own materiality level. If the pension scheme auditor is carrying out their audit to a higher materiality level, the engagement team may need to either request the pension scheme auditor to perform additional work or to perform further work. The engagement team should also perform sufficient review of the pension scheme auditor's work and consider any differences between the scope of the pension scheme auditor's risk assessment and the engagement team's own risk assessment.

Defined benefit pension balances – assurance over scheme assets

44.31 Where appropriate and efficient, the engagement team should use the work of the pension scheme auditors to gain assurance over the scheme assets. Where this approach is not possible, the engagement team should undertake additional procedures to gain sufficient assurance.

44.32 The engagement team should consider testing investments and other assets in the same way as if the investment were separately disclosed on the Statement of Financial Position.

44.33 Engagement teams should perform procedures to obtain sufficient and appropriate evidence to assess whether the valuation of pension assets is appropriate and reflects their fair value.

- The Risk Assessment in Apex, along with the associated Content Library, includes guidance to enable teams to determine an appropriate approach to obtaining assurance over scheme assets for defined benefit pension schemes.

Guidance and procedures issued by the Pensions Centre of Expertise

44.34 Guidance on audit procedures in specific scenarios, as well as the impact of pensions sector developments on financial statement audits, is provided on the Pensions Centre of Expertise page on Sharepoint.

44.35 Engagement teams auditing pension schemes and pension balances and disclosures in audited entities' accounts are required to comply with procedures mandated by the Pensions Centre of Expertise. These matters are incorporated as content in the Risk Assessment in Apex and the Content Library.

Materiality

44.36 The engagement team should determine materiality following the requirements of ISA (UK) 320 (Revised June 2016) (Updated May 2022) *Materiality in planning and performing an audit* and the guidance in Chapter 16: Materiality, performance materiality and trivial threshold.

44.37 For the audit of pension scheme accounts, it is typically appropriate to set materiality for the financial statements as a whole using the gross pension liability as a benchmark, as this is generally a focus of user interest in the financial statements. For these accounts, benefits paid and contributions received are typically treated as particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements, in which case the engagement team should determine the materiality level or levels to be applied for those particular classes of transactions, account balances or disclosures in accordance with paragraph 10 of ISA (UK) 320 (Revised June 2016) (Updated May 2022).

44.38 Where defined benefit pension balances are included in employers' accounts, the determination of materiality should take account of the entity's other activities in addition to the pension scheme.

44.39 Guidance on setting materiality where assets and liabilities on the balance sheet are much larger than expenditure and income transaction streams is given in the section entitled 'Areas with reduced materiality' in Chapter 16: Materiality, performance materiality and trivial threshold. In the context of pension scheme accounts, this guidance may be applied by considering benefits paid rather than expenditure.

Defined benefit scheme transactions and balances within employer accounts

44.40 Participating employers normally recognise defined benefit pension scheme deficits in their financial statements. Defined benefit pension scheme surpluses are recognised in circumstances where accounting standards (such as IAS 19 and IFRIC 14) allow for this.

44.41 For defined benefit pension schemes with a single participating employer, the employer's financial statements normally recognise the assets and the liabilities for which the employer is responsible, along with the actuarially assessed current service cost. For employers preparing their accounts in accordance with the FReM and IFRS, the relevant standard is IAS 19 *Employee*

benefits. For those preparing their accounts in accordance with UK GAAP the relevant standard is Section 28 (‘employee benefits’) of FRS 102 (2022).

44.42 For defined benefit schemes with more than one participating employer, the employer only recognises an asset and liability where its share of these can be individually identified with sufficient certainty. Where this is not the case (for example, in the case of the Principal Civil Service Pension Scheme), the employer does not recognise assets and liabilities and simply accounts for contributions as they fall due.

Chapter 45: Public Interest Entities

Relevant standards and guidance

45.1 The FRC's Glossary of Terms – Ethics and Auditing (Updated December 2019) defines a Public Interest Entity. This definition includes entities covered by the meaning of a Public Interest Entity codified in Section 494A of the Companies Act 2006.

45.2 Paragraphs 18-1, 24-2, 25-1 to 25-3, 30-1 to 30-2, A27-3 and A48-1 to A48-4 of ISQM (UK) 2 *Engagement quality reviews* set out requirements relating to Engagement Quality Review for Public Interest Entities.

45.3 Paragraphs 41-1 and 43-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* and the related application guidance set out responsibilities of the auditor of a Public Interest Entity relating to fraud.

45.4 ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector* deals with the circumstances in which the auditor of an entity subject to statutory regulation (which includes Public Interest Entities) is required to report direct to a regulator information which comes to the auditor's attention in the course of the work undertaken in the auditor's capacity as auditor of the regulated entity. This may include work undertaken to express an opinion on the entity's financial statements, other financial information or on other matters specified by legislation or by a regulator.

45.5 Paragraphs 11-1, 16-2, 17-1, 20-1, 21-1 and 23-1 of ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance* and the related application guidance set out the requirements for the auditor's additional communications with, and reporting to, those charged with governance of a Public Interest Entity.

45.6 Paragraph 19R-1 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks* and the related application guidance set out requirements for the auditor of a Public Interest Entity to assess the valuation methods applied to the various items in the financial statements, including any impact of changes of such methods, and communicate this assessment in the additional report to the audit committee.

45.7 Paragraph 8R-1 of ISA (UK) 510 (Revised June 2016) *Initial audit engagements – opening balances* and the related application guidance set out requirements for the auditor of a Public Interest Entity to obtain an understanding of the predecessor auditor's methodology.

45.8 Paragraph A22-2 of ISA (UK) 580 (Updated May 2022) *Written representations* sets out that the written representations requested by the auditor of a Public Interest Entity from those charged with governance are relevant to the auditor's communications in the additional report to the audit committee that all requested explanations and documents were provided by the entity.

45.9 Paragraphs 30-1 and 45-1 of ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* and the related application guidance require the auditor of a Public Interest Entity to communicate in the auditor's report in accordance with ISA (UK) 701 (Revised November 2019) (Updated May 2022) *Communicating Key Audit*

Matters in the independent auditor's report (paragraphs 13-1, A51-1, A53-1 and A59-1 of which include additional requirements for the auditor's report of Public Interest Entities) and to include other communications in the auditor's report.

45.10 The FRC's Revised Ethical Standard 2019 includes a number of additional requirements that apply specifically to Public Interest Entities.

Background

45.11 This Chapter sets out the additional requirements on auditors of Public Interest Entities (PIEs). In addition to these requirements, engagement teams auditing PIEs are required to comply with the remainder of the FAM, as applicable, in full.

45.12 ***Consultation required*** Where an existing audited entity has become a PIE, the engagement team should consult with FAPQ on the next steps to be taken.

Quality arrangements

45.13 The NAO's system of quality management, as set out in Section 3: Quality management, will also apply to the audit of PIEs. By their nature audits of PIEs are of greater interest to members of the public. Therefore, engagement teams are expected to be particularly mindful of the guidance on ensuring quality in the performance of the audit as set out in Section 3: Quality management.

45.14 Given the increased sensitivity and scrutiny around audits of PIEs, the Director, Audit Quality will appoint an Engagement Quality Reviewer (EQR) for every audit of the financial statements of a PIE.

45.15 An EQR for the audit of the financial statements of a PIE shall be subject to the qualification and skills requirements for all EQRs as set out in Chapter 7: Engagement Quality Review. However, in addition to this, an EQR for the audit of the financial statements of a PIE shall:

- be eligible for appointment as a Senior Statutory Auditor (a Responsible Individual); and
- Not be involved in any other way in the engagement for which they have been appointed as EQR.

45.16 Paragraphs 18-1, 24-2, 25-1 to 25-3, 30-1 to 30-2, A27-3 and A48-1 to A48-4 of ISQM (UK) 2 set out specific requirements for EQRs of PIEs. The circumstances set out in paragraph A48-1 of ISA (UK) 220 (Revised July 2021) (there are no matters to discuss with key audit partners, and the EQR concludes that a discussion with the key audit partners is therefore unnecessary, having documented the rationale for this decision) may apply in the context of NAO-audited PIEs, which may be relatively small or straightforward.

45.17 Paragraphs 11 to 13 of the Financial Reporting Council's Staff Guidance Note SGN 02/2018 set out further requirements in relation to Engagement Quality Review for PIEs.

Performance and documentation requirements – additional requirements for audits of Public Interest Entities

45.18 In accordance with paragraphs 24-1 to 24-2, 25-1 to 25-3 and 30-1 to 30-2 of ISQM (UK) 2, for audits of Public Interest Entities (PIEs), the following policy requirements apply:

- An EQR should be performed in accordance with ISQM (UK) 1 to assess whether the key audit partner(s) could reasonably have come to the opinion and conclusions expressed in the draft of those reports before the auditor's report and the additional report to the audit committee are issued.
- Any disagreement between the key audit partner(s) and the EQR should be resolved in line with the procedure set out in the section of Chapter 6: Technical support and consultation entitled 'Other differences of opinion'.
- The EQR for the audit of a PIE should consider the following matters (for audits of group financial statements of PIEs, the EQR should additionally consider these matters for components and discuss the results of the review which each of the relevant key audit partners) and document their consideration and their conclusion thereon as appropriate:
    - the independence of the firm from the entity;
    - the significant risks which are relevant to the audit and which the key audit partner(s) has identified during the performance of the audit and the measures that the key audit partner(s) has taken to adequately manage those risks;
    - the reasoning of the key audit partner(s), in particular with regard to the level of materiality and the significant risks referred to in paragraph 25-1(b) of ISQM (UK) 2;
    - any request for advice to external experts and the implementation of such advice;
    - the nature and scope of the corrected and uncorrected misstatements in the financial statements that were identified during the carrying out of the audit;
    - the subjects discussed with the audit committee and management and/or supervisory bodies of the entity;
    - the subjects discussed with competent authorities and, where applicable, with other third parties; and
    - whether the documents and information selected from the file by the engagement quality reviewer support the opinion of the key audit partner(s) as expressed in the draft of the auditor's report and the additional report to the audit committee.
- The EQR should document:
    - the oral and written information provided by the key audit partner(s) to support the significant judgements as well as the main findings of the audit procedures carried out and the conclusions drawn from those findings, whether or not at the request of the EQR; and
    - the opinions of the key audit partner(s), as expressed in the draft of the reports required by ISA (UK) 260 (Revised November 2019) (Updated May 2022) and ISA (UK) 700 (Revised November 2019) (Updated May 2022); and
    - the results of the engagement quality review, together with the considerations underlying those results, in the audit documentation.

45.19 Performance of the above requirements should be documented in the EQR Response Group for PIEs.

Ethical considerations

45.20 Audits of the financial statements of PIEs are undertaken in accordance with the FRC's Revised Ethical Standard 2019, as applied to PIEs. Given the additional public interest in such entities, this places high expectations on auditors in the ethical standards which are required to be complied with in undertaking such engagements.

45.21 The engagement team should clearly state that the audit has been conducted in accordance with the FRC's Revised Ethical Standard 2019, as applicable to public interest entities, in the auditor's report, the additional report to the audit committee and any further reporting to those charged with governance.

45.22 All engagements, including the audit of PIEs, undertaken by the NAO are undertaken in accordance with the requirements of the FRC's Revised Ethical Standard 2019, as applied to listed entities. The Revised Ethical Standard 2019 introduces a number of additional requirements for the audit of PIEs.

Ethical considerations – engagement team rotation

45.23 The Engagement Director for the audit of the financial statements of a PIE shall cease their participation in the audit not later than five years from their date of appointment. They shall not participate in the audit of the PIE for a period of five years following their cessation as Engagement Director. This includes time spent participating in an audit engagement where the audit engagement has moved between firms.

45.24 Where an entity becomes a PIE, the length of time that the Engagement Director has served the entity in that role in total is taken into account when considering whether rotation is required. This would include the time period before the entity became a PIE.

45.25 However, where the Engagement Director has already been in post for more than four years at the point at which an entity becomes a PIE, they may remain in post for a further two years.

45.26 ***Consultation required*** In circumstances where the audit committee of a PIE decides that a degree of flexibility is required over the timing of rotation in order to safeguard audit quality, the Engagement Director may continue in post for a further two years, providing that no longer than seven years in total is spent in the position of Engagement Director. Any such circumstances must be approved by the Executive Director of Financial Audit based on a recommendation from the Director, Audit Operations, following review and approval by the Director, Audit Risk and Compliance and suitable safeguards will be implemented to mitigate any threats to independence or objectivity.

45.27 A gradual rotation mechanism should be established for the audits of PIEs. This rotation mechanism should constitute a succession plan encompassing the roles of Engagement Director, Engagement Manager and Engagement Team-Leader. Plans should be made to ensure that the Engagement Director, Engagement Manager and Engagement Team-Leader do not rotate off the audit at the same point. These succession plans should be agreed with People Directors, in consultation with the Financial Audit Operations team where appropriate, and clearly documented on the audit file.

Ethical considerations – audit fees

45.28 Where additional services or non-audit services are provided to PIEs subject to audit, its parent entity or subsidiaries, by either the NAO or by a contractor auditor who has been contracted to perform audit work in respect of the audit of the financial statements of the PIE, the total fees charged for such services provided to the PIE and its controlled undertakings shall be less than 70% of the average of the total fees charged for the audit of the PIE, the audit of its controlled undertakings and the audit of any consolidated financial statements in the previous three financial years. The services subject to this limit include the permitted services listed in paragraph 5.40 of the FRC's Revised Ethical Standard 2019, which are discussed in the following section, entitled 'Ethical

considerations – non-audit services' – as set out in that paragraph, other services should not be provided to PIEs.

Ethical considerations – non-audit services

45.29 Paragraph 5.40 of the FRC's Revised Ethical Standard 2019 sets out a number of permitted services that the NAO (or contractor firms, in relation to contracted out audits) can provide to PIEs, subject to the approval of the audit committee, after it has properly assessed threats to independence and safeguards applied. Services other than those set out described in that paragraph should not be provided to the PIE, its parent undertaking or controlled undertakings from any point preceding the start of the first accounting period, where the C&AG is the appointed auditor.

45.30 ***Consultation required*** The engagement team should consult the Director, Audit Risk and Compliance where a request has been made by the PIE to the NAO, or to a contractor firm to which the audit of the PIE or its parent undertaking or controlled undertaking has been contracted out, for prohibited non-audit services to be provided.

45.31 ***Consultation required*** The Engagement Director must consider the threats to independence in circumstances where a non-audit service is provided by a contractor firm involved in the audit of the PIE, its parent undertaking or controlled undertakings, to a controlled undertaking of a PIE which is audited by the C&AG which is based outside of the UK. The engagement team should consult the Director, Audit Risk and Compliance in such circumstances and appropriate safeguards will be put in place to mitigate any threats to independence.

45.32 If a non-permitted service is inadvertently provided, the NAO (or the contractor firm, in the case of a contracted-out audit) may continue to carry out the statutory audit of the PIE only if the engagement team can justify that the provision of services does not affect their professional judgment and the audit report. This must be reported in the Audit Completion Report.

Preliminary engagement activities

45.33 PIEs are subject to a greater level of public scrutiny than other entities and therefore audits of such entities carry additional reputation risk to the C&AG. A robust assessment of the engagement risk arising from the audit of a PIE should be undertaken by the engagement team. In particular consideration should be given as to whether the NAO have sufficient skills and expertise to undertake the engagement.

45.34 PIEs are subject to a wide range of regulatory requirements. As part of the processes set out in Chapter 15: Gathering entity initial information and Chapter 31: Consideration of laws and regulations and reporting to regulators, engagement teams should ensure that they have a sufficient understanding of the regulatory requirements applicable to the entity. This will include obtaining an understanding of any obligations placed upon the engagement team by the regulatory environment of the PIE. This consideration should be clearly documented in the Apex audit file.

45.35 As part of the engagement risk assessment process set out in Chapter 9: Engagement acceptance (statutory and non-statutory), the engagement team should consider whether they have the skills and capacity to comply with any regulatory requirements placed upon them by the

regulations which the PIE is subject to. This consideration should inform any engagement acceptance decision.

45.36 ***Consultation required*** The engagement team should consult FAPQ and the Legal and Policy teams where a further understanding of a PIE's regulatory environment or the obligations placed upon engagement teams by the regulatory environment is required.

45.37 The engagement team should seek to obtain assurance over the integrity of management and those charged with governance as part of the due diligence process undertaken prior to accepting the audit of the financial statements of a PIE. This will generally involve meeting with both management and those charged with governance to understand their qualifications and background. In addition, the engagement team should seek to corroborate this with desk-based research, such as checks of directorships held on the Companies House register.

45.38 The engagement team should seek to review the prior year working papers held by the predecessor auditor as part of the due diligence processes. This is undertaken both with the view of understanding the prior year audit methodology to fulfil the reporting requirements in the additional report to the audit committee and to consider whether this identifies any relevant factors which affect the engagement risk assessment. The engagement team should consider whether this review identifies any misstatement in the prior period comparative information in the current year financial statements.

45.39 The engagement team should perform an assessment of whether the audited entity meets the definition of a PIE as part of the preliminary engagement activities. This should be considered as part of the engagement acceptance procedures and in the context of the engagement risk to the C&AG from performing the audit.

45.40 The engagement team should consider whether there is any particular engagement risk arising from an entity's status as a PIE as part of the engagement acceptance process. In particular consideration should be given as to whether the engagement team has sufficient skills and knowledge of the entity's regulatory environment to perform the audit, as well as the C&AG's potential exposure to regulatory risk from the engagement.

45.41 Prior to accepting the engagement to audit the financial statements of a PIE, the engagement team should consider whether the C&AG is able to comply with the requirements of the Revised Ethical Standard 2019 applicable to PIEs (see the section earlier in this Chapter entitled 'Ethical considerations').

45.42 As part of the engagement acceptance process, the engagement team should consider whether any engagement risk is posed by issues concerning the integrity of members of the PIE's:

- supervisory, administrative and management bodies;
- Board; and
- audit committee.

Valuation methods and techniques

45.43 In accordance with paragraph 19R-1 of ISA (UK) 330 (Revised July 2017) (Updated May 2022), the engagement team should identify and assess the valuation methods applied by a PIE to the various items in the financial statements, including any impact of changes of such methods.

45.44 In accordance with paragraph A51-1 of ISA (UK) 330 (Revised July 2017) (Updated May 2022), this assessment should be included in the additional report to the audit committee, which is described in the section later in this Chapter entitled 'Reporting to those charged with governance'.

45.45 The engagement team should document in the Public Interest Entities Response Group in Apex the valuation methods, techniques or models employed for the purpose of preparing the PIE's financial statements methods and their assessment of their appropriateness and suitability. This assessment should be made based the work undertaken to obtain assurance over these valuation methods, as well as the PIE's disclosures surrounding the methods employed and uncertainties associated with these. The engagement team should also consider any changes in the valuation methodology employed since the prior year and factors which may lead to a change in the assessment of the valuation method compared to the prior year.

45.46 The work carried out by the engagement team that is described in Chapter 36: Accounting estimates may inform the engagement team's assessment and communication to the audit committee described in the preceding paragraphs.

45.47 The engagement team's assessment of a PIE's valuation methods should refer to the consideration undertaken as part of their work on the relevant 'method' Risks of Material Misstatement (RoMMs). Where these 'method' RoMMs were not considered or scoped-in within the Risk Assessment in Apex as part of the risk assessment process described in Chapter 17: Risk assessment and response planning, the engagement team should undertake further consideration to ensure the requirement in paragraph 19R-1 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) has been complied with. Where this assessment indicates that the risk assessment undertaken on the 'method' RoMMs was inappropriate, the engagement team should re-visit and update the Risk Assessment in Apex.

Fraud and irregularity

45.48 In accordance with paragraph A23-1 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements*, where the engagement team identifies or suspects non-compliance with laws and regulations, they may determine that a significant deficiency in internal control exists. In such circumstances, the requirements in ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* apply.

45.49 As set out in paragraph A29-1 of ISA (UK) 250A (Revised November 2019) (Updated May 2022), anti-money laundering legislation in the UK imposes a duty on the auditor to report suspected money laundering activity. There are similar laws and regulations relating to financing terrorist offences. The impact on the auditor of this legislation can broadly be summarised as follows:

- partners and staff in the firm are required to report suspicions of conduct which would constitute a criminal offence which gives rise to direct or indirect benefit; and
- partners and staff in the firm need to be alert to the dangers of 'tipping off' as this will constitute a criminal offence under the anti-money laundering legislation.

45.50 The Appendix to ISA (UK) 250A (Revised November 2019) (Updated May 2022) contains further guidance on the auditor's responsibilities in respect of money laundering, terrorist financing and proceeds of crime legislation in the UK.

45.51 In accordance with paragraph 16 of ISA (UK) 250B (Revised November 2019), when a matter comes to the engagement team's attention which they conclude does not give rise to a statutory duty to report but nevertheless may be relevant to the regulator's exercise of its functions, the engagement team should consider whether the matter should be brought to the attention of the regulator under the terms of the appropriate legal provisions enabling the auditor to report directly to the regulator and, if so, advise those charged with governance that in the auditor's opinion the matter should be drawn to the regulators' attention. Where the engagement team is unable to obtain, within a reasonable period, adequate evidence that those charged with governance have properly informed the regulator of the matter, the engagement team should make a report direct to the regulator as soon as practicable.

45.52 As set out in paragraph 42 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), unless all of those charged with governance are involved in managing the entity, if the engagement team has identified or suspects fraud involving:

- management;
- employees who have significant roles in internal control; or
- others where the fraud results in a material misstatement in the financial statements,

the engagement team should communicate these matters with those charged with governance on a timely basis. If the engagement team suspects fraud involving management, the engagement team should communicate these suspicions with those charged with governance and discuss with them the nature, timing and extent of audit procedures necessary to complete the audit. Such communications with those charged with governance are required unless the communication is prohibited by law or regulation.

45.53 ***Consultation required*** The engagement team should consult FAPQ where the engagement team has reported an actual or suspected irregularity (that is, an instance of non-compliance with laws and regulations, as distinct from irregular transactions for the purpose of the regularity opinion, which are transactions that are not in accordance with the framework of authorities) to management of a PIE but management has not taken any further action to investigate the irregularity. In such circumstances, in accordance with paragraph 44 of ISA (UK) 240 (Revised May 2021) (Updated May 2022), the engagement team has a duty to report such irregularities to the relevant authority responsible for investigating them.

45.54 Any reports of actual or suspected irregularities made by the engagement team to the relevant authorities shall not constitute a breach of any contractual or legal restriction on disclosure of information, in accordance with the Article 7 of Regulation (EU) 537/2014 of the European Parliament and Council, as amended by Regulation 82 of the Statutory Auditors and Third Country Auditors (Amendment) (EU Exit) Regulations 2019.

Statutory right and duty to report to regulators of public interest entities

45.55 The auditor of a PIE is required to establish an effective dialogue with the entity's supervising and credit institutions. This communication will be managed by FAPQ and any significant issues will be notified to the relevant engagement teams for consideration.

45.56 The engagement team should seek to understand and document the regulatory environment of the PIE as part of the risk assessment procedures. Based upon this understanding, the engagement team should consider areas whether a breach of regulatory requirements may be identified during the course of the audit.

45.57 The Engagement Director should ensure that all members of the engagement team are aware of the regulatory environment of the PIE and areas where a breach of these requirements may be identified during the course of the audit.

45.58 In accordance with paragraph 14 of ISA (UK) 250B (Revised November 2019), the engagement team should report promptly to the regulator any information concerning a PIE of which they have become aware while carrying out the audit and which may bring about any of the following:

- a material breach of the laws, regulations or administrative provisions which lay down, where appropriate, the conditions governing authorisation or which specifically govern pursuit of the activities of such PIE;
- a material threat or doubt concerning the continuous functioning of the PIE; or
- a refusal to issue an audit opinion on the financial statements or the issuing of an adverse or qualified opinion.

45.59 In accordance with paragraph 14(b) of ISA (UK) 250B (Revised November 2019), the engagement team should report any information referred to in the preceding paragraph of which they become aware in the course of carrying out the audit of an undertaking having close links with the PIE for which they are also carrying out the audit.

Reporting to those charged with governance

45.60 The auditor of a PIE is required to report additional information to those charged with governance to ensure that they are able to perform their functions adequately in light of the additional level of scrutiny faced by public interest entities. These additional reporting requirements are discharged through the preparation of an additional report to the audit committee of a PIE, as set out in ISA (UK) 260 (Revised November 2019) (Updated May 2022).

45.61 ***Consultation required*** This additional report to the audit committee must be a standalone document and may not cross-refer to information disclosed either in the auditor's report or within the audit completion report. A template is available to assist engagement teams in preparing the additional report to the audit committee. Additional reports for PIEs where the audit is contracted out or a two-tier or joint audit should be submitted to FAPQ for review.

45.62 The additional report to the audit committee of a PIE should be a reflection of the audit of the financial statements. It should therefore reflect the key matters and judgements documented within the audit file. The engagement team should take care to ensure that the information disclosed within the additional report to the audit committee is consistent with the documentation in the audit file, as well as the Audit Completion Report and auditor's report.

45.63 All significant deficiencies in the PIE's internal controls which have been identified during the course of the audit should be reported on in the additional report to the audit committee, regardless of whether or not management has taken action to resolve the deficiency. Nonetheless, the additional report to the audit committee should include a clear statement of whether or not such deficiencies have been resolved by management.

45.64 The engagement team is required to include within the additional report to the audit committee a confirmation that all relevant documents and explanations relevant to the audit have been provided. In providing this confirmation, the engagement team should consider whether the engagement team have obtained all written representations required from management and those charged with governance, particularly those included within the management letter of representation.

45.65 The additional report to the audit committee of a PIE is required to include a significant amount of additional information incidental to the performance of the audit. Sufficient documentation to support the additional report to the audit committee should be held within the Apex audit file. To support this, the engagement team should perform a data reconciliation of the additional report to the audit committee to the documentation held within the audit file.

45.66 In addition to the matters required to be included in the additional report to the audit committee of a PIE by paragraph 16-2 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), the additional report should also include:

- any threats to the auditor's independence and the safeguards which have been applied to mitigate those threats;
- the Directors who have been involved in the audit of the PIE, excluding any Directors whose involvement in the audit has solely related to consultation (for example, consultation with FAPQ or Centres of Expertise, or involvement in Audit Panels);
- for consolidated financial statements, details of any work performed by component auditors in support of the group audit; and
- any instances of non-compliance with the applicable legal or regulatory requirements relating to the statutory other information (director's report, strategic report, remuneration report and governance statement).

45.67 For the purpose of the confirmation required by paragraph 17-1(a) of ISA (UK) 260 (Revised November 2019) (Updated May 2022), the firm and partners, senior managers and managers conducting the audit includes:

- the C&AG;
- relevant Executive Directors; and
- the Engagement Director, the Engagement Manager and any other Directors and Managers who have been involved in the audit, excluding any Directors or Managers whose involvement in the audit has solely related to consultation (for example, consultation with FAPQ or Centres of Expertise, or involvement in Audit Panels).

45.68 Where the PIE is a group, the Group Engagement Team, as auditor the PIE will hold responsibility for the preparation of the additional report to the audit committee.

45.69 Where a PIE does not have an audit committee, the additional report to the audit committee should be submitted to the body performing equivalent functions within the entity.

45.70 The additional report to the audit committee of a PIE may not be submitted to the audit committee until the EQR has concluded their review.

45.71 As required by paragraph 20-1(c) of ISA (UK) 260 (Revised November 2019) (Updated May 2022), upon request by either the auditor or the audit committee, the engagement team shall discuss key matters arising from the audit referred to in the additional report to the audit committee, and in particular deficiencies communicated in accordance with paragraph 16-2(j) of ISA (UK) 260 (Revised November 2019) (Updated May 2022).

The auditor's report

45.72 There are a number of additional disclosures which should be included in the auditor's report on the audit of the financial statements of a PIE, as set out in ISA (UK) 700 (Revised November 2019) (Updated May 2022) and ISA (UK) 701 (Revised November 2019) (Updated May 2022).

45.73 The template Extended Auditor Report for companies will assist engagement teams in complying with these requirements, which are marked out as relevant to PIEs within the template. In addition to incorporating these, the engagement team should refer to Chapter 54: Overall conclusions and preparing the certificate or report when preparing the auditor's report.

45.74 The auditor's report should be a standalone document and should not cross-refer to information also disclosed in the additional report to the audit committee. However, engagement teams should seek to ensure that the auditor's report is consistent with the findings disclosed within the additional report to the audit committee. A statement to confirm this should be included within the auditor's report.

45.75 The engagement team should ensure that all evidence supporting the auditor's report is documented within the audit file. Engagement teams may find it helpful to perform a data reconciliation of the auditor's report to the documentation held on the audit file.

45.76 The auditor's report on a PIE may not be issued until the EQR has completed their review.

Resignation, removal and expiry of the audit term

45.77 The requirements when resigning as auditor of a PIE are similar to those of non-PIE companies (see Chapter 42: Companies). There is one slight difference, in that, under Section 519(1) of the Companies Act 2006, notice of resignation as auditor of a PIE must be accompanied by a statement of reasons for resignation regardless of what the reasons are.

Chapter 46: Service organisations and shared service centres

Relevant standards and guidance

46.1 ISA (UK) 402 (Updated May 2022) *Audit considerations relating to an entity using a service organisation* deals with the user auditor's responsibility to obtain sufficient appropriate audit evidence when a user entity uses the services of one or more service organisations. Specifically, it expands on how the user auditor applies ISA (UK) 315 (Revised July 2020) and ISA (UK) 330 (Revised July 2017) (Updated May 2022) in obtaining an understanding of the user entity, including internal control relevant to the audit, sufficient to identify and assess the risks of material misstatement and in designing and performing further audit procedures responsive to those risks. However, ISA (UK) 402 (Updated May 2022) does not apply to:

- services provided by financial institutions that are limited to processing, for an entity's account held at the financial institution, transactions that are specifically authorised by the entity, such as the processing of checking account transactions by a bank or the processing of securities transactions by a broker; or
- the audit of transactions arising from proprietary financial interests in other entities, such as partnerships, corporations and joint ventures, when proprietary interests are accounted for and reported to interest holders.

46.2 Paragraphs 1-90 to 1-96 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 402 (Updated May 2022) in the public sector.

46.3 International Standard on Assurance Engagements 3402 (ISAE 3402) *Assurance reports on controls at a service organisation* deals with assurance engagements undertaken by a professional accountant in public practice to provide a report for use by user entities and their auditors on the controls at a service organisation that provides a service to user entities that is likely to be relevant to user entities' internal control as it relates to financial reporting. It complements ISA (UK) 402 (Updated May 2022), in that reports prepared in accordance with ISAE 3402 are capable of providing appropriate evidence under ISA (UK) 402 (Updated May 2022). This standard has not been adopted formally by the Financial Reporting Council for the UK but can be drawn upon for best practice.

Background

46.4 A service organisation is a third-party organisation that provides services to "user entities" that are an integral part of the information systems supporting the financial reporting process, such as transaction processing (administration and collection of membership fees via a credit card payment mechanism) or payroll bureau services.

46.5 As set out in paragraph 2 of ISA (UK) 402 (Updated May 2022), many entities outsource aspects of their business to organisations that provide services ranging from performing a specific task under the direction of an entity to replacing an entity's entire business units or functions, such as the tax compliance function. Many of the services provided by such organisations are integral to the entity's business operations; however, not all those services are relevant to the audit.

46.6 As set out in paragraph 3 of ISA (UK) 402 (Updated May 2022), services provided by a service organisation are relevant to the audit of a user entity's financial statements when those services, and the controls over them, are part of the user entity's information system relevant to the preparation of the financial statements. Most controls at the service organisation are likely to relate to be part of the user entity's information system relevant to the preparation of the financial statements, or related controls, such as controls over the safeguarding of assets. A service organisation's services are part of a user entity's information system if these services affect any of the following:

- How information relating to significant classes of transactions, account balances and disclosures (COTABDs) flows through the user entity's information system, whether manually or using IT, and whether obtained from within or outside the general ledger and subsidiary ledgers. This includes when the service organisation's services affect how:
    - transactions of the user entity are initiated, and how information about them is recorded, processed, corrected as necessary, and incorporated in the general ledger and reported in the financial statements; and
    - information about events or conditions, other than transactions, is captured, processed and disclosed by the user entity in the financial statements.
- The accounting records, specific accounts in the user entity's financial statements and other supporting records relating to the flows of information relating to significant COTABDs.
- The financial reporting process used to prepare the user entity's financial statements from the records described in the previous bullet point, including as it relates to disclosures and to accounting estimates relating to significant COTABDs.
- The entity's IT environment relevant to the aspects listed above.

46.7 A shared service centre is where a number of bodies establish a service organisation to provide services to them. In the public sector, shared service centres may be part of another public body or outsourcing company.

46.8 If appropriate controls are in place at the service organisation (as well as the audited entity), there is potential to deliver more efficient audits across all those entities that utilise the service organisation. Regardless of the audit approach, there are particular matters that engagement teams should consider when an audited entity uses a service organisation, for example are there any additional risks of material misstatement. This may, for example, include weak controls over data migration from one system at a data centre/shared service centre to another new system which could increase the risk of material misstatement if there is no reasonable assurance on the completeness, accuracy and integrity of financial records migrated.

46.9 The engagement team needs to understand the arrangements the audited entity has in place in order to be able to plan our work and identify any risks arising from the use of a service organisation. The scope of their activities and the assurance arrangements that the entity has put in place will determine the appropriate audit response.

46.10 In some cases, the service organisation may have a “service auditor” provide an assurance report on their controls. The “service auditor” may be the NAO or an external audit firm which does not have a direct relationship with the NAO. This Chapter explains the audit considerations of the user auditor: i.e., the auditor of the user entity in receipt of the shared services, including how engagement teams might take assurance from the work of service auditors.

46.11 In other cases, there may be a “common function audit” where a centralised NAO audit provides internal assurances to one or more Engagement Directors covering a suite of audited

bodies. For example, a common payroll system may exist for a department and its agencies. Alternatively, a single review of an actuarial valuation may impact on many audited entities.

46.12 This differs from a shared services situation in so far as the common functions audit is undertaken on behalf of the user auditor, and not the service organisation. However, many of the principles are common between the two scenarios and this Chapter also explains how engagement teams might take assurance from common function audits.

Obtaining an understanding of the services provided by a service organisation, including internal control

46.13 Paragraphs 9 to 14 of ISA (UK) 402 (Updated May 2022) and the related application guidance set out how the engagement team should:

- obtain an understanding of how the user entity uses the services of a service organisation in the user entity's operations;
- evaluate the design and implementation of relevant controls at the user entity that relate to the services provided by the service organisation, including those that are applied to the transactions processed by the service organisation (it is only relevant to evaluate the design and implementation of controls at the user entity to the extent that ISA (UK) 315 (Revised July 2020) or otherwise this Manual requires the engagement team to evaluate the design and implementation of controls in place at the service organisation); and
- determine whether a sufficient understanding of the nature and significance of the services provided by the service organisation and their effect on the user entity's internal control relevant to the audit has been obtained to provide a basis for the identification and assessment of risks of material misstatement (for engagements involving a regularity opinion, this should also cover the identification and assessment of risks of material irregular transactions, where relevant).

46.14 This work is relevant to the understanding of the audited entity and its internal control which the engagement team is required to obtain under ISA (UK) 315 (Revised July 2020). It should be documented in the Understanding of Information Systems and Control Activity Components template.

46.15 The engagement team should document those of the controls identified as covering risks of material misstatement that are operated by the service organisation in tab '6) D&I Service Orgs' of the Understanding of Information Systems and Control Activity Components template, referring to the Type 1 or Type 2 report if available. If a service auditor report is not available, the engagement team may need to enquire directly with the service organisation to identify relevant controls.

46.16 The engagement team should also document elsewhere in the same template:

- all complementary user entity controls identified by the service organisation; and
- controls that the user entity implements over the processing performed by the service organisation.

46.17 From the work required above, and drawing on their risk assessment, the engagement team should identify the controls operated by the service organisation that they would expect to be operating effectively, in that either:

- they will reduce the extent of substantive testing; or
- substantive testing alone will be insufficient to address the Assertion-level risks.

46.18 Paragraphs 19 and A41 of ISA (UK) 402 (Updated May 2022) includes requirements regarding inquiry of management relating to fraud reported by the service organisation and evaluating these matters.

46.19 Even where an audited entity uses a service organisation, the engagement team may, having obtained an understanding of the services provided by the service organisation, seek to place reliance on controls operating at the user entity in addition to, or instead of, testing controls operating at the service organisation.

46.20 Paragraph 12 of ISA (UK) 402 (Updated May 2022) provides the following options where the engagement team is unable to obtain a sufficient understanding from the user entity. These options may involve the exercise of the C&AG's statutory access rights:

- obtaining a Type 1 or Type 2 report on the description and design of controls at a service organisation, if available (these are commonly performed under ISAE 3402 or SSAE 16 and may be referred to referencing those standards, but they are also commonly referred to as "SOC 1" and "SOC 2" reports – Type 1 and SOC 1, and Type 2 and SOC 2, refer to equivalent reports) (see the following paragraph for considerations around the sufficiency of evidence from such reports);
- contacting the service organisation, through the user entity, to obtain specific information;
- visiting the service organisation and performing procedures that will provide the necessary information about the relevant controls at the service organisation; or
- using another auditor (such as a common function auditor) to perform procedures that will provide the necessary information about the relevant controls at the service organisation.

The user entity's responsibilities for maintaining accounting records

46.21 Paragraphs A11-1 to A11-3 of ISA (UK) 402 (Updated May 2022) comment on the user entity's responsibilities for maintaining accounting records, even where using a service organisation.

46.22 Use of a service organisation does not diminish the ultimate responsibility of those charged with governance of a user entity for conducting its business in a manner which meets their legal responsibilities, including those of safeguarding the user entity's assets, maintaining adequate accounting records and preparing financial statements which provide information about its economic activities and financial position. In particular, for NAO audited entities, many of these remain the personal responsibility of the Accounting Officer, regardless of the use of the service organisation.

46.23 Engagement teams should consider the implications for the C&AG's opinion of such situations as are described in paragraph A11-2 of ISA (UK) 402 (Updated May 2022) (a user entity outsources the preparation of its accounting records to a service organisation and there is doubt as to whether the arrangements with a service organisation are such as to permit the user entity to meet its statutory obligations) and may consult with FAPQ as appropriate.

46.24 As set out in paragraph A11-3 of ISA (UK) 402 (Updated May 2022), the Companies Act 2006 is clear in requiring companies to "keep" accounting records. Consequently, whether a company 'keeps' records (as opposed to 'causes records to be kept') will depend upon the particular terms of the outsourcing arrangements and, in particular, the extent to which the company retains ownership of, has access to, or holds copies of, those records.

Planning the audit approach

46.25 When engagement teams use the work of a service auditor or common function auditor, this in effect replaces testing which they would otherwise need to perform.

46.26 The objectives of the other auditor's work may not match the NAO's in the context of the particular engagement. The nature, timing and extent of their work may not be precisely the same as

the engagement team would have planned themselves, although this risk can be managed through appropriate communication.

46.27 The risks of material misstatement (RoMMs) (but not necessarily their Likelihood – see the following paragraph) remain the same for each Financial Reporting Activity (FRA) where an audited entity uses a service organisation. However, depending on the scope of the service organisation's work, the service organisation may be responsible for either:

- preparing the subject matter relevant to the FRA; or
- operating control activities relevant to the FRA.

46.28 The use of a service organisation may increase the Likelihood assessment of RoMMs in areas where the service organisation undertakes activity for an audited entity. For example, if the use of a service organisation is leading to processing errors, or if controls in place at the service organisation and the user entity together would not suffice to prevent or detect material misstatements, this may increase the Likelihood of particular RoMMs.

46.29 Some of the key standards that impact upon this area of an audit have yet to be adopted formally by the Financial Reporting Council for the UK (except ISAE (UK) 3000), and so specific reference should be made in the Letter of Engagement and audit report to the standards used. These standards can be found at the links below:

- International Standard on Assurance Engagements (UK) 3000 (ISAE (UK) 3000) (July 2020) *Assurance engagements other than audits or reviews of historical financial information*
- International Standard on Review Engagements 2400 (ISRE 2400) (Revised) *Engagements to review historical financial statements*
- International Standard on Related Services 4400 (ISRS 4400) (Revised) *Agreed-upon procedures engagements*
- ISAE 3402 *Assurance reports on controls at a service organisation*
- ICAEW Audit and Assurance Faculty Technical Release TECH 01/20 AAF *Assurance on internal controls of service organisations*
- Other standards or certifications which the service organisation may have attained and can be used to provide limited assurance should be considered, such as ISO 27001/ISO 27002 *Information Security Management System Certification* or the Payment Card Industry Data Security Standard (PCI DSS).

46.30 Service auditors may adopt terminology derived from other auditing frameworks that are used in foreign jurisdictions and apply this terminology to similar concepts as are used in the standards listed above. For example, "System and Organization Controls" (SOC) reports are referred to in the US Statement on Standards for Attestation Engagements 18 (SSAE 18); these correspond to equivalent types of report in ISAE 3402, since SSAE 18 and ISAE 3402 share a common framework.

46.31 In addition to the standards listed above, dependent on the nature and scope of the work performed by the service auditor, ISA (UK) 800 (Revised October 2016) *Special considerations – audits of financial statements prepared in accordance with special purpose frameworks* and ISA (UK) 805 (Revised October 2016) *Special considerations – audits of single financial statements and specific elements, accounts or items of a financial statement* may also be relevant.

46.32 When establishing the Overall Audit Strategy, the Engagement Director and Engagement Manager should consider the impact of the use of a service organisation on the risk of material misstatement, including the risk of material irregularity and whether the use of the service organisation gives rise to IT-related risks. The migration to a shared service organisation may be a

significant risk for the audit and should be considered through the IT audit Financial Statements Level Risk Area.

46.33 The engagement team should determine and document whether sufficient appropriate audit evidence concerning the relevant financial statement assertions is available from records held at the user entity.

46.34 If sufficient appropriate audit evidence is not available from records held at the user entity, the engagement team should, in accordance with paragraph 15 of ISA (UK) 402 (Updated May 2022) plan to perform control and/or substantive procedures to obtain sufficient appropriate audit evidence or use a common function auditor (or other auditor, which would usually be the service organisation's auditor) to perform those procedures at the service organisation on their behalf.

46.35 The Engagement Director and Engagement Manager must use professional judgement in assessing whether the work of a service auditor or a common function auditor provides sufficient appropriate audit evidence, or whether additional testing should be performed.

46.36 As part of the engagement team's planning inquiries, they should inquire of management of the user entity whether the service organisation has reported to the user entity, or whether the user entity is otherwise aware of, any fraud, non-compliance with laws and regulations or uncorrected misstatements affecting the financial statements of the user entity.

46.37 The engagement team should communicate to those charged with governance how such matters affected the nature, timing and extent of our controls and substantive procedures as user auditor, including the effect on their conclusions and audit certificate/report.

46.38 The Engagement Director and Engagement Manager should consider whether the use of service organisations gives rise to IT-related risks. For example, the initial transfer of data on moving to a service organisation may be a significant risk for the audit. This may indicate the need to involve IT audit specialists as appropriate at an early stage.

46.39 Service organisation controls relevant to our audit may be dependent upon related IT general controls (ITGC) and IT application controls (ITAC) at the service organisation. Any work performed on service organisation controls should therefore take account of related IT general controls as a minimum. Where there may be a dependency on ITGCs or ITACs at the service organisation, the engagement team should consider whether it is appropriate to consult the IT Audit team to ensure that proper consideration has been made of any underlying ITGCs or ITACs.

Relying on the operating effectiveness of controls at the service organisation

46.40 The engagement team should consider and document whether it would be effective and efficient to rely on the operating effectiveness of controls at the service organisation. The engagement team will need to do so where they consider that sufficient assurance cannot be obtained from testing controls or from substantive testing alone at the user entity.

46.41 If the engagement team plans to rely on service organisation controls, they should follow the requirements of paragraph 16 of ISA (UK) 402 (Updated May 2022) and the related application guidance.

46.42 If the engagement team plans to use a Type 1 or a Type 2 report that excludes the services provided by a subservice organisation and those services are relevant to the audit of the user entity's

financial statements, the engagement team should follow the requirements of paragraph 18 of ISA (UK) 402 (Updated May 2022) and the related application guidance.

46.43 Where the audit plan includes an expectation of the operating effectiveness of controls operated at the service organisation, the engagement team should document their evaluation of the operating effectiveness of those controls in tab '10) OE Service Orgs' of the Understanding of Information Systems and Control Activity Components template, referring to the Type 2 report if available.

46.44 If a Type 2 report is available, the engagement team should:

- obtain the report;
- evaluate and document whether the description and design of controls at the service organisation is at a date or for a period that is appropriate for our purposes (i.e. not a report relating to a different financial year); and
- evaluate the adequacy of the time period covered by the tests of controls (performed by the service auditor) and the time elapsed since the performance of the tests of controls (by the service auditor). If there is a gap between the period covered by the Type 2 report and the period of account for the user entity, then either:
    - a "bridge" letter may be required from the service organisation's management; or
    - additional procedures should be performed to obtain assurance over the parts of the audited entity's period of account not included in the period covered by the Type 2 report.
    - ***Consultation required*** If the engagement team is in doubt as to what procedures are required to bridge any gap between the periods covered, they should consult FAPQ.
- The engagement team should also evaluate whether the tests of controls performed by the service auditor and the results thereof, as described in the service auditor's report, are relevant to the assertions in the user entity's financial statements and provide sufficient appropriate audit evidence to support the user auditor's risk assessment (i.e., whether the Type 2 report covers the relevant risks of material misstatement per the Risk Assessment in Apex).

46.45 If a service auditor report is not available, the engagement team should either:

- work directly with the shared service centre or third party service organisation to perform procedures to gain sufficient appropriate assurance over the operating effectiveness of controls identified as addressing Assertion-level risks of material misstatement; or
- use another auditor to perform procedures at the service organisation that test the operating effectiveness of those controls (see the section of this Chapter below entitled 'Requesting a common function auditor or other auditor perform work – controls work').

46.46 The engagement team should evaluate whether the tests of controls performed by the service auditor, and the results thereof as described in the service auditor's report, provide sufficient appropriate audit evidence to support their risk assessment. This includes relevant IT General Controls.

Using a Type 1 or Type 2 report as audit evidence

46.47 Paragraphs 13 to 14, and 17, of ISA (UK) 402 (Updated May 2022) and the related application guidance set out, respectively, requirements on the user auditor when using a Type 1 or Type 2 report as audit evidence to:

- support the user auditor's understanding of the service organisation; and/or
- provide assurance that controls at the service organisation are operating effectively (Type 2 only).

46.48 Where the engagement team is obtaining a Type 1 or Type 2 report in respect of regularity controls or requesting a non-NAO auditor perform work at a service organisation, they should ensure that the scope of work is sufficient to give assurance over regularity before taking assurance from the work. A summary of the key elements of Type 1 and Type 2 reports is included in the following section of this Chapter.

46.49 Where engagement teams are evaluating the sufficiency and appropriateness of the evidence provided by (Type 1 or Type 2) reports on internal controls at the service organisation, they should involve IT specialists as appropriate.

46.50 Engagement teams are not expected to re-perform controls testing at the service organisation where they can take assurance from a Type 2 report after considering the above requirements.

46.51 A Type 2 report may be intended to satisfy the needs of several different user auditors, and therefore its scope may be sufficient for our purposes. The engagement team should consider the following factors and perform (or request the service auditor perform) additional procedures if necessary:

- the time period covered by the tests of controls and the time elapsed since the performance of the tests of controls;
- the scope of the service auditor's work and the services and processes covered, the controls tested and tests that were performed, and the way in which tested controls relate to the user entity's controls; and
- the results of those tests of controls and the service auditor's opinion on the operating effectiveness of the controls.

46.52 As set out in paragraph 13 of ISA (UK) 402 (Updated May 2022), in determining the sufficiency and appropriateness of the audit evidence provided by a Type 1 or Type 2 report, the engagement team, as user auditor, should be satisfied as to:

- the service auditor's professional competence and independence from the service organisation; and
- the adequacy of the standards under which the Type 1 or Type 2 report was issued.

46.53 As set out in paragraph 14 of ISA (UK) 402 (Updated May 2022), if the engagement team, as user auditor, plans to use a Type 1 or Type 2 report as audit evidence to support the engagement team's understanding about the design and implementation of controls at the service organisation, the engagement team should:

- evaluate whether the description and design of controls at the service organisation is at a date or for a period that is appropriate for the engagement team's purposes;
- evaluate the sufficiency and appropriateness of the evidence provided by the report for the understanding of the controls at the service organisation; and
- determine whether complementary user entity controls identified by the service organisation are relevant to the user entity and, if so, obtain an understanding of whether the user entity has designed and implemented such controls.

Key elements of Type 1 and Type 2 reports (produced by service auditors)

46.54 Typically, a service auditor will be engaged by the service provider to undertake an assurance engagement in line with ISAE 3402 issued by the IAASB or SSAE 16 (US standard). Service auditors of public sector service organisations are being encouraged to adopt these standards. Reporting under ISAE 3402 results in one of two formats, which are compared in ***Table 46A*** below.

Table 46A: Comparative formats of Type 1 and Type 2 reports under ISAE 3402

	ISAE 3402 Type 1	ISAE 3402 Type 2
System description prepared by management at a specific point in time	Y	Y
Management assertion that: i) the system description is fairly presented; ii) controls mitigating the risks are suitably designed; iii) controls were operating effectively	Y Y N	Y Y Y
Audit opinion that the system description is fairly presented	Y	Y
Audit opinion regarding points (i) and (ii)	Y	Y
Audit opinion regarding assertion (iii)	N	Y
Description of tests performed by the auditor, and their results	N/A	Y

46.55 ***Consultation required*** Where placing reliance on ISAE 3402 reports, engagement teams should ensure they have obtained and reviewed the latest available reports before placing reliance on their internal controls. Where the latest available report available does not cover the entire period under audit, the engagement team should consult with FAPQ.

Requesting a common function or other auditor perform work

46.56 Teams requesting a common function auditor (or other auditor) perform work should follow the requirements in Chapter 25: Group audit procedures for taking assurance from another auditor's work, in particular to assess the professional competence and independence of the auditors performing the work.

46.57 The engagement team should agree in writing and record in the audit file the scope of common function work with the director overseeing the common function work. If the Engagement Director is also undertaking the common function work, then a formal note of the scope should be set out in the Apex audit file.

46.58 The Engagement Director should agree the form and content of the reporting with the common functions auditor at the planning stage. This must provide for self-standing sufficient and appropriate audit assurance to be retained on the Apex audit file. For central controls testing, an assurance report may be sufficient, along the lines of a Type 1 or Type 2 report. However, the Engagement Director must ensure that this addresses the risks specific to the user entity.

Requesting a common function or other auditor perform work – controls work

46.59 If the engagement team plans to take assurance from the work of a common function or other auditor as evidence on the design and implementation of service organisation controls, they should follow the requirements of paragraph 14 of ISA (UK) 402 (Updated May 2022) and the related application guidance.

46.60 If the engagement team plans to place assurance from their work as evidence of the operating effectiveness of controls, they should follow the relevant requirements of paragraphs 16 and 17 of ISA (UK) 402 (Updated May 2022) and the related application guidance. This work should include testing the operating effectiveness of any relevant complementary user entity controls.

46.61 Where there is commonality in the system controls across the user entities at a service organisation, then assurance may be gained from general controls testing. If controls are not entity

specific, testing effectiveness of controls will provide assurance whether or not the user entity is tested specifically. This is because it is the effectiveness of a control operation that is being tested, not its application to individual transactions. This is most likely to occur when a common system is in operation across the full audit portfolio. In this scenario, the engagement team to obtain assurance that their own audited entity's subject matter is included within the scope of the controls applied by the service organisation to which such commonality applies.

46.62 If there are controls specific to individual entities that are applied only in relation to that entity, these will need to be tested specifically, subject to risk and materiality, using the principles set out in Chapter 35: Controls testing. This is most likely to occur when there are different systems, or sub-systems, in operation for each audited entity. For example, if there is an audited entity-specific interface, manual or electronic, between the main system and the user entity, this will need to be considered separately. Alternatively, there may be a different transaction processing stream for each audited entity, reflecting the user-entity requirements. This needs to be identified and assessed at planning.

Requesting a common function or other auditor perform work – substantive work

46.63 If the engagement team plans to use substantive work performed by a common function auditor (or other auditor), they should:

- agree the nature, timing and extent of their work to reflect the assessed risks of material misstatement and performance materiality for the entity which is subject to audit;
- review the findings of their work to determine whether they constitute sufficient appropriate audit evidence for the purposes of the audit; and
- review the working papers of the common function auditor (as appropriate).

46.64 Substantive testing must be specific to the user entity, and the report will be in the form of factual findings for the user entity auditor to evaluate in the context of the user entity audit. Sampling methodology, including sample sizes, should be discussed and agreed before work commences, if a sampling approach is to be undertaken, and the report from the common function auditor will identify what was tested and the results for each item.

46.65 The engagement team should consider the impact of wider findings from the common functions auditor. For example, in the case of a non-current asset existence test at a site shared by several audited bodies, errors for other entities could affect the completeness risk assessment at the user entity. Appropriate and timely communications are therefore required between the Engagement Director and the common function auditor.

Concluding and reporting

46.66 Paragraphs 20 to 22 of ISA (UK) 402 (Updated May 2022) and the related application guidance include requirements on reporting by the user auditor.

46.67 The Engagement Director for the user entity audit is responsible for collecting sufficient, appropriate audit evidence to support the C&AG's opinion.

46.68 The output from the service auditor or common function auditor should be evaluated in light of its scope and the assurances required. A formal consideration of whether the results of the work provide the planned assurance must be recorded on the Apex audit file. Errors, omissions or control failings identified by the service auditor must be evaluated in light of the impact on the audit of the

user entity, and this consideration and the proposal for auditor action must be documented in the Apex audit file.

46.69 If the output from the service auditor is not in the expected/agreed form, or does not provide the expected assurances, the engagement team should seek further explanation from the user entity or, if relevant, the service auditor. If this does not generate the necessary audit evidence, the engagement team should seek alternative sources of evidence. If there are no procedures that the user auditor can undertake to gain sufficient, appropriate assurance, then a limitation of scope may exist that requires a modification to the audit opinion. Paragraph 20 of ISA (UK) 402 (Updated May 2022) requires the engagement team, as user auditor, to modify the opinion in the user auditor's report in accordance with ISA (UK) 705 (Revised June 2016) if the user auditor is unable to obtain sufficient appropriate audit evidence regarding the services provided by the service organisation relevant to the audit of the user entity's financial statements.

46.70 The engagement team should not refer to the work of a service auditor in an unmodified audit report for UK bodies. However:

- If a reference to the work of a service auditor is required in an international report by law or regulation, then in accordance with paragraph 21 of ISA (UK) 402 (Updated May 2022), the report should indicate that the reference does not diminish the C&AG's responsibility for the audit opinion.
- If reference to the work of a service auditor is relevant to an understanding of a modification to the user auditor's opinion, then in accordance with paragraph 22 of ISA (UK) 402 (Updated May 2022) the report should indicate that such reference does not diminish the C&AG's responsibility for that opinion.

46.71 The engagement team should raise misstatements, deficiencies or other exceptions identified by the service auditor with the user entity in line with the requirements of ISA (UK) 260 (Revised November 2019) (Updated May 2022) and ISA (UK) 265 (Updated May 2022).

Undertaking assurance engagements on service organisations

46.72 Teams auditing shared service centres or common functions should agree an appropriate approach with NAO teams taking assurance from their work. Teams may apply one or more of the relevant standards listed in the section of this Chapter entitled 'Planning the audit approach'.

46.73 Common function work should be undertaken in accordance with the principles of this Manual, taking account of the need to agree terms of engagement with the user entity Engagement Director as described within this Chapter.

46.74 When undertaking other assurance engagements, including the audit of a shared service centre, the principles of this Chapter should be considered. In particular, the following factors need to be addressed:

- The engagement team should understand and evaluate the terms of engagement, following the procedures set out in Section 5: New engagements and standing information. In particular, the Engagement Director should identify the stakeholders and consider the business risks in light of whom may be owed a duty of care
- The terms of the engagement may specify the form of reporting and/or the review framework to apply. If so, the Engagement Director considers whether the assurance requested is deliverable. Consideration should be given to the cost of providing the assurance requested. If the service entity is not prepared to pay that cost, negotiation on the level of assurance may be required for discretionary engagements. This is particularly relevant for grant certification, such as where grant-giving bodies prescribe a form of report that seeks a high level of assurance – further guidance on

grant certification can be found in the ICAEW Technical Release AAF 01/10: 'Framework document for accountants' reports on grant claims'

- A letter of agreement must be in place before the start of any such work. If the service entity, or other relevant body, seeks subsequently to change the terms of engagement, the Engagement Director must reconsider whether the revised scope can be met. If these changes seek a lower level of assurance than originally planned, the engagement team must be satisfied that there is a reasonable justification for the change. For example, it is not appropriate to change the terms from a Type 2 report to a Type 1 report simply to avoid a qualification – in such cases, revisit the business risk management procedures and consider the impact on the report
- Materiality and performance materiality should be set in accordance with this manual, taking account of the context in which the assignment is being undertaken. In an engagement to report on controls at a service organisation, the concept of materiality relates to the information being reported on, not the financial statements of user entity. Qualitative factors will therefore be reflected in materiality considerations, although there should also be consideration of tolerable rates of deviation. Further guidance on the evaluation of deviations can be obtained from the Analytical Methodology Team via the Financial Audit Support Tool (FAST).
- Gathering evidence for the audit report should be undertaken in accordance with this manual. This includes using the work of others such as internal audit or other experts, where appropriate. Written representations from the service entity management may also be necessary to gain sufficient, appropriate evidence
- Reporting should be in line with the assurance engagement framework adopted. The engagement team should familiarise themselves with the relevant framework and requirements. In particular, where opinion or professional judgement is given, this must be supported by sufficient, appropriate audit evidence. For prescribed procedures, the testing and results should be set out in a factual report, without specific opinion.

46.75 ***Consultation required*** Before embarking on an assignment that falls outside the ISAs, the engagement team should familiarise themselves with the relevant standards, requirements and Ethical Standard. In these circumstances, the engagement team must consult FAPQ.

46.76 Documentation on file should include at least:

- details our understanding of the entity's use of service organisations;
- our proposed approach to any testing required;
- how risks are addressed by the approach adopted;
- our consideration of the professional competence and independence of any service auditors, common function auditors, or other auditors the engagement team relies on;
- their reports;
- an analysis of the results, including the impact of errors/anomalies;
- our evaluation of that work; and
- documentation of any additional procedures required.

Chapter 47: Interim audit procedures, including hard close audits

Relevant standards and guidance

47.1 ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks* deals with the following matters relevant to interim audit procedures:

- paragraph 12 and the related application guidance deal with the auditor's use of audit evidence about the operating effectiveness of controls during an interim period;
- paragraph 22 and the related application guidance set out how the auditor covers the remaining period if substantive procedures are performed at an interim date;
- paragraph 23 and the related application guidance set out circumstances where the auditor may need to modify their risk assessment and the planned nature, timing and extent of substantive procedures covering the remaining period based on misstatements detected at an interim date;
- paragraphs A11 to A14 discuss the timing of responses to the assessed risks at the assertion level;

Background

47.2 For the purpose of this Chapter, references to the (accounting) year or year-end should be taken to refer to the period under report and the end of the period, respectively, where the period is longer or shorter than twelve months.

47.3 The following definitions are used in this Chapter:

- A "hard close" is a month-end close performed by the audited entity with the same controls and processes in place, and with the same rigor, as their year-end close.
- A "hard close audit" involves auditing balances and transactions at a date prior to the year-end (usually at the end of month nine, ten or eleven) as if that earlier date were the year-end date.
- "Interim audit procedures" are procedures performed to obtain assurance over transactions recognised during a portion of the accounting year and/or balances as at the date of a hard close.
- The "interim period" is the period covered by interim audit procedures.
- The "stub period" begins at the end of interim period and ends at the year-end date.
- "Roll-forward procedures" are the procedures used to obtain assurance over transactions in the stub period and/or year-end balances on the basis of the work done at an interim date.

47.4 Even at entities with strong controls, financial close process controls are usually applied more rigorously at the year-end than on a monthly basis. A "hard close" is where an entity performs a month-end close to year-end standards by, for example:

- planning the finance team's schedule to be able to perform a rigorous close;
- circularising department heads to confirm accrued amounts (where this is not done on a monthly basis);
- resolving any issues identified before closing the books on the period, rather than noting issues to resolve over the course of the month; and/or
- undertaking more thorough reviews than the entity's normal monthly reviews.

47.5 If an audited entity is willing to perform a hard close, the engagement team can perform a hard close audit. This enables the engagement team to audit balances and transactions at a date

prior to the year-end date (usually at the end of month nine, ten or eleven) as if that earlier date were the year-end date.

47.6 An audited entity will not necessarily update all balances at an interim date. For example, it is usually inefficient to prepare fair value calculations such as actuarial valuations more than once a year. Provided that this only applies to a few balances, the engagement team can test those balances at year-end and still perform a hard close audit on other balances.

47.7 Roll-forward procedures may consist of substantive analytical procedures or tests of detail over a relatively short stub period. A hard close audit can therefore be an effective way of reducing the extent of year-end audit procedures, which can make it easier to schedule staff and to deliver the audit pre-recess.

47.8 Procedures that should be considered for performing at an interim date include those procedures it would be effective and efficient to perform:

- at an interim date and then roll-forward to the year-end;
- unannounced or at unpredictable times, such as performing procedures at selected locations on an unannounced basis (which may be particularly appropriate when responding to risks of fraud); and
- where performing interim work would be expected to identify significant matters at an early stage of the audit, enabling them to be resolved on a timely basis.

47.9 Other factors which may influence the approach include:

- the predictability of transactions and balances over the course of the year – this will influence what approach would be appropriate for roll-forward procedures;
- the control environment (including IT controls) – a weaker control environment will usually mean that interim testing provides less reliable evidence;
- when relevant information is available – for example, electronic files may subsequently be overwritten, or procedures to be observed may occur only at certain times; and
- the characteristics of the entity's balances and transactions and the nature of the risks which have been identified – for example, if there is a risk of inflated expenditure to preserve budgets by early receipting of goods and services received, the engagement team may wish to examine evidence available at the year-end date.

47.10 Most classes of transaction, account balances and disclosures could, in principle, be tested at an interim date. The engagement team may be able to do so using a range of audit procedures, including substantive analytical procedures.

47.11 However, it is usually only where the audited entity carries out a "hard close" that it is effective and efficient to test account balances, accounting estimates and the completeness of transactions at an interim date.

47.12 Even when the audited entity does not perform a "hard close", interim audit procedures may still be performed, such as:

- testing the operating effectiveness of controls during the interim period;
- testing the occurrence, accuracy, or regularity of transactions recognised in the interim period;
- testing non-current assets (or other audit areas where the items making up the balance would not be expected to change significantly to year-end)

- work on significant risks, particularly around individually significant transactions or balances where the audited entity is able to determine the likely accounting and disclosures prior to the year-end; and/or
- testing of inputs used in calculating accounting estimates at the year-end.

Planning whether to perform a hard close audit or other interim procedures

47.13 In determining an audit approach, engagement teams should consider what work they will be able to perform at an interim date. Performing audit work at an interim date can reduce the level of testing to be performed during final audit fieldwork, which in turn can help to ensure timely completion of the audit and relieve staffing pressures.

47.14 The procedures performed at an interim stage range from very limited testing to a full "hard close" audit. The level of testing to be performed will depend on the willingness of the audited entity to undertake a "hard close" and the engagement team's judgement as to whether such an audit approach would lead to a high-quality audit – for example, whether the engagement team anticipates that the audited entity is in a position provide a set of "hard close" accounts of sufficient quality and adequate evidence to enable testing of these.

47.15 When a formal "hard close" audit is performed, the majority of audit work will be able to be performed on the "hard close" accounts prepared by the audited entity. At the year-end date, the engagement team applies roll forward procedures to obtain assurance on the transactions occurring in the stub period.

47.16 Even if it is not possible to perform a full hard close, it may still be effective and efficient to perform more limited testing at an interim date.

47.17 As part of establishing the overall audit strategy, the Engagement Director and Engagement Manager should consider whether it would be effective and efficient to perform controls and/or substantive procedures at an interim date.

47.18 The planned procedures should reflect the risks of material misstatement or and risks of material irregular transactions associated with the classes of transactions, account balances and disclosures being tested. For example, if there is a significant risk over the completeness of liabilities it may not be appropriate to test these liabilities at an interim date (as testing will need to be repeated after the year-end).

47.19 The engagement team should consider whether it is possible to perform other interim procedures even in the absence of a formal "hard close".

47.20 Having performed interim audit procedures over balances at a hard close, the engagement team should consider and document, based on the nature of the balances and risks of material misstatement, whether it may be appropriate to not to perform any further testing over those balances at year-end.

47.21 The engagement team should consider whether it is possible to test the regularity of transactions at an interim date.

47.22 Engagement teams should be alert to the risk that the production of a complete set of financial statements at the hard close date may increase the risk of fraud through management override of controls in order to achieve the desired financial position at the year-end and may reduce the engagement team's ability to detect this type of manipulation.

47.23 The engagement team should discuss their preferred approach to the timing of testing with management and, where relevant, agree with management the arrangements for an interim audit visit. The audited entity may need to conduct additional work to support a "hard close" approach, so the engagement team should discuss the planned approach early enough for client staff to plan accordingly. Performing the "hard close" audit work as close as possible to the year-end date will reduce the scope and scale of procedures required to be performed in respect of the stub period.

Designing interim audit procedures

47.24 Interim audit procedures may consist of a wholly substantive or a controls and substantive approach. Engagement teams should refer to Section 9: Testing techniques when designing audit procedures in response to the assessed risks.

Testing to obtain assurance over the stub period

47.25 The Engagement Director agrees the approach obtaining assurance over balances and transactions for the stub-period, usually when approving the audit plan.

47.26 The assessment of the extent of the procedures required to obtain additional evidence should take account of:

- the Likelihood and Financial Statement Impact (magnitude) assessments of the relevant risks of material misstatement and risks of material irregular transactions;
- the degree of assurance obtained to date; and
- the length of the remaining period.

47.27 Factors affecting the approach adopted include:

- whether the year-end balances of the particular classes of transactions or account balances are reasonably predictable with respect to amount, relative significance, and composition;
- whether the entity's procedures for analysing and adjusting such classes of transactions or account balances at interim dates and for establishing proper accounting cut-offs are appropriate; and
- whether it is possible to obtain information concerning the balances at the period end and the transactions in the remaining period that is sufficient to permit investigation of significant unusual transactions or entries (including those at or near the year-end), other causes of significant fluctuations or expected fluctuations that did not occur, and changes in the composition of the classes of transactions or account balances.

Testing to obtain assurance over the stub period – controls testing

47.28 In most cases, the engagement team extends the controls testing to cover the entire period or confirms that the control remained in place and review the entity's monitoring of that control over the remaining period.

47.29 Where a hard close audit is undertaken and there have not been significant changes to controls after the interim period, it is expected that confirming that the control remained in place and reviewing the entity's monitoring of that control over the stub period should be sufficient.

47.30 Depending upon the circumstances, the engagement team may obtain evidence about whether or not controls have changed significantly through one or more of:

- inquiry of management;
- walking through a transaction to check that the controls are still implemented in accordance with the engagement team's understanding;
- examining process manuals or other documentation; and/or
- other procedures appropriate to the control being tested.

47.31 If the engagement team plan to test controls for the stub period, the controls sample will usually be split proportionally between the interim period and the stub period.

47.32 If there have been significant changes in the controls after the interim period, the engagement team should either:

- evaluate the design and implementation of the new control and test its operating effectiveness; or
- not take controls assurance for the remainder of the year and increase the extent of the substantive procedures on transactions in the stub period.

Testing to obtain assurance over the stub period – substantive procedures

47.33 The engagement team should compare and reconcile information concerning the balance at the year-end with the comparable information at the interim date to identify and investigate unusual items.

47.34 The engagement team should consider the existence of unusually large transactions or significant fluctuations in the volume of transactions during the stub period.

47.35 It is expected that it will be more effective and efficient to obtain assurance over the stub period through substantive analytical procedures (in combination with controls assurance), particularly where a hard close approach has been taken, than through tests of detail. Where it is necessary to perform tests of detail, if there is a large volume of reconciling items which must be tested, this may be inefficient. It is usually more efficient to use substantive analytical procedures as roll forward procedures for account balances. Where this is not practical, it may not be appropriate to test balances at an interim date.

47.36 Tests of detail to extend assurance over classes of transactions will usually consist of performing the same tests for the stub period as were performed for the interim period. Further guidance on sample testing that covers both an interim period and a stub period may be found in Chapter 34: Tests of detail.

47.37 Tests of detail to extend assurance over account balances will usually consist of testing movements between the interim and year-end dates by testing the occurrence, accuracy and completeness of transactions impacting the year-end balance (such as asset additions and disposals).

47.38 If accounting estimates have been tested at an interim date, the engagement team should consider whether there have been any changes in the entity, its environment, or the affected balances which may impact upon the accounting estimates.

47.39 When testing journal entries to address the presumed significant risk of fraud through management override of controls, the engagement team should, at a minimum (regardless of whether using a hard close approach or performing other interim testing), select and test journal entries and other adjustments made at the end of a reporting period and post-closing entries, in accordance with paragraph 33(a)(ii) of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements*.

Continuous risk assessment

47.40 As part of the continuous risk assessment process, following the processes set out in Chapter 19: Continuous risk assessment, the engagement team should revisit the risks of material misstatement as set out in the Risk Assessment in Apex and the risks of material irregular transactions as set out in the Regularity Testing Plan in light of the findings of interim audit procedures. Consideration should be given as to whether the risks remain relevant and complete. The engagement team should also consider whether the planned audit approach remains appropriate in light of the findings of the interim audit.

47.41 Following the completion of interim audit procedures, for any audits where Engagement Director or Engagement Manager roles have been delegated, the Portfolio Director should meet with the engagement team to discuss the findings of audit work to date. Based upon this, the Portfolio Director should revisit their assessment of engagement risk in making the delegation to ensure that it remains appropriate. Further guidance on the delegation of audit responsibilities may be found in Chapter 12: Roles, delegations and licences.

Evaluating the results of procedures performed

47.42 The engagement team should evaluate the results of interim and roll-forward testing in the same way as other testing, following the processes set out in Chapter 52: Evaluating the results of procedures, including identified misstatements and irregular transactions.

47.43 Audited entities will ordinarily correct the specific misstatements identified during interim audits. Where misstatements are identified as part of sample testing undertaken during the interim audit, the engagement team will need to consider the impact of those misstatements across the population as a whole. This may either be done by extrapolating the findings of interim audit procedures across the stub period population or through undertaking further work to establish the full extent of misstatement. The engagement team may also consider amending the sampling approach to the stub period to reflect the level of error identified through sample testing undertaken at interim audit.

Section 12: Use of experts

Chapter 48: Assessing the need for an auditor's expert

Relevant standards and guidance

48.1 Paragraphs A19 and A101 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deal with situations where the engagement team includes a member with expertise in a specialised area of accounting or auditing (an auditor's expert).

48.2 Paragraphs 8 and A45 to A59 of ISA (UK) 500 (Updated May 2022) *Audit evidence* deal with the auditor's use of the work of an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements (a management's expert).

48.3 ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors* deals with the external auditor's responsibilities if using the work of internal auditors. This includes:

- using the work of the internal audit function in obtaining audit evidence; and
- using internal auditors to provide direct assistance under the direction, supervision and review of the external auditor.

48.4 Paragraphs 1-197 to 1-199 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 610 (Revised June 2013) (Updated May 2022) in the public sector.

48.5 ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert* deals with the auditor's responsibilities relating to the work of an individual or organisation in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

48.6 Paragraphs 1-201 to 1-203 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 620 (Revised November 2019) (Updated May 2022) in the public sector.

When and where might an expert be used?

48.7 ***Table 48A*** provides examples of when engagement teams should consider using the work of others.

Table 48A: Circumstances when engagement teams should consider using the work of others

		Work required to understand the entity in planning the audit	Work required by engagement team to place reliance on the work of others
Use of an NAO expert	Independent legal advice on regularity of a transaction		Evaluate whether the NAO expert has the necessary competence, capabilities and

(for procuring expertise through the Financial Audit Contract, refer to Section 10: Contracted-out work)	(organise through FAPQ) Independent legal advice on treatment of a liability (organise through FAPQ) Actuarial support in auditing a pension liability Valuations support in auditing asset values Support from MESH in reviewing and auditing models		objectivity for the purposes of the audit. Obtain an understanding of the expert's field of expertise sufficient to scope and evaluate their work. Make arrangements for the expert to perform their role. Evaluate the adequacy of the expert's work for the purposes of the audit, including their assumptions and methods, the source data they have used, their findings, and the consistency of their findings with other audit evidence.
Entity has internal audit function	Entity has its own internal audit function NDPB uses the Department's internal audit function Entity contracts in internal audit services from a firm	Understand Internal Audit's (IA's) activities under ISA (UK) 610 (Revised June 2013) (Updated May 2022)/ ISA (UK) 315 (Revised July 2020) and how they may affect the audit.	
Entity has internal audit function – work not directly relevant to the audit	Work in the year is mainly on operational issues Scope of work is too narrow to support our audit e.g. focussed on small number of individual locations	High level review and discussion of internal audit findings to inform the risk assessment.	
Entity has internal audit function - performed work which the engagement team would want to take assurance from	IA have completed testing on the implementation of a new IT system IA have tested specific controls IA have verified inputs into a model for calculating a provision	Evaluate the competence and independence of IA staff.	Evaluate the adequacy of the work which it is planned to take assurance from. Perform procedures to earn the right to take assurance from IA's work: for example, by re-performance.

	IA have completed substantive testing to give management assurance		
Entity uses a service organisation (refer to Chapter 46: Service organisations and shared service centres)	Outsourced payroll, finance and IT functions Outsourced management of a compensation scheme	Obtain an understanding of the services provided by the service organisation, including how they impact upon the entity's system of internal control. Determine the impact that the use of a service organisation has upon our audit approach. Where appropriate, obtain a Type 1 or Type 2 report on controls at the service organisation and perform procedures to be able to use this as audit evidence.	If the engagement team consider it appropriate to use a Type 1 report as evidence of the design and implementation of service organisation controls, or a Type 2 report as evidence of their operating effectiveness: • evaluate the professional competence and independence of the service auditor, and the adequacy of the standards under which their report has been issued; • evaluate their findings and whether their report provides sufficient appropriate evidence; and • perform procedures, where necessary, upon complementary user entity controls

48.8 Paragraph 7 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) requires that the auditor appoints an internal or external auditor's expert if expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence. This may be at any stage of the audit, as explained by paragraph A4 of ISA (UK) 620 (Revised November 2019) (Updated May 2022), including the following stages:

- gathering entity initial information;
- risk assessment and response planning (including for regularity);
- continuous risk assessment;
- evidence assessment and evaluation; and/or
- the stand-back assessment.

48.9 Paragraph A1 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) provides examples of the kinds of areas where expertise other than accounting or auditing might be required in preparation of the financial statements. Those found in the NAO's work include:

- valuation of complex financial instruments (for example, level 2 or 3 fair valuations - i.e. those not based on quoted prices from an active market);
- estimation of expected credit losses (other than basic short-term receivables), especially where economic modelling is required;
- valuation/impairment of non-current assets (property, plant and equipment; heritage assets; intangible assets; and infrastructure assets);
- actuarial calculations (such as those on pensions, provisions or insurance contracts);
- valuation of environmental and decommissioning liabilities;
- interpretation of contracts, laws and regulations (for example, in relation to legal provisions or contingent liabilities); and

- analysis of complex or unusual tax compliance issues.

48.10 ISA (UK) 620 (Revised November 2019) (Updated May 2022) makes an important distinction between a specialised area of accounting or auditing and expertise in another field. For example, as discussed in paragraph A2, an individual with expertise in methods of accounting for financial instruments would not be an expert for the purpose of ISA (UK) 620 (Revised November 2019) (Updated May 2022). However, an individual with expertise in complex modelling for the purpose of valuing financial instruments would be.

48.11 The NAO's audit methodology includes the following policies in respect of considering the use of experts in a financial statement audit:

- The use of expertise outside accounting or auditing by management in preparation of the financial statements should always lead the engagement team to document an assessment of whether an auditor's expert is required.
- The assessment should be specific to the types of expertise being used and cover each of these. For example, a complex provisions valuation might require expertise in both actuarial calculations and interpretation of contracts or legislation.

When might an auditor's expert be required (not merely an option)?

48.12 ISA (UK) 620 (Revised November 2019) (Updated May 2022) does not make a presumption that an auditor's expert is always required. For instance, the auditor may obtain a sufficient understanding of the relevant field of expertise via other means, such as the examples given in paragraph A7.

48.13 However, paragraph A8 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) does provide examples of considerations which might lead the engagement team to decide to use the work of an expert; whether by necessity or by choice. This is ultimately a risk-based assessment, but, practically, any or a combination of the following factors would indicate an auditor's expert is likely to be required:

- management has used a management's expert in preparing the financial statements (paragraph A9 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) provides further specific guidance on this point);
- there is a relevant significant risk of material misstatement;
- specialised skills or knowledge are needed to understand the level of risk or to carry out the audit procedures responding to these risks; and/or
- alternative sources of audit evidence (from that provided by an expert) are not available.

48.14 Other considerations when deciding whether to use an auditor's expert (appointed by the NAO) may include:

- the nature and significance of the matter, including its complexity;
- the Likelihood and Financial Statement Impact (magnitude) of the related risks of material misstatement (noting that a significant risk would likely indicate an expert should be used, as per the above paragraph);
- the expected nature of procedures to respond to identified risks, including the engagement team's knowledge of and experience with the work of experts in relation to such matters; and
- the available expertise within the NAO team.

48.15 ***Consultation required*** The NAO's audit methodology includes the following policies in respect of areas where the use of an expert in a financial statement audit may be required:

- If the engagement team decides that they have a sufficient understanding of the relevant field of expertise such that an expert is not required, they should document that fact, referring to the factors in paragraph A7 of ISA (UK) 620 (Revised November 2019) (Updated May 2022). This should refer to the specific individuals involved in carrying out and reviewing the audit work.
- If any of the factors in paragraph A8 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) are present, it is essential that the engagement team carefully considers and documents their rationale if they have decided not to use an expert. In these circumstances, the engagement team should consult with FAPQ or the relevant Centre of Expertise.
- In particular, where management makes accounting estimates that involve multiple economic scenarios (such as may be required for expected credit losses), there is a presumption that economic expertise will be engaged. The engagement team should consult FAPQ where they wish to rebut this presumption (i.e. they conclude that economic expertise is not required).
- If the factors listed in the paragraph above are present, but the engagement team considers there are barriers to the use of an auditor's expert, they should consult FAPQ.

Planning whether to use an auditor's expert

48.16 The engagement team should include appropriate team members, either from within the NAO or from a contractor, when an engagement requires expertise in a specialised area of auditing or accounting.

48.17 Where skills other than auditing or accounting are required, it may be necessary to plan to use the work of an expert retained by the NAO ("an NAO expert").

48.18 The Engagement Director has sole responsibility for the audit opinion expressed, and that responsibility is not reduced by the use of the work of an expert.

48.19 The Engagement Director must be satisfied that the engagement team, and any experts who are not part of the engagement team, collectively have the appropriate competence and capabilities to perform the audit engagement.

48.20 The inclusion in the engagement team of members of staff or contractors with particular IT audit skills will not usually represent the use of an auditor's expert. In some circumstances, the use of contractor staff with a particular expertise in the underlying workings of a particular system (rather than audit skills) may represent the use of an auditor's expert.

48.21 The engagement team should monitor the need for using the work of an auditor's expert as the audit progresses.

48.22 The assessment should be specific to the types of expertise being used and cover each of these. For example, a complex provisions valuation might require expertise in both actuarial calculations and interpretation of contracts or legislation.

48.23 If management has used a management's expert and their work may be used as audit evidence, when considering whether to use an auditor's expert, the engagement should consider and document:

- the nature, scope and objectives of the management's expert's work;
- whether the management's expert is employed by the entity, or is a party engaged by it to provide relevant services;
- the extent to which management can exercise control or influence over the work of the management's expert

- the management's expert's competence and capabilities;
- whether the management's expert is subject to technical performance standards or other professional or industry requirements; and
- any controls within the entity over the management's expert's work.

48.24 The following circumstances may raise difficult questions of both application of the standards and client handling. The engagement team may consider consulting FAPQ if any of these apply:

- the audited body (or another organisation within government) is the primary or only recognised source of expertise on the relevant subject matter;
- there are no organisations with the relevant expertise that are also independent of the audited body (as sometimes occurs with major infrastructure projects);
- management or those charged with governance challenge a change in the engagement team's assessment of whether external expertise is required (including challenges relating to the impact on audit fees); and/or
- there is a perceived lack of interest from users of the accounts in the balances in question?

Planning whether to use the work of internal audit

48.25 Engagement teams should explore using the work of internal audit.

48.26 If the engagement team intends to use the work of internal audit, they should:

- assess the internal audit function at the planning phase; and
- perform procedures to earn the right to use specific pieces of work which are being used in the audit.

48.27 Paragraph 5-1 of ISA (UK) 610 (Revised June 2013) (Updated May 2022) prohibits the use of internal auditors to provide direct assistance (this provision is specific to the UK version of the standard). Accordingly, the use of internal auditors to provide direct assistance is not permitted for NAO audit engagements, except those international audits carried out under the international (non-UK-adapted) versions of the ISAs.

48.28 The engagement team should consider internal audit's planned Audit Response Group and consider whether using their planned work could benefit the effectiveness and efficiency of our audit.

48.29 If there are areas where it would be effective and efficient to use the work of internal audit, the engagement team should determine whether the work of the internal auditors is likely to be adequate for purposes of the audit.

48.30 In evaluating the likely adequacy of internal audit's work for the purposes of the audit, the engagement team should evaluate:

- the objectivity of the internal audit function;
- the technical competence of the internal auditors;
- whether the work of the internal auditors is likely to be carried out with due professional care; and
- whether there is likely to be effective communication between the internal auditors and the external auditor.

48.31 If it is considered appropriate to plan to use the results of internal audit's existing Audit Response Group, the engagement team should plan how this will affect the nature, timing or extent of their own audit procedures. In doing so, the engagement team should consider and document:

- the nature and scope of specific work performed, or to be performed, by the internal auditors;

- the assessed Assertion-level risks of material misstatement for the relevant classes of transactions, account balances, and disclosures; and
- the degree of subjectivity involved in the evaluation of the audit evidence gathered by the internal auditors in support of the relevant assertions.

48.32 Where a class of transactions, account balance or disclosure (COTABD) or a risk of material misstatement (RoMM) involves a significant level of risk, estimation or judgement, the engagement team should not place undue reliance upon the work of internal audit, but should seek to directly test these COTABDs or RoMMs themselves.

48.33 If the engagement team does not plan to take assurance from internal audit's work, they should consider the reasons for this. If the reasons involve, for instance, internal audit's objectivity or competence, rather than the scope or timing of their work, the engagement team should discuss them with the Head of Internal Audit and those charged with governance. The engagement team should also consider the implications of any such concerns regarding internal audit's objectivity or competence on their risk assessment, including their understanding of the entity's process for monitoring the system of internal control. This consideration should include updating the Understanding The Entity's System of Internal Control template as appropriate (see ***Table 15D*** in Chapter 15: Gathering entity initial information). Any deficiencies in internal audit's objectivity or competence may need to be reported to those charged with governance under ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* (see Chapter 57: Reporting to those charged with governance).

48.34 If the engagement team believe that the internal audit function does not meet the Public Sector Internal Audit Standards (for example, because it is not adequately resourced or is not focusing on the audited entity's risk areas) then the engagement team should recommend that steps are taken to address these issues.

48.35 There is no requirement to audit the statements made in the Governance Statement. NAO policy is to review the annual report of the Head of Internal Audit as part of the review of the Governance Statement.

48.36 The presence or absence of evidence of significant control failings will help the engagement team to form a view on the reliability of the Accounting Officer's Statement. The engagement team should consider the annual report in conjunction with the individual reports and the audit needs assessment produced by internal audit.

48.37 In accordance with paragraph 19 of ISA (UK) 610 (Revised June 2013) (Updated May 2022), the engagement team should evaluate whether, in aggregate, using the work of internal audit to the extent planned would mean that they remain sufficiently involved in the audit, given the C&AG's sole responsibility for the audit opinion.

48.38 The Treasury expects central government internal auditors to comply with the Public Sector Internal Audit Standards (PSIAS). It is the Accounting Officer's responsibility to ensure that internal audit arrangements are put in place that comply with the PSIAS. These standards are useful reference material when assessing an internal audit function and when discussing that assessment with our audited entities, but just because an IA function does not subscribe to these, does not automatically preclude using their work. ISA (UK) 610 (Revised June 2013) (Updated May 2022) should be followed.

48.39 The PSIAS state that internal auditors should share information and cooperate with external auditors. However, the ISAs (UK) prohibit direct assistance from internal audit.

48.40 If the engagement team conclude it is not appropriate to use internal audits' work, reviewing and discussing their reports will usually be helpful in informing our continual risk assessment and also to confirm that their findings are not inconsistent with our own.

48.41 Irrespective of the degree of autonomy and objectivity of the internal audit function, such a function is not independent of the entity. As external auditors, the NAO has sole responsibility for the C&AG's audit opinion, and that responsibility is not reduced by any use of the work of the internal auditors.

48.42 It is important that the engagement team engages with internal audit about their annual plan at the right time. Most internal audit functions will prepare a plan of their work shortly before the start of a new financial year. It is at that time that the external auditor can have most influence in helping to determine:

- what assurance the Accounting Officer should be looking for and which audits should be carried out to obtain that assurance; and
- the scope to reduce the amount of external audit work undertaken if internal audit can provide positive assurances to support the opinion on the annual accounts.

48.43 The engagement team's liaison with internal audit might also include allowing them access to our audit plans and discussions about how the engagement team can work closely together to maximise audit effectiveness and avoid duplication of effort.

48.44 The engagement team's focus should be on considering how internal audit could give them assurance over financial statement assertions or risks. If their work has been focused on operational matters that do not directly impact the financial statements, then their work will not provide assurance for our audit

48.45 Internal audit investigations that would assist the engagement team in forming an opinion on the financial statements may include work on areas such as:

- manual and IT controls over the financial accounting system;
- controls testing over particular RoMMs;
- the IT control environment, where relevant to specific controls supporting the production of the financial statements;
- fraud; and/or
- governance and risk management (required annually under HM Treasury's Public Sector Internal Audit Standards).

48.46 Internal audit may also carry out work to provide management with assurance over significant risks. Internal audit's work is performed for different reasons to our audit work. Therefore, it is unlikely that the nature, timing and extent of internal audit's work will be precisely the same as the engagement team would have planned themselves.

48.47 Accordingly, the Engagement Director and Engagement Manager must use professional judgement in assessing whether their work provides sufficient appropriate audit evidence, or whether additional testing should be performed.

48.48 It is unlikely to be appropriate to use work performed by employees of the entity in addressing significant risks that may relate to fraud by management. By contrast, work by the entity

to quantify the extent of irregularity due to fraud by benefit or grant claimants may well be appropriate use.

48.49 Factors to consider when considering whether it is appropriate to use the work of internal audit include:

- Objectivity:
  - the status of the internal audit function within the entity and the effect such status has on the ability of the internal auditors to be objective;
  - whether the internal audit function reports to those charged with governance or an officer with appropriate authority, and whether the internal auditors have direct access to those charged with governance;
  - whether the internal auditors are free of any conflicting responsibilities;
  - whether those charged with governance oversee employment decisions related to the internal audit function;
  - whether there are any constraints or restrictions placed on the internal audit function by management or those charged with governance; and
  - whether, and to what extent, management acts on the recommendations of the internal audit function, and how such action is evidenced.
- Technical competence:
  - whether the internal auditors are members of relevant professional bodies;
  - whether the internal auditors have adequate technical training and proficiency as internal auditors; and
  - whether there are established policies for hiring and training internal auditors.
- Due professional care:
  - whether activities of the internal audit function are properly planned, supervised, reviewed and documented; and
  - the existence and adequacy of audit manuals or other similar documents, work programs and internal audit documentation.

48.50 Our interaction with internal audit will be most effective when:

- the internal auditors are free to communicate openly with the external auditors;
- meetings are held at appropriate intervals throughout the period;
- the engagement team are advised of and has access to relevant internal audit reports and is informed of any significant matters that come to the attention of the internal auditors which may affect our audit; and
- internal auditors are informed of any significant matters identified that may affect the internal audit function.

48.51 It will often be most practical to examine items already examined by internal audit, but this will depend on the nature of their procedures and how they have documented their work. Where engagement teams plan to use their work, it may be appropriate to agree an appropriate format for their documentation.

The engagement team is asked to sign a "hold harmless" letter

48.52 In some cases, there has been difficulty in gaining reasonable access to the working papers of private sector internal auditors. On occasion, NAO auditors have been asked to sign "hold harmless" letters issued by firms. Such letters often seek to place unreasonable restrictions upon the C&AG's rights to take assurance from the work of internal audit or to make disclosures in reports to Parliament arising from that work. Where this is the case "hold harmless" letters should not be signed by NAO auditors.

48.53 Where the private sector firm refuses to provide access to working papers without a "hold harmless" letter being in place, engagement teams may sign such a letter so long as it contains the following wording which acknowledges the C&AG's statutory rights of access:

"We acknowledge that as external auditor, the Comptroller and Auditor General (C&AG) has a statutory right of access to the records of [audited entity]*. Consequently the non-proprietary working papers and files produced by* [Name of Firm] *to support the internal audit reports issued to* [audited entity]*, to which* [audited entity] *has a right of access and permits us to disclose, will be freely available to the NAO. In addition, where* [audited entity] *has no right of access to our files and non-proprietary working papers, we will, following your acceptance of the terms of this letter and our receipt of permission from* [audited entity]*, grant you access to files and non-proprietary working papers retained by us (other than those kept for* [Name of Firm]*'s internal practice management purposes), including copies thereof."*

48.54 The "hold harmless" letter may also seek to restrict use of any information provided to the purpose of the external audit. The NAO are not able to comply with such requirements due to the C&AG's Parliamentary reporting requirements and potential FOI requests. Therefore, such a letter would only be signed which contained the following wording:

"Save as may be required by law or in exercise by the C&AG of his statutory functions or by any other competent regulatory authority of its functions (in which case you shall, unless prohibited by law, inform us in advance of disclosure), you shall keep the working papers confidential and shall not provide copies of the working papers, or give any information obtained from them or from us, to anyone outside those within your organisation who are involved in the discharge of the C&AG's functions.

You shall not use the working papers, or any information obtained from them or from any explanations provided by us, for any purpose other than the provision of an external audit service to the [audited entity] *and of the preparation and provision of reports to Parliament or other exercise of the NAO's statutory functions. For any other purpose, you will not use our working papers without our prior written agreement thereto."*

48.55 ***Consultation required*** Where engagement teams are considering signing a "hold harmless" letter that does not include this wording, they must consult FAPQ.

Formal protocols for working with internal audit

48.56 ***Consultation required*** Where existing arrangements work well, no further discussion is necessary. However, where private sector firms seek more formal agreements, the protocol set out in ***Figure 48B*** should act as a model. Engagement teams must consult with FAPQ before any such protocols are agreed.

48.57 The protocol set out in ***Figure 48B*** embodies guidelines for managing the NAO's relationship with private sector internal auditors. It is based on an agreement with one private sector provider. The agreed protocol preserves the C&AG's right to report to Parliament as he sees fit. It accepts that, provided the internal auditors include in their reports the level of information that the engagement team need to assess the scope, quality and findings from the internal audit programme, access to the working papers will not normally be required. Should circumstances dictate that access to the underlying working papers is required, terms and conditions will be agreed at the time. The table accompanying the protocol sets out our expectations in respect of the standard and scope of internal audit work.

Figure 48B: Protocol for use of internal audit contractor work at [audited entity]

- *NAO and* [Name of Firm] *are committed to making the overall audit process as efficient and effective as possible, through co-operation to reduce duplication and enhance both parties' understanding of risks facing the organisation.*
- *As external auditor, NAO has a statutory right of access to the records of the audited body. Consequently, both the annual report and individual reports on reviews produced by [Name of Firm] and issued to the* [Name of Client] *will be freely available to the NAO.*
- *In obtaining access to the documents in paragraph 2 above and in discussing the risk assessment and Internal Audit Plan with* [Name of Firm], *NAO accept and confirm their agreement to audit and draw its own conclusions, prior to reporting to Parliament.*
- *Provided* [Name of Firm] *include in their reports the level of information NAO need to assess the scope, quality and findings from the internal audit programme, NAO will not normally require access to the underlying working papers belonging to* [Name of Firm]. *Since access will generally not be required to the working papers of* [Name of Firm], [Name of Firm] *will not require any hold harmless letter to be signed. In the event that the NAO do require access to* [Name of Firm]*'s working papers, the terms and conditions of access will be agreed at that time, having regard to the C&AG's statutory rights under Section 8 of the Government Resources and Accounts Act 2000. NAO's requirements for internal audit reports produced by* [Name of Firm], *and identified actions to ensure compliance are set out in Table 1.*
- *In circumstances where the NAO clears with* [audited entity] *the content of a report for factual accuracy,* [audited entity] *will consult with* [Name of Firm] *beforehand, where appropriate, to seek to agree the wording to their mutual satisfaction.*
- *All reports will be tabled to* [audited entity]*'s Audit Committee and therefore be available for NAO review. Copies of system notes will also be given to the Head of Finance at* [audited entity] *with an appropriate disclaimer note.*

Table 1 [accompanying ***Figure 48B***]

Ref	NAO Requirement	Actions where [Name of Firm] demonstrate compliance
1	Explicit assurance to [audited entity] in each report that the contractor has: • deployed appropriate staff, who are suitably skilled, experienced and supervised; and • quality assured their work.	A statement confirming compliance with this standard will be included in each report.
2	Assurance that judgements and conclusions in particular are quality assured by a competent more senior professional with relevant experience.	Team structure for each review will be specified in the terms of reference.
3	That each report makes completely clear the scope of the work, including the risks addressed, procedures undertaken and staff interviewed.	The scope of our work, and any limitations placed on the scope, will be disclosed in each terms of reference and report. Reports will also disclose risks addressed, procedures performed and staff interviewed as part of the audit.
4	That contractor staff involved are aware of public sector and central government guidelines and practices. In particular, those practices applicable to the particular sector and area of business under consideration.	Staff attend regular training on industry and sector issues and receive technical updates from our knowledge mangers. This training will be referred to in the Annual Report. Key audit risks will be documented in the terms of reference for each review.

5	That the contractor recognises the use that others will seek to make of their work, including the external auditors, sponsoring department, and/or partners in joint schemes.	Other parties may seek to use reports for their own purpose. They do so at their own risk. [Name of Firm] does not owe them a legal duty of care. Reports will include the following paragraph: *"We have prepared this report solely for your use. We believe that it would not be appropriate for it, or extracts from it, to be made available to third parties. If such a third party were to obtain a copy, in whole or in part, without our prior consent, we would not accept any responsibility for any reliance that they might place upon it".*
6	That the contractor will share risk assessment judgements and insights with the external auditors.	[Name of Firm] undertake to share with external audit their risk assessment and the Internal Audit Plan under the terms set out in the Agreed Protocols.
7	That the contractor will do more than simply accept management's own risk assessment and risk register.	[Name of Firm] shall review [Name of audited entity]'s risk register and the processes used to compile the register. If appropriate, [Name of Firm] will supplement this work with interviews with key stakeholders to attest to the register's credibility and completeness.
8	That the contractor appreciates the audited entity's reputational risk vis a vis the quality of their internal audit contractor's work.	[Name of Firm]'s work is subject to stringent quality assurance standards.
9	[Audited entity] will consult with the contractor if they receive a request for copies of internal audit reports or extracts of information contained therein from NAO or other third parties.	[Name of Firm] will discuss such requests with [Audited entity].

48.58 ***Consultation required*** Engagement teams must also consult with FAPQ before agreeing to any restrictions on the C&AG's rights of access to documentation.

Internal audit involvement in regularity

48.59 Internal audit is often part of the entity's controls over regularity, as set out in ***Table 48C***.

Table 48C: Possible involvement by internal audit in audited entities' controls over regularity

Possible risk	Description	Mitigating control
Complexity of Regulations	The more complex the regulations the greater the risk of error. This may occur either through a misunderstanding or misinterpretation of the regulation or through an error in application.	Review of scheme control plans and operating manuals by internal audit
New legislation	New legislation may require the introduction of new administrative and control procedures. This may result in errors in either the design or operation of controls required to ensure regularity.	Formal control plans and the independent review of operating instructions and control plans may apply where schemes are introduced following new legislation.

Services and programmes delivered through third parties	Where programmes are administered by agents, departments lose a degree of direct control and may have to rely on agents to ensure compliance with authorities.	Inspection visits by internal audit to third parties to review systems and procedures, including those relevant to regularity.
Regularity of grant expenditure	It can often be difficult to gain sufficient appropriate audit evidence that grants have been used for the purposes intended by Parliament.	Internal audit, or other function within the body, directly test grant expenditure to ensure that is has been used as intended.

Chapter 49: Obtaining internal expertise

Relevant standards and guidance

49.1 Paragraphs A19 and A101 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deal with situations where the engagement team includes a member with expertise in a specialised area of accounting or auditing (an auditor's expert).

49.2 Paragraphs 8 and A45 to A59 of ISA (UK) 500 (Updated May 2022) *Audit evidence* deal with the auditor's use of the work of an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements (a management's expert).

49.3 ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert* deals with the auditor's responsibilities relating to the work of an individual or organisation in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

49.4 Paragraphs 1-201 to 1-203 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 620 (Revised November 2019) (Updated May 2022) in the public sector.

Centres of Expertise

49.5 The NAO has established Centres of Expertise, on which financial audit engagement teams may draw for expert support in their audits. The Centres of Expertise provide thematic knowledge, guidance and ad-hoc advice to audit teams in specific audit areas that are more difficult or complex.

49.6 Details of the services provided by each of the Centres of Expertise may be found on the FA Service Line pages on Sharepoint:

- Charities Centre of Expertise
- Pensions Centre of Expertise
- Property Centre of Expertise
- Financial Instruments Centre of Expertise (see items which require mandatory consultation later in this section)

49.7 They may, respectively, be contacted using the following email addresses/query form:

- CharitiesCoE@nao.org.uk
- PensionsCoE@nao.org.uk
- PropertyCoE@nao.org.uk
- Financial Instruments CoE query form

49.8 The Centres of Expertise may establish their own processes for assisting engagement teams in assessing the need for an expert (including risk assessment tools), scoping this work and engaging with relevant external providers where appropriate.

49.9 ***Consultation required*** Engagement teams are required to consult with the Financial Instruments Centre of Expertise in respect of any material financial instruments balance which:

- is derived from a complex model(s) with an unusual underlying methodology (which questions its compliance with the relevant standards and industry best practice); or

- is derived from significant management's judgements (for example, complex and material post model adjustments (PMAs) or valuation techniques for unlisted equity investments); or
- relies on significant assumptions from third party sources (i.e., future macroeconomic assumptions over specific and specialist industries or sectors, such as energy markets); or
- relates to an unlisted equity investment and uses unobservable inputs (Level 3 inputs, as defined in IFRS 13 *Fair value measurement*) and complex valuation methods such as cost as a proxy, discounted cash flows, options valuations or comparable multiples; or
- relates to expected credit losses (ECLs) where subjective assumptions are made around key elements of judgement including the credit risk, discount rates and the use of forward-looking data; or
- is complex and the audit team requires support in assessing the control environment within the audited entity (for example, confirming the appropriateness of credit file reviews).

Analytical methodology

49.10 The Analytical Methodology Team (AMT) can provide guidance relating to statistical techniques, analytical techniques and issues surrounding data collection, analysis and evaluation. They may be contacted via the Financial Audit Support Tool (FAST).

Digital and IT audit

49.11 The Digital and IT Audit function can help teams with:

- auditing digital technologies, including the systems, processes, people and data employed by audited bodies; and
- using digital technologies in our audit approach including tools, systems, processes and data.

Hubs

49.12 Expertise and resources from the Hubs and how to contact them may be found on their Sharepoint pages. The Hubs include:

- Analysis
- Commercial
- Digital
- Financial and Risk Management
- Major Project Delivery
- People and Operational Management

Fraud and error

49.13 The Financial and Risk Management Hub has responsibility for the NAO's central work on auditing fraud and error.

49.14 ***Consultation required*** Paragraph 33-1 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* requires the engagement team to consider whether specialised skills or knowledge are needed to investigate a misstatement due to fraud or suspected fraud further for the purposes of the audit. Engagement teams in such a situation should consult FAPQ along with those in the Financial and Risk Management Hub who are responsible for the Hub's work on fraud and error.

Other internal expertise

49.15 ***Consultation required*** Engagement teams with a need for expertise not covered by the sources described above should consult FAPQ, who may recommend the use of external expertise (see Chapter 50: Obtaining external expertise).

Chapter 50: Obtaining external expertise

Relevant standards and guidance

50.1 Paragraphs A19 and A101 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deal with situations where the engagement team includes a member with expertise in a specialised area of accounting or auditing (an auditor's expert).

50.2 Paragraphs 8 and A45 to A59 of ISA (UK) 500 (Updated May 2022) *Audit evidence* deal with the auditor's use of the work of an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements (a management's expert).

50.3 ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors* deals with the external auditor's responsibilities if using the work of internal auditors. This includes:

- using the work of the internal audit function in obtaining audit evidence; and
- using internal auditors to provide direct assistance under the direction, supervision and review of the external auditor.

50.4 Paragraphs 1-197 to 1-199 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 610 (Revised June 2013) (Updated May 2022) in the public sector.

50.5 ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert* deals with the auditor's responsibilities relating to the work of an individual or organisation in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

50.6 Paragraphs 1-201 to 1-203 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 620 (Revised November 2019) (Updated May 2022) in the public sector.

Financial Audit Contract

50.7 When seeking to engage external expertise, other than through arrangements set up by the Centres of Expertise or Hubs (see Chapter 49: Obtaining internal expertise), in the first instance, engagement teams should determine whether this can be procured through the Financial Audit Contract. Further guidance may be found on the Financial Audit Contract pages on Sharepoint.

Other external expertise

50.8 ***Consultation required*** Where engagement teams identify needs for external expertise that cannot be met through the arrangements described above, they should consult FAPQ, who may arrange for a procurement process to take place in coordination with the Central Procurement Team.

50.9 ***Consultation required*** Engagement teams should be aware that the lead times for obtaining external expertise outside existing procurement frameworks may be lengthy (particularly at busy times for the Central Procurement Team). It is therefore important to engage with FAPQ at an early stage where such an arrangement may be appropriate for the engagement.

Chapter 51: Scoping and evaluating the work of an expert

Relevant standards and guidance

51.1 Paragraphs A19 and A101 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements* deal with situations where the engagement team includes a member with expertise in a specialised area of accounting or auditing (an auditor's expert).

51.2 Paragraphs 8 and A45 to A59 of ISA (UK) 500 (Updated May 2022) *Audit evidence* deal with the auditor's use of the work of an individual or organisation possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements (a management's expert).

51.3 ISA (UK) 610 (Revised June 2013) (Updated May 2022) *Using the work of internal auditors* deals with the external auditor's responsibilities if using the work of internal auditors. This includes:

- using the work of the internal audit function in obtaining audit evidence; and
- using internal auditors to provide direct assistance under the direction, supervision and review of the external auditor.

51.4 Paragraphs 1-197 to 1-199 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 610 (Revised June 2013) (Updated May 2022) in the public sector.

51.5 ISA (UK) 620 (Revised November 2019) (Updated May 2022) *Using the work of an auditor's expert* deals with the auditor's responsibilities relating to the work of an individual or organisation in a field of expertise other than accounting or auditing, when that work is used to assist the auditor in obtaining sufficient appropriate audit evidence.

51.6 Paragraphs 1-201 to 1-203 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 620 (Revised November 2019) (Updated May 2022) in the public sector.

Scoping the work of an auditor's expert and related NAO procedures

51.7 When planning to use the work of any auditor's expert, the engagement should determine the nature, timing and extent of procedures to evaluate the competence, capability and objectivity of the auditor's expert. This should include consideration of the matters set out in paragraph 8 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) and the related application guidance. The engagement team should carry out the procedures themselves in accordance with paragraph 9 and the related application guidance.

51.8 The engagement team should plan and document an approach to the audit area that provides the full assurance required, rather than assuming that the expert's report will provide sufficient assurance across all risks of material misstatement.

51.9 Members of NAO staff or contractor staff from outside of financial audit will usually not be subject to the NAO's financial audit quality control policies and procedures.

51.10 The engagement team should carry out the requirements of paragraphs 10 to 11 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) and the related application guidance to obtain

an understanding of the field of expertise of the auditor's expert and to agree matters, in writing where appropriate, with the auditor's expert relating to their planned work.

51.11 Understanding the field of expertise of the expert usually involves understanding:

- whether that expert's field has areas of specialty within it that are relevant to the audit;
- whether any professional or other standards, and regulatory or legal requirements apply;
- what assumptions and methods, including models where applicable, are used by the NAO expert, and whether they are generally accepted within that expert's field and appropriate for financial reporting purposes; and
- the nature of internal and external data or information the NAO expert uses.

51.12 The engagement team should ensure that the agreed division of tasks is reflected in the final scope of the auditor's expert's report, and also in the work that the engagement team plans to perform.

51.13 An auditor's external expert's working papers are their own and do not form part of the audit documentation in the absence of any agreement to the contrary reached at the time of the audit. The engagement team should either:

- include an agreement in the engagement letter with the expert that the external auditor's expert's working papers would form part of the audit documentation; or
- include in the Apex audit file sufficient documentation to meet the requirements of auditing standards.

51.14 The engagement team should include in the Audit Planning Report details of our intended use of an auditor's expert in order to agree protocols for the expert's involvement.

51.15 Information regarding the competence, capabilities and objectivity of an NAO expert may come from a variety of sources, such as:

- personal experience with previous work of that expert;
- discussions with that expert;
- discussions with other auditors or others who are familiar with that expert's work;
- knowledge of that expert's qualifications, membership of a professional body or industry association, license to practice, or other external recognition; and/or
- published papers or books written by that expert.

51.16 Other matters that may be relevant include:

- the relevance of their expertise for the purposes of the audit, including any areas of specialty within that expert's field e.g. a particular actuary may specialise in property and casualty insurance, but have limited expertise regarding pension calculations;
- the expert's knowledge of relevant accounting and auditing requirements, such as knowledge of assumptions and methods, including models where applicable, that are consistent with the FReM (or other applicable financial reporting framework); and
- whether unexpected events, changes in conditions, or the audit evidence obtained from the results of audit procedures indicate that it may be necessary to reconsider the initial evaluation of the competence, capabilities and objectivity of the NAO expert as the audit progresses.

Use of the work of an auditor's expert – independence and ethical considerations

51.17 Although an auditor's external expert is not a member of the engagement team, the external expert is subject to ethical requirements that are relevant to the audit engagement, including independence. Such requirements may be different, or in addition, to those applying to the external

expert, by virtue of their membership of a particular professional body. Accordingly, the auditor's external expert is subject to the requirements in the FRC's Ethical Standard as applicable to that expert, recognising that they may not be an auditor or professional accountant.

51.18 The threats to the objectivity of an expert are the same as for those for auditors, which are discussed in Chapter 8: Ethical considerations. Safeguards may eliminate or reduce such threats. However, in some circumstances it may not be possible to devise appropriate safeguards, such as when the same expert has also been involved in the preparation of the information being audited.

51.19 In evaluating the objectivity of an NAO external expert, it may be relevant to:

- inquire of the entity about any known interests or relationships that the entity has with the NAO external expert that may affect that expert's objectivity;
- discuss with the NAO expert any applicable safeguards, including any professional requirements that apply to that expert; and
- evaluate whether the safeguards are adequate to reduce threats to an acceptable level.

51.20 Interests and relationships that it may be relevant to discuss with the NAO expert include:

- financial interests;
- business and personal relationships; and
- provision of other services by the expert, including by the organisation in the case of an external expert that is an organisation.

51.21 In some cases, it may also be appropriate for the engagement team to obtain a written representation from the NAO external expert about any interests or relationships.

Evaluating the adequacy of the auditor's expert's work

51.22 Paragraphs 12 to 13 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) and the related application guidance set out the requirement to evaluate the adequacy of the auditor's expert's work for the auditor's purposes and procedures to be undertaken where the auditor determines that the work of the auditor's expert is not adequate for the auditor's purposes.

51.23 The requirement in paragraph 12(b) of ISA (UK) 620 (Revised November 2019) (Updated May 2022) to evaluate the relevance and reasonableness in the circumstances of significant assumptions and methods used in the auditor's expert's work will usually not be necessary where the auditor's expert has been evaluating the assumptions and methods used by management. In these circumstances, the engagement team should consider whether the auditor's expert has adequately reviewed those assumptions and methods.

51.24 The engagement team should refer to Chapter 36: Accounting estimates where the work of the auditor's experts concerns an accounting estimate.

51.25 A report by an expert that is reliant upon unchecked source data or unassessed assumptions will not provide sufficient appropriate audit evidence.

51.26 The engagement team should consider any caveats or qualifications included in the expert's findings, and clearly conclude upon these in the Apex audit file.

51.27 In accordance with paragraph 15-1 of paragraph 14 of ISA (UK) 620 (Revised November 2019) (Updated May 2022), the engagement team should ensure that any request for advice from an expert, together with the advice received, is documented on the Apex audit file.

51.28 If the engagement team determines that the work of the auditor's expert is not adequate for the purposes of the audit, they should:

- agree with that expert on the nature and extent of further work to be performed by that expert; and
- perform additional audit procedures appropriate to the circumstances.

51.29 Procedures to evaluate the relevant and reasonableness of the expert's findings or conclusions, and their consistency with other audit evidence may include:

- inquiries of the NAO expert;
- reviewing the NAO expert's working papers and reports;
- corroborative procedures, such as observing the NAO expert's work, examining published data, (such as statistical reports from reputable, authoritative sources), confirming relevant matters with third parties, performing detailed analytical procedures; and re-performing calculations;
- discussion with another expert with relevant expertise when, e.g. the findings or conclusions of the NAO expert are not consistent with other audit evidence; and/or
- discussing the NAO expert's report with management.

51.30 Factors relevant to evaluating an NAO expert's assumptions and methods include whether they are:

- generally accepted within the expert's field;
- consistent with the requirements of the financial reporting framework;
- dependent on the use of specialised models; and
- consistent with those of management, and if not, the reason for, and effects of, the differences.

51.31 Care should be taken when using an NAO expert that this is not seen as a substitute for the audited entity taking responsibility for preparation of the financial statements. For example, any independent estimates developed by an NAO expert should be used to test the estimates that management have made, rather than used as the basis for the figures recognised in the financial statements.

51.32 The engagement team will usually be responsible for checking source data by, for example:

- verifying the origin of the data, including obtaining an understanding of, and where applicable testing, the internal controls over the data and, where relevant, its transmission to the expert; and/or
- reviewing the data for completeness and internal consistency.

51.33 When the nature of the source data used by an NAO expert is highly technical in relation to the expert's field, it may be the case that the expert tests the source data. If the NAO expert has tested the source data, inquiry of that expert by the engagement team, or supervision or review of that expert's tests may be an appropriate way to evaluate that data's relevance, completeness, and accuracy.

Reference to the auditor's expert in the auditor's report

51.34 ***Consultation required*** In accordance with paragraph 14 of ISA (UK) 620 (Revised November 2019) (Updated May 2022), the C&AG should not refer to the work of an auditor's expert in an auditor's report containing an unmodified opinion unless required by law or regulation to do so. In such extremely rare circumstances, the engagement team should consult FAPQ. If such reference is required by law or regulation, the C&AG's opinion would indicate that the reference does not reduce the C&AG's responsibility for the opinion.

51.35 If the C&AG is issuing a modified opinion, or report, it may be necessary to make reference to the work of an NAO expert to enable a proper understanding of the modification or report. In such circumstances, the requirements of paragraph 15 of ISA (UK) 620 (Revised November 2019) (Updated May 2022) apply.

Use of the work of an auditor's expert – quality considerations

51.36 For specialist and complex areas it may well be appropriate to engage an auditor's expert, especially where management has used an expert. Engagement teams should consider and evidence on file whether the engagement team has the necessary skills for the specific issues that relate to that engagement

51.37 Where engagement teams engage an expert, they need to sufficiently evaluate the expert's work to assess whether it is adequate to support the audit opinion.

51.38 Where the auditor's expert identifies issues and shortcomings, the engagement team needs to fully consider these and evidence how these have been addressed (see the section below entitled 'Instances where the auditor's expert identifies issues').

51.39 If the auditor's expert's work involves examining a sample, engagement teams need to ensure the sample is representative of the area where a view is sought.

Instances where the auditor's expert identifies issues

51.40 Where the auditor's expert has raised issues in their report to the engagement team, the engagement team should undertake the following actions:

- Reducing the risk: Engagement teams are required to agree the nature, scope and objectives of the expert's work. By carefully scoping the work of the expert, the engagement team can reduce the risk of adverse findings arising which are not relevant to the risks of material misstatement you are aiming to address. The aim is to ensure that the work of the expert is relevant in supporting the conclusions on which the opinion is based. This also reduces the risk that the engagement team arrives at a conclusion that the work of the expert is not adequate when evaluating their work. This might be done by:
    - Being precise about the matter on which the engagement team are seeking an expert view.
    - Considering areas where there may be a range of expert views
    - Incorporating evaluation into the scope of the expert's work. Especially where issues are expected to occur, the engagement team should consider incorporating making an estimate of the likely financial impact of any deficiencies within the scope of the expert's work.
- Following up the expert's concerns: Despite actions taken at the scoping stage, it is possible that the auditor's expert may identify issues that the engagement team considers to be immaterial or irrelevant to the audit opinion. In these cases, it is critical the engagement team quantify the impact of the issues raised to support this judgment.

Use of information produced by management's experts

51.41 The preparation of the financial statements may require expertise in fields other than accounting or auditing, such as actuarial calculations, valuations or engineering data. Management may employ or engage experts to provide the necessary expertise.

51.42 Paragraph 8 of ISA (UK) 500 (Updated May 2022) and the related application guidance set out procedures for the auditor to undertake where information to be used as audit evidence has been prepared using the work of a management's expert.

51.43 For example, as per paragraph A46 of ISA (UK) 500 (Updated May 2022), an individual or organisation may possess expertise in the application of models to estimate the fair value of securities for which there is no observable market. If the individual or organisation applies that expertise in making an estimate which the audited entity uses in preparing its financial statements, the individual or organisation is a management's expert. If, on the other hand, that individual or organisation merely provides price data regarding private transactions not otherwise available to the audited entity which the audited entity uses in its own estimation methods, such information, if used as audit evidence, is information from an external information source and not the use of a management's expert by the audited entity.

51.44 The extent of the work required depends on how significant management's expert's work is in the context of the audit: i.e., the level of work should reflect the Financial Statement Impact (magnitude) and Likelihood of the related Risk(s) of Material Misstatement.

51.45 If management's experts work involves significant assumptions, engagement teams need to evaluate the relevance and reasonableness of those assumptions. Where appropriate, engagement teams should consider requesting that management perform sensitivity analysis in respect of key assumptions and consider the need to disclose this information in the financial statements.

51.46 Where the audited entity has used an expert because of a need for expertise in a field other than accounting or auditing, the engagement team should determine whether to appoint an auditor's expert.

51.47 The nature, timing and extent of the audit procedures required to use the work of management expert may be affected by, for example: who employed the expert, the complexity of the matter, and so on. Paragraph A47 of ISA (UK) 500 (Updated May 2022) gives further examples.

51.48 The competence, capabilities and objectivity of management's expert should be evaluated to assess the reliability of information produced by the expert.

- Competence relates to the nature and level of expertise of management's expert.
- Capability relates the ability of management's expert to exercise that competence in the circumstances. For example, geographic location, and the availability of time and resources.
- Objectivity relates to the possible effects that bias, conflict of interest or the influence of others may have on the judgment of management's expert.

51.49 Information can come from various sources such as previous experience, discussions with the expert or others familiar with them, membership of a professional body, published works of the expert, or the auditor's experts. Relevant factors should be considered, such as professional requirements, legal requirements and so on. Further examples can be found in paragraphs A49 to A51 of ISA (UK) 500 (Updated May 2022).

51.50 Threats to objectivity can arise from a variety of sources, which are analogous to those considered in the FRC's Ethical Standard:

- self-interest threats;
- advocacy threats;
- familiarity threats;
- self-review threats; and

- intimidation threats.

51.51 Safeguards may reduce such threats, and may be created either by external structures, such as legislation, or by the management's expert's work environment, such as quality control procedures.

51.52 The threat to objectivity created by being an employee of the entity will always be present. An expert employed by the entity cannot therefore ordinarily be regarded as being more likely to be objective than other employees. The engagement team should consider other interests and relationships that may create threats, such as financial interests, business and personal relationships or provision of other services.

51.53 Understanding the work of the management's expert includes the relevant field of expertise. This may be obtained when it is determined whether the engagement team have the expertise to evaluate the work of the management's expert, or whether the engagement team need to involve an auditor's expert in the audit to be able to evaluate management's expert's work. The engagement team should obtain an understanding of any legal requirements that apply, assumptions and data used and other relevant factors.

51.54 Paragraph A59 of ISA (UK) 500 (Updated May 2022) gives examples of considerations when evaluating the appropriateness of the work of management's expert as audit evidence for the relevant assertion.

Use of the work of management's expert – quality considerations

51.55 Engagement teams should sufficiently evidence their assessment of management's expert's competence and capabilities.

51.56 If management's expert's work involves significant assumptions, engagement teams need to evaluate the relevance and reasonableness of those assumptions.

51.57 Where appropriate, engagement teams should consider requesting that management perform sensitivity analysis in respect of key assumptions and consider the need to disclose this information in the financial statements.

51.58 Engagement teams should consider and evidence their conclusions on the need for an auditor's expert to assess the work of management's expert.

Using the work of internal audit

51.59 If the engagement team are planning to use the results of a specific piece of work by internal audit, they should discuss with internal audit:

- the timing of their work;
- the planned extent of their work;
- our assessment of materiality and performance materiality;
- their proposed methods of item selection;
- how they will document the work performed; and
- their review and reporting procedures.

51.60 The engagement team should always evaluate the scope of internal audit's work and determine whether it is necessary to perform additional procedures to obtain sufficient assurance over a risk of material misstatement.

51.61 The engagement team should evaluate and document the conclusions reached regarding the adequacy of internal audit's work for the purposes of the audit, including whether:

- the work was performed by internal auditor having adequate technical training and proficiency
- the work was properly supervised and documented
- adequate audit evidence has been obtained to enable the internal auditors to draw reasonable conclusions;
- conclusions reached are appropriate in the circumstances and any reports prepared by the internal auditors are consistent with the results of the work performed; and
- any exceptions or unusual matters disclosed by the internal auditors are properly resolved.

51.62 The engagement team should review the working papers, findings and report of pieces of work the engagement team plan to use.

51.63 The engagement team should document the details and results of their own audit procedures performed on internal audit's work to earn the right to use that work. These may include one or more of:

- examination of items already examined by the internal auditors;
- examination of other similar items; and/or
- observation of procedures performed by the internal auditors

51.64 The engagement team should document the professional judgements taken in determining the extent of procedures.

51.65 The engagement team should ensure the audit documentation, including the required communications with those charged with governance under ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance*, which are made in the Audit Planning and Audit Completion Reports, is clear as to whether internal audit's work is being used to inform the risk assessment, or whether a specific piece of work is being used to provide assurance.

Section 13: Concluding and reporting

Chapter 52: Evaluating the results of procedures, including identified misstatements and irregular transactions

Relevant standards and guidance

52.1 ISA (UK) 450 (Revised June 2016) (Updated May 2022) *Evaluation of misstatements identified during the audit* deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.

Background

52.2 The purpose of the audit is to obtain reasonable assurance to support the C&AG's opinion that the financial statements as a whole are free from material misstatement and give a true and fair view. Our controls and substantive procedures are planned to obtain this assurance, based upon the results of the risk assessment procedures performed at the planning stage.

52.3 The objective of the engagement team is to evaluate the effect of identified misstatements on the audit; and the effect of uncorrected misstatements, if any, on the financial statements. The engagement team will also evaluate identified irregularities, if any.

52.4 In doing so, the engagement team should consider whether in aggregate the procedures performed have provided the planned level of assurance, including any tests of controls performed.

52.5 A "misstatement" is defined in paragraph 4 of ISA (UK) 450 (Revised June 2016) (Updated May 2022) as a difference between the amount, classification, presentation or disclosure of a reported financial statement item and the amount, classification, presentation, or disclosure that is required for the item to be in accordance with the applicable financial reporting framework. Misstatements can arise from error or fraud.

52.6 For the majority of the NAO's audits, where the C&AG is giving a "true and fair" opinion, the definition of a "misstatement" also includes any adjustments of amounts, classifications, presentation, or disclosures that are considered necessary for the financial statements to give a true and fair view. This also applies if the NAO is undertaking a "presents fairly in all material respects" audit.

52.7 Misstatements can arise in a number of ways including:

- an inaccuracy in gathering or processing data from which the financial statements are prepared;
- an omission of an amount or disclosure;
- an incorrect accounting estimate arising from overlooking, or clear misinterpretation of, facts;
- judgments of management concerning accounting estimates that are considered unreasonable; or
- the selection and application of accounting policies that are inappropriate.

52.8 Chapter 30: Fraud responsibilities contains more detailed examples of how misstatements can arise through fraud. The nature and cause of a misstatement may indicate that other misstatements may exist and so require revisions to our audit procedures.

52.9 “Uncorrected misstatements” are misstatements that have been accumulated during the audit and that have not been corrected.

52.10 “Most Likely Error”/”MLE” is our best estimate of the level of error in a population based upon the procedures performed.

52.11 “Upper Error Limit” - this is the maximum misstatement would be expected given the procedures which have been performed.

52.12 Tests are planned to enable the engagement team to estimate the maximum level of error as the Most Likely Error +/- Performance Materiality (or precision). Therefore, if the Most Likely Error significantly exceeds the expected level of error, the Upper Error Limit will exceed materiality, and the engagement team may need to perform more procedures to obtain sufficient assurance.

Overall process for evaluating the results of procedures and misstatements identified

52.13 In order to be able to form an opinion on the financial statements, the engagement team should evaluate whether they have obtained reasonable assurance the financial statements as a whole are free from material misstatement or irregularity.

52.14 The engagement team should evaluate whether the procedures performed have obtained the planned level of assurance, and, if misstatements have been identified, whether these are material to the financial statements.

52.15 The engagement team should assess whether each procedure provides the planned level of assurance, or otherwise identifies misstatements which impact upon our approach.

52.16 The engagement team should assess whether in aggregate the procedures performed have provided the planned level of assurance, whether the misstatements identified require further modifications to our audit approach, or whether uncorrected misstatements are material to the financial statements.

52.17 The engagement team should evaluate the results of procedures performed to determine whether the planned assurance has been achieved from the test and whether any revisions are required to our planned procedures.

Figure 52A: High-level process for concluding and reporting

Performing the audit	Concluding and reporting
Evaluate the results of procedures and whether planned assurance is obtained	Evaluate whether overall planned assurance obtained
Accumulate misstatements that are not clearly trivial (after extrapolation)	Evaluate effect of uncorrected misstatements in the audit
Request management correct misstatements	

Evaluation of results of audit procedures

52.18 The engagement team should evaluate the results of controls and substantive procedures as the audit progresses to determine whether the planned level of assurance is being achieved.

52.19 As per paragraph 7 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), if, at the engagement team's request, management has examined a class of transactions, account balance or disclosure and corrected misstatements that were detected, the engagement team should perform additional audit procedures to determine whether misstatements remain.

52.20 If misstatements have been identified in a sample, the engagement team may request management examine a class of transaction, account balance or disclosure in order for management to understand the cause of the misstatement, perform procedures to determine the amount of the actual misstatement, and make appropriate adjustments to the financial statements.

Evaluation of results of audit procedures – controls

52.21 Engagement teams should refer to Chapter 35: Controls testing when evaluating the results of tests of controls.

Evaluation of results of audit procedures – substantive analytical procedures

52.22 Engagement teams should refer to Chapter 33: Analytical procedures when evaluating the results of substantive analytical procedures.

Evaluation of results of audit procedures – tests of detail

52.23 Engagement teams should refer to Chapter 34: Tests of detail when evaluating the results of tests of detail.

Evaluation of misstatements

52.24 In order to respond appropriately to misstatements or irregularities identified in testing, it is important that engagement team members who identify issues should obtain an understanding of their nature and cause.

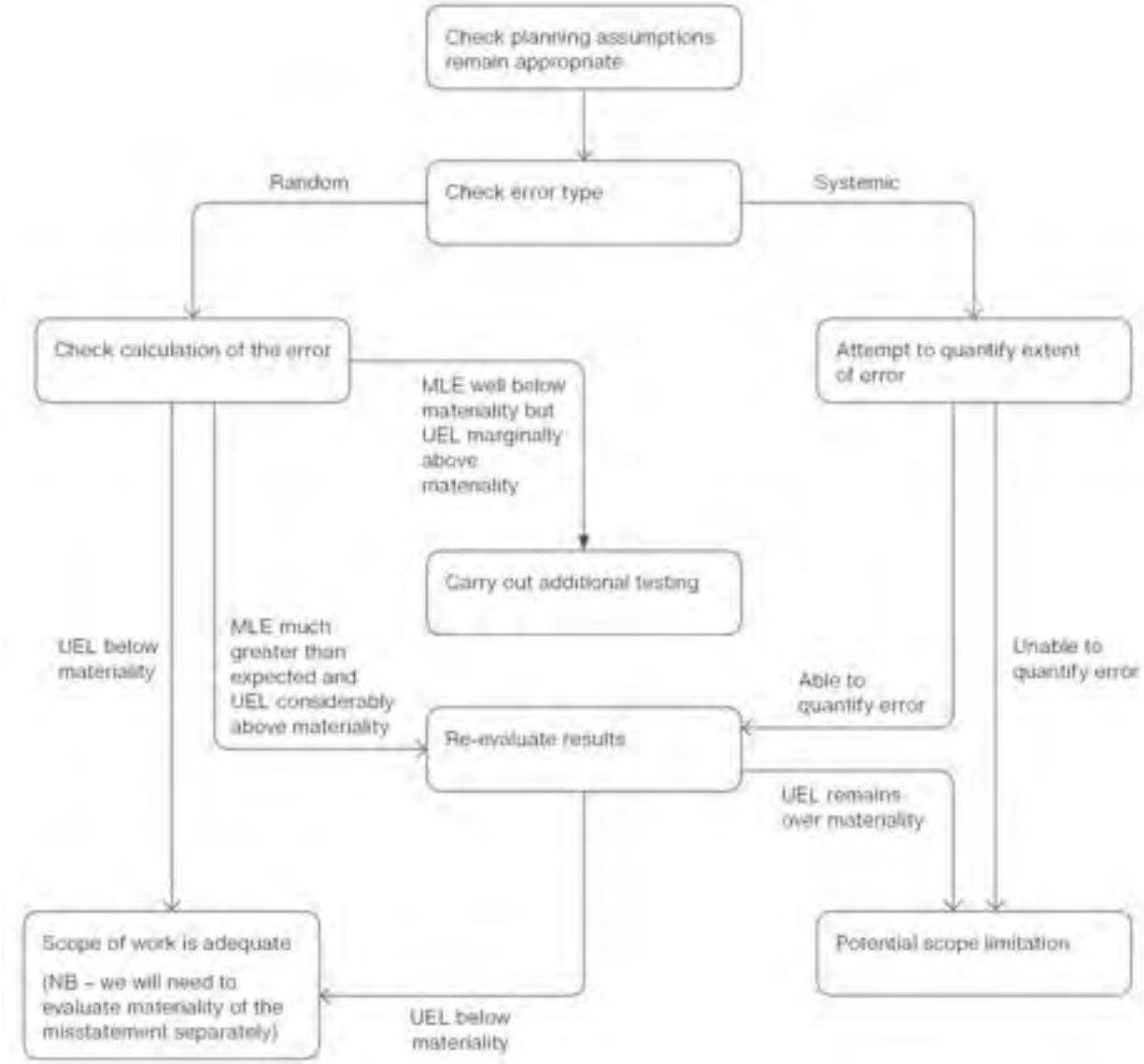
52.25 The engagement team should determine whether they indicate that other misstatements may exist. This may be due to a previously unidentified significant risk. Indications that other misstatements may exist include if a misstatement arose from a breakdown in internal control, or from inappropriate assumptions or valuation methods that have been widely applied by the entity.

52.26 In addition, such misstatements or irregular transactions may be intentional, and may indicate the possibility of fraud. Where the engagement team identifies a misstatement, paragraph 35 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires them to obtain an understanding of how the misstatement arose and evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the engagement team should revisit the Engagement Team Discussion on Risk and Fraud and, as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan to reflect any additional risks of material misstatement or risks of material irregular transactions. Further guidance may be found in Chapter 30: Fraud responsibilities.

52.27 There is a risk that other misstatements may exist that, aggregated with identified misstatements may be material, the engagement team should revisit their risk assessment with the Risk Assessment in Apex.

52.28 Where the Upper Error Limit resulting from extrapolating the results of a test of detail in accordance with Chapter 34: Tests of detail exceeds materiality, the engagement team should follow the process set out in ***Figure 52B*** to evaluate the scope of work performed. If engagement teams identify issues when evaluating the scope of work, they may consult FAPQ.

Figure 52B: Decision process for responding to errors



52.29 The engagement team should consider whether the planning assumptions remain appropriate. In particular, they should consider whether the risk assessment and required assurance from the Audit Response indicated within the Risk Assessment in Apex remains appropriate; and if the engagement team have concluded controls are operating effectively, whether this conclusion remains appropriate.

52.30 If the expected level of error increases and/or performance materiality decreases, the engagement team should as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan.

52.31 The engagement team should consider whether the misstatements identified appear to be due to a systematic error, or random (non-systematic). For systematic errors, teams should attempt to obtain evidence enabling them to quantify the total error:

- If the error can be quantified, then the planned assurance has been obtained from the test and the scope of work is adequate. The engagement team would then need to consider the implications of the misstatement on our overall audit conclusions.

- ***Consultation required*** If the error cannot be quantified, then this may indicate a scope limitation to the audit. Engagement teams must consult with FAPQ in these circumstances.

52.32 For random (non-systematic) errors, teams should first recheck the calculation of the error. If this indicates the Upper Error Limit (UEL) is below materiality or the Most Likely Error (MLE) is below the expected level of error, then the planned assurance has been achieved from the test and the scope of work is adequate. Otherwise, additional testing should be performed to obtain adequate assurance.

52.33 Engagement teams may contact FAPQ if it is not clear how to extend sampling to provide appropriate assurance in the circumstances. This is particularly relevant where the engagement team have used a bespoke sampling approach devised by AMT. In these circumstances, AMT will be able to advise on how to extend the sample – they may be contacted via the Financial Audit Support Tool (FAST).

52.34 Where the initial results are indicative of material misstatement or material irregular transactions, an alternative sampling basis may be required. In this circumstance, engagement teams may consult the Analytical Methodology Team using the Financial Audit Support Tool (FAST).

52.35 If additional testing reduces the UEL below materiality, then the planned assurance has been achieved from the test and the scope of work is adequate.

52.36 ***Consultation required*** If additional testing does not reduce the UEL below materiality (due to additional errors being identified) then this may indicate a scope limitation to our audit. Engagement teams should consult with FAPQ in these circumstances.

52.37 If the engagement team have identified misstatements using a sample test of detail, the results of procedures should be evaluated by assessing whether the Upper Error Limit ("UEL") is greater than materiality.

52.38 If the UEL is below materiality, subject to any qualitative factors, the planned level of assurance from the test has been obtained. If the UEL is above materiality, then sufficient assurance may not have been obtained from the work performed. Engagement teams should evaluate the impact on the audit and whether any additional procedures are required.

52.39 Profiling can be complex, in particular in quantifying misstatements identified, and engagement teams should ensure that they are familiar with the guidance in Chapter 34: Tests of detail before using this technique.

52.40 When using stratified sampling, misstatements or irregularities in sub-populations of audit interest should be extrapolated and evaluated using the sampling guidelines in Chapter 34: Tests of detail and guidance provided by the Analytical Methodology Team.

52.41 ***Consultation required*** If misstatements or irregular transactions are detected in several sub-populations, they should be combined when considering the possible effect of misstatements and irregular transactions on the balance as a whole. Engagement teams should consult the Analytical Methodology Team on how to extrapolate and evaluate misstatements or irregularities arising in the residual sub-population.

52.42 Evaluation of sample testing can be complex, and engagement teams may consult with FAPQ and the Analytical Methodology Team as required. The conclusion on whether the planned

level of assurance has been achieved depends upon the MLE and whether the upper and lower error limits are above or below materiality.

52.43 If the error limits extend above materiality, sufficient assurance may not have been obtained, and the engagement team may consult FAPQ to evaluate the adequacy of the scope of our work.

52.44 ***Consultation required*** The engagement team should consult FAPQ where the sum of unadjusted misstatements is within 5% of performance materiality.

52.45 ***Consultation required*** Where, in the engagement team's opinion, the level of adjusted and unadjusted misstatements is such that it provides evidence of the quality of the control environment that may call into question the judgements made when calculating performance materiality, they should:

- consult FAPQ;
- consider the implications for the team's evaluation of the audited entity's control environment at the planning stage; and
- as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan to reflect any additional risks of material misstatement or risks of material irregular transactions.

52.46 If a 100% test of a balance has been performed, the actual level of misstatements in the balance will have been identified, and it is not necessary to quantitatively evaluate the scope of work performed.

52.47 If misstatements have been identified using a sample selected through other tests of detail, then the results of procedures should be evaluated by assessing whether the MLE is less than the expected level of error.

52.48 If the MLE is less than the expected level of error then the planned level of assurance has been obtained from the test.

52.49 If the MLE is above the expected level of error, then sufficient assurance may not have been obtained from the work performed. The engagement team should evaluate the impact on the audit and whether any additional procedures are required, as discussed below, and clearly document the rationale for their conclusion on the adequacy of the scope of work performed. Based on the results of this evaluation, the engagement team should, as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan

52.50 Clearly trivial items are clearly inconsequential, whether taken individually or in aggregate and whether judged by any criteria of size, nature or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the engagement team should not consider them clearly trivial. A threshold is set at the planning stage above which items cannot be considered clearly trivial (see Chapter 16: Materiality, performance materiality and trivial threshold).

52.51 Engagement teams should not communicate misstatements which may arise due to fraud without following the process set out in Chapter 30: Fraud responsibilities.

52.52 Timely communication of misstatements is part of effective communication throughout the audit. It enables management to evaluate the issues identified, decide whether they agree they are misstatements, and take action as necessary.

52.53 Management should maintain accurate books and records, and so should correct identified misstatements. Doing so:

- reduces the risk that the cumulative effect of immaterial uncorrected misstatements could be material in future years; and
- reduces the risk that undetected misstatements in the current year financial statements could be material in combination with uncorrected identified misstatements.

52.54 Management's reasons for not correcting misstatements may be particularly relevant when considering qualitative aspects of the entity's accounting practices, including indicators of possible bias in management's judgments.

Evaluation of irregular transactions

52.55 The engagement team should evaluate irregular transactions separately from misstatements. The engagement team should obtain a proper understanding of the qualitative aspects and context of irregular transactions identified in order to be able to assess whether they are material. The engagement team should consider whether irregular transactions identified are additive or are separate issues.

52.56 An irregular transaction in the financial statements occurs where a transaction or balance is recorded within the financial statements as a result of a non-compliance with the entity's framework of authorities.

52.57 In considering whether an irregularity is quantitatively material, the engagement team should consider the value of irregularity within the transaction. The level of irregularity within the transaction is the additional income or expenditure recognised by the entity as a result of non-compliance with the framework of authorities. This does not necessary constitute the full value of the transaction concerned.

52.58 A qualitative assessment of whether an irregularity is material to the financial statements, needs to take account of the views of the users of the financial statements. In the NAO context, this is primarily the view of Parliament. Therefore, factors to consider in determining whether an irregularity is qualitatively material would include:

- the level of disclosure made by the entity of the irregularity in its Annual Report and in particular the Governance Statement;
- actions taken by management to address the causes of the irregularity;
- whether the irregularity was a result of deliberate or inappropriate actions by management;
- whether the non-compliance with the framework of authorities has been separately reported to Parliament or has otherwise been made public;
- the impact of the irregularity on individuals or corporate entities; and
- whether the irregularity is a direct breach of Parliament's intentions (for example expenditure in excess of a voted control total).

52.59 The effect of different sources of irregularity should be assessed on an individual basis and not aggregated. However, the cumulative effect of multiple irregularities within an entity may be a contributory factor in the consideration of whether any of the individual irregularities are material.

52.60 Where a judgement is made that an irregularity is not material, the C&AG may nonetheless decide to take alternative courses of action to influence improvement within the entity. Such courses of actions may include:

- a letter being written by the C&AG to the Accounting Officer concerning the matter and actions which may be required to rectify the situation;
- scoping further Value for Money or other non-financial audit work in the area in which the irregularity occurred;
- a report on accounts concerning the matter which led to the irregularity; and/or
- reporting the matter to Parliament through the Chair of the Committee of Public Accounts.

52.61 ***Consultation required*** Engagement teams must consult with FAPQ where they have identified irregular transactions that they consider may be material.

Accumulation of identified misstatements

52.62 Paragraph 5 of ISA (UK) 450 (Revised June 2016) (Updated May 2022) and the related application guidance require the engagement team to accumulate misstatements identified during the audit, other than those that are clearly trivial, distinguishing between:

- actual misstatements;
- extrapolated misstatements (our best estimate of misstatements in populations extrapolated from sample tests);
- judgemental misstatements (differences arising from the judgments of management concerning accounting estimates that are considered unreasonable, or the selection or application of accounting policies that are considered inappropriate).

52.63 In accordance with paragraph 11(b) of ISA (UK) 450 (Revised June 2016) (Updated May 2022), accumulated misstatements should include uncorrected misstatements related to prior periods.

52.64 As stated in paragraph A8 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), where the aggregate of misstatements accumulated during the audit approaches materiality, there may be a greater than acceptable level of risk that possible undetected misstatements, when taken with the aggregate of misstatements accumulated during the audit, could exceed materiality. Undetected misstatements could exist because of the presence of sampling risk and non-sampling risk.

52.65 As required by paragraph 8 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), the engagement team should communicate on a timely basis all misstatements accumulated during the audit with the appropriate level of management, unless prohibited by law or regulation and request management to correct those misstatements. This does not include misstatements the engagement team considers to be clearly trivial.

52.66 Paragraphs 9 and A13 of ISA (UK) 450 (Revised June 2016) (Updated May 2022) deal with the situation where management refuses to correct some or all identified misstatements.

52.67 Paragraphs 12 to 13 of ISA (UK) 450 (Revised June 2016) (Updated May 2022) and the related application guidance sets out requirements to communicate identified misstatements, individually, to those charged with governance, unless prohibited by law or regulation, such as due to money-laundering reporting requirements (see Chapter 30: Fraud responsibilities).

52.68 The communication required by paragraph 13 of ISA (UK) 450 (Revised June 2016) (Updated May 2022) (the effect of uncorrected misstatements related to prior periods) should include reporting any non-trivial extrapolated misstatements and irregularities identified through sampling.

Misstatements in other information

52.69 Application of the concept of materiality for the audit is not necessarily the same for the financial statements and the Other Information in the annual report.

52.70 For other information, the auditor considers whether it is subject to a framework which provides a frame of reference for the auditor's judgments about materiality under ISA (UK) 720 (Revised November 2019) (Updated May 2022).

52.71 In the UK, legislation sets out what other information is required in an annual report (excluding the financial statements and the auditor's report thereon). The annual report may include, for example:

- a directors' report;
- a strategic report;
- a non-financial information statement included in the strategic report;
- a separate Corporate Governance Statement; and/or
- a trustees' report.

52.72 The relevant legal requirements do not refer to or define "materiality". They do, however, include terms which are intended to ensure that all relevant information and only that information is provided. For example, the strategic report requirements uses terms such as "principal" (for instance, principal risks), "key" (for instance, key performance indicators) and "necessary for an understanding of" (for example, the strategic report must contain information to the "extent necessary for an understanding of the company's development, performance and position and the impact of its activity…").

52.73 These and similar principles, when considered in the context of an entity, can be considered as relevant discussion of what other information would be material for inclusion in the annual report.

52.74 However, to the extent that the relevant legal requirements do not provide a comprehensive discussion of the application of the concept of materiality to such other information, the frame of reference provided by ISA (UK) 720 (Revised November 2019) (Updated May 2022) is also relevant to the auditor's judgments about materiality.

52.75 As defined in paragraph 12(b) of ISA (UK) 720 (Revised November 2019) (Updated May 2022) *The auditor's responsibilities relating to Other Information*, a misstatement of the other information exists when the other information is incorrectly stated or otherwise misleading (including because it omits or obscures information necessary for a proper understanding of a matter disclosed in the other information). In the UK, a misstatement of the other information also exists when the statutory other information has not been prepared in accordance with the legal and regulatory requirements applicable to the statutory other information.

52.76 The engagement team therefore assesses whether any misstatement of the other information is material, taking into account both the size (quantitative factors) and the nature (qualitative factors) of the misstatement.

52.77 Further guidance is provided in Chapter 32: Other information and other reporting responsibilities.

Final evaluation of the overall scope of work

52.78 As required by paragraph 10 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), prior to the final evaluation of the scope of work and of uncorrected misstatements, the engagement team should reassess materiality to confirm it remains appropriate in the context of the entity's actual financial results.

52.79 The engagement team should assess the adequacy of the scope of work performed through a qualitative and quantitative assessment of identified misstatements, corrected and uncorrected.

52.80 If the scope of the audit is not sufficient (for example, due to the identification of additional significant risks), the engagement team should revise the assessment in the Risk Assessment in Apex and/or the Regularity Testing Plan, as appropriate, and perform the additional controls or substantive procedures required. If the engagement team's concerns regarding the scope of the audit are due to a significant volume of identified errors due to fraud, the engagement team should also revisit the Engagement Team Discussion on Risk and Fraud. Further guidance may be found in Chapter 30: Fraud responsibilities.

52.81 In accordance with paragraph 6 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), the engagement team should consider the nature and cause of identified misstatements. If these indicate that other misstatements, when aggregated with the identified misstatements accumulated during the audit, could be material, the engagement team should determine whether the overall audit strategy, the Risk Assessment in Apex and the Regularity Testing Plan need to be revised.

52.82 In accordance with paragraph 6 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), The engagement team should assess whether the aggregate of identified misstatements is large enough that there is an unacceptable risk that possible undetected misstatements, when taken with uncorrected identified misstatements, could exceed materiality. This aggregation should also take account of the extrapolated errors identified through our sample testing and the precision surrounding these errors (see Chapter 34: Tests of detail).

52.83 If different levels of materiality have been set for particular areas of the audit, the engagement team should perform separate assessments of the adequacy of the scope of work for each, as well as an overall assessment.

52.84 If the quantitative assessment indicates the actual level of error is above the expected level of error, the engagement team should determine whether this impacts upon the audit.

52.85 As required by paragraph 11 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), the engagement team should determine whether uncorrected misstatements are material, individually or in aggregate.

52.86 If a number of immaterial misstatements are identified within the same class of transactions, account balance or disclosure (COTABD), the engagement team may consider that they need to reassess the risks of material misstatement for that COTABD.

52.87 In assessing the impact of uncorrected misstatements, including prior year misstatements, the engagement team should also consider the effect of the reversal of prior period misstatements which have been corrected.

52.88 In accordance with paragraph 15 of ISA (UK) 450 (Revised June 2016) (Updated May 2022), the engagement team should include in the Apex audit file:

- the amount below which misstatements would be regarded as clearly trivial (in the absence of qualitative factors);
- all misstatements accumulated during the audit and whether they have been corrected;
- all irregular transactions accumulated during the audit and whether they have been regularised; and
- our conclusion as to whether uncorrected misstatements or irregularities are material, individually or in aggregate, and the basis for that conclusion.

52.89 When documenting the accumulation of misstatements, the engagement team should include evaluation of:

- the aggregate effect of uncorrected misstatements; and
- whether the materiality level or levels for particular classes of transactions, account balances or disclosures, if any, have been exceeded.

52.90 Where relevant, the engagement team should document within this the effect of uncorrected misstatements on key ratios or trends, and compliance with legal, regulatory and contractual requirements, such as a requirement to break even over a period of years.

Materiality considerations

52.91 Materiality is usually assessed as part of establishing the overall audit strategy on the basis of estimated results for the year, and corrected misstatements may significantly affect the final results for the year. It may therefore be necessary to revise materiality to reflect the actual financial results.

52.92 If materiality is revised, the engagement team should consider whether performance materiality should be revised and whether any additional audit procedures are required to obtain sufficient assurance. To avoid difficulties from significant changes to materiality at the end of the audit, if information comes to light during the audit suggesting materiality is inappropriate, the engagement team should reassess materiality at that time.

52.93 At any stage during the audit where the engagement team revises either materiality or performance materiality or makes any other changes that may affect the scoping of Financial Reporting Activities (FRAs) and/or Financial Reporting Sub-Activities (FRSAs), they should update the Risk Assessment in Apex to reflect fully these changes. At the conclusion of the audit and prior to certification, they will also need to update the Risk Assessment in Apex to reflect the final values for materiality, performance materiality and the scoping of FRAs and FRSAs.

52.94 If an individual misstatement is judged to be material, it is unlikely that it can be offset by other misstatements. For example, if payroll has been materially overstated, the financial statements as a whole will be materially misstated, even if the effect of the misstatement is completely offset by an equivalent understatement of grant expenditure.

52.95 It may be appropriate to offset misstatements within the same account balance or class of transactions; however, the risk that further undetected misstatements may exist should be considered before concluding that offsetting even immaterial misstatements is appropriate.

52.96 There may be circumstances where engagement teams may conclude that classification misstatements are not material, even if they exceed the assessed materiality figure if qualitative considerations (such as the effect of the classification misstatement on whether there is an Excess Vote, on debt or other contractual covenants, the effect on individual line items or sub-totals, or the effect on key ratios) have been evaluated. For example, a SoFP misclassification may not be

material in the context of the financial statements as a whole when the amount of the misclassification is small in relation to the size of the related SoFP line items, and the misclassification does not affect the SoCNE or any key ratios.

52.97 Some misstatements may be assessed as being material, even if they are lower than the assessed materiality figure, due to the circumstances relating to it. Examples of considerations (which would not necessarily indicate a misstatement is material) include whether a misstatement:

- affects whether there is an Excess Vote;
- affects other regularity considerations;
- affects compliance with regulatory requirements;
- affects compliance with debt covenants or other contractual requirements;
- relates to the incorrect selection or application of an accounting policy that has an immaterial effect on the current period's financial statements but is likely to have a material effect on future periods' financial statements;
- masks a change in expenditure levels or other trends, especially in the context of general economic or other conditions;
- affects ratios used to evaluate the entity's financial position, results of operations or cash flows;
- affects segment information presented in the financial statements;
- has the effect of increasing management compensation, such as by ensuring that the requirements for the award of bonuses or other incentives are satisfied;
- is significant having regard to our understanding of known previous communications to users, e.g. in relation to forecast expenditure;
- relates to items involving particular parties (such as whether external parties to the transaction are related to members of the entity's management);
- is an omission of information not specifically required by the applicable financial reporting framework but which, in our judgment, is important to the users' understanding of the financial position, financial performance or cash flows of the entity; and/or
- affects other information that will be communicated in documents containing the audited financial statements that may be expected to be of interest to users of the financial statements.

52.98 These circumstances are only examples; not all are likely to be present in all audits nor is the list necessarily complete. The existence of any circumstances such as these does not necessarily lead to a conclusion that the misstatement is material. Engagement teams may consult with FAPQ if any of the above examples apply.

Communication of misstatements to those charged with governance

52.99 Corrected material misstatements will usually be communicated, in order to assist those charged with governance in fulfilling their governance responsibilities, in particular with respect to their on-going review of internal control. This would include reporting any non-trivial extrapolated errors identified through sampling.

52.100 Where there are a large number of individual immaterial uncorrected misstatements, the engagement team may consider it to be appropriate to communicate the number and overall monetary effect of the uncorrected misstatements, rather than the details of each individual uncorrected misstatement.

52.101 The engagement team will usually discuss with those charged with governance the reasons for not correcting misstatements. The engagement team may consider it appropriate to request written representations that set out the reasons for not correcting misstatements to help focus the

attention of those charged with governance on those misstatements and the circumstances giving rise to them (see Chapter 57: Reporting to those charged with governance).

Other considerations

52.102 Evaluating the nature and cause of misstatements or irregular transactions is necessary to enable the engagement team to identify whether there are related control deficiencies or other factors which could lead to other misstatements or irregularities occurring. It also enables the engagement team to determine how to respond to these issues in its audit work.

52.103 The evaluation of the impact of misstatements and irregularities, and in particular their qualitative assessment, should be performed by appropriately experienced members of the engagement team who are able to identify and assess the impact that they have upon the financial statements as a whole.

Chapter 53: Submission, signing and printing of annual reports and accounts

Delivery of signed account

53.1 Many of the accounts the NAO audits are subject to a statutory deadline for submission of accounts to the C&AG and subsequent presentation to Parliament. In the case of other accounts, deadline for submission to the C&AG and to Parliament are set out in legislation or the audited entity's accounts direction. In addition, an administrative deadline may be agreed with HM Treasury.

53.2 It is the Engagement Director's responsibility to be aware of the deadlines that apply to their accounts. For all accounts and especially if there is a statutory deadline, they should agree key dates with the audited entity as part of the planning process. This will include dates for the Accounting Officer signature, C&AG certification and the laying and publication of an account.

53.3 The engagement team should agree with the audited entity the date on which the accounts are to be signed by the Accounting Officer. Section 5(7) of the Government Resources and Accounts Act 2000 requires the Accounting Officer to ensure that signed accounts are sent to the C&AG, and signing the accounts demonstrates that the Accounting Officer accepts personal responsibility for their proper presentation as prescribed in legislation or by the Treasury.

53.4 The engagement team should review the procedures that the audited entity has in place to ensure that the accounts sent to the C&AG are those that have been signed up to by the Accounting Officer, then confirm that:

- (for accounts submitted physically rather than electronically) the account is a good copy, printed on A4 portrait, white paper and not bound;
- the pages of the account are sequentially numbered; and
- the account has been signed by the Accounting Officer on the Performance Report, Accountability Report and Statement of Financial Position.

53.5 When the signed annual report and account is submitted to the NAO electronically, it should come from the Accounting Officer's email address directly to the C&AG at (C&AG@nao.org.uk) cc'ing in the engagement team. Private Office will accept annual reports and accounts with electronic signatures from Accounting Officers as long as these documents are sent to the C&AG's inbox from the Accounting Officer's email address.

53.6 Where amendments are required to the account after it has been signed by the Accounting Officer, the following options are available:

- manuscript amendments for minor amendments; or
- replacement pages or a new signed version of the accounts for significant amendments.

53.7 All amendments should be requested in a letter signed by the Accounting Officer, or by an appropriate person certifying on the authority of the Accounting Officer confirming that the changes have been approved by the Accounting Officer. All changes should be initialled by the Engagement Director.

53.8 Superseded pages should be struck through and included on the certification journal.

53.9 Where annual reports and accounts are submitted electronically, green pen amendments should be made on the signed PDF. Where replacement pages are required, the redundant pages should be struck through on the PDF with a green marking “superseded”. Replacement pages should be included in a separate document entitled “Replacement page(s) to ARAC” within the documents uploaded on the Certification tab in Apex.

53.10 The engagement team should take appropriate measures to confirm that the account signed by the Accounting Officer is consistent with the final draft account agreed with the audited entity. This includes checking that all pages of the signed account cast and cross-cast and internal cross-references agree.

Stage of work that must be reached prior to certification

53.11 Before submitting an account for certification, the Engagement Manager and Engagement Director must ensure that:

- all Audit Response Groups have been reviewed;
- all Workflow Steps within Apex, except the Closure Workflow Step, have been reviewed;
- all Consultations have been completed; and
- all Team Tasks (which the exception of Keep in View points) and Engagement Director (and, where relevant, Portfolio Director) review actions have been completed and reviewed.

53.12 In accordance with paragraph 49 of ISA (UK) 700 (Revised November 2019) (Updated May 2022), an account should not be submitted for certification until the Engagement Director is satisfied that sufficient appropriate audit evidence on which to base the auditor’s opinion on the financial statements has been obtained, including evidence that:

- all the statements and disclosures that comprise the financial statements have been prepared; and
- those with the recognised authority (for example, the Accounting Officer or person with appropriate delegated authority) have asserted that they have taken responsibility for the financial statements, including any replacement pages or manuscript amendments made to the signed accounts.

53.13 At the Engagement Director’s discretion, near-finalised draft accounts may be submitted for Private Office pre-certification checks, using the Certification functionality in Apex, at an earlier stage than outlined in the preceding paragraphs.

53.14 Although all procedures must be performed and judgements taken prior to certification, it may be necessary in some circumstances to finalise documentation post-certification. This should be a purely administrative process that does not involve performing new audit procedures. Further guidance may be found in the Chapter 22: Finalise, close and destroy audit file.

53.15 The engagement team should ensure the following information is updated within the Certification tab in the Apex audit file:

- updated audit opinion, providing further narrative in the event of modification of the certificate and report; and
- certification date.

53.16 The engagement team should ensure that key summary documents held within the Apex audit file allow easy knowledge sharing, ensuring also that the file complies with key provisions of the Security Manual and relevant laws and regulations. Summary documents normally include:

- signature brief;
- Audit Completion Report and (where relevant) separate Management Letter; and
- where relevant, documents relating to the C&AG’s report.

Certification steps in Apex

53.17 The Certification functionality in Apex is the method by which engagement teams present the audit certificate, signed accounts and letter of representation to the C&AG for signature. It is also used to record the approval of audit reports where the Signing Authority is a Responsible Individual, in which case the Engagement Director will mark the report as 'certified' when the report is ready for signature. The Certification tab in Apex is a part of the audit file.

53.18 The C&AG uses the Certification functionality in Apex to consider substantial judgements and other issues prior to certifying an accounts.

53.19 The engagement team should complete the Planned Certification Date field, which will feed into central planning of Private Office reviews and the C&AG's diary, and use the Certification functionality in Apex to submit certification documents to Private Office and. in busy periods, set times for certification submissions will be advised by the FA Operations Team in consultation with Private Office.

53.20 ***Table 53A*** below sets out the information which should be uploaded to Apex within the Certification tab as part of a certification submission to the C&AG, or as the Responsible Individual's documentation of the information they have considered before signing the audit report.

Table 53A: Documents to be included in the Certification tab in Apex

Annual report and accounts	**Mandatory:** The Accounting Officer, Chief Executive or other individual with authority to authorise them for issue should send the final annual report and accounts for signature by email to C&AG@nao.org.uk. The engagement team should upload the version for C&AG or Responsible Individual signature (incorporating any manuscript amendments or replacement pages) to the Certification tab in Apex.C&AG@nao.org.uk
Final Audit Completion Report	**Mandatory**
Certification Journals Form	**Mandatory:** This requires details of the account type and planned laying date, along with other publication requirements as applicable.
Confirmation that the Accounting Officer/Chief Executive/other individual with authority to authorise them for issue would still sign the Annual Report and Accounts as at the date of submitting for certification	**Mandatory:** This may be an email from a member of the audited entity's management with appropriate authority to provide this confirmation on behalf of the signatory of the Annual Report and Accounts, or a note of a telephone conversation with such an individual.
Engagement Director's note of any matters they wish to bring to the C&AG's attention	**By exception:** A note of any such matters may be included in the certification submission at the Engagement Director's discretion.
Portfolio Director minute	**For audits where the Engagement Director role has been assigned to a Senior Audit Manager:** This should be prepared using the appropriate template. This confirms the Engagement Director role assignment remains appropriate and that the Portfolio Director has briefly reviewed the annual report and accounts.

Director, Audit Quality minute and FAPQ-reviewed certificate or audit report	**Where the certificate or audit report is modified:** All modified (Emphasis of Matter, Material uncertainty related to going concern, Other Matters, Report, qualification or non-standard) certificates or reports require FAPQ review and a Minute from the Director, Audit Quality.
Shadow certificates	**For contracted-out audits:** Where the audit has been contracted-out, include the firm's audit report to the C&AG within the certification journal.
Letter of amendment and struck through replaced pages	**Where amendments to the annual reports and accounts have been made after signing by the audited entity:** These should be requested as appropriate from the audited entity. More details on this process are provided in the 'Delivery of signed account' section earlier in this Chapter.

53.21 Special arrangements are made for certifying accounts before Parliament's Summer Recess if the C&AG is away from the Office. Engagement teams should familiarise themselves with any instructions issued by Private Office about the procedures that they need to follow in such circumstances.

Laying and publishing

53.22 Presentation to the House of Commons or the Houses of Parliament is referred to as 'laying'.

53.23 ***Consultation required*** Laying can only take place when Parliament is sitting. When the NAO is responsible for laying accounts on the audited entity's behalf and physical documents are laid, five copies are required for laying. These copies are taken by messenger to the Journals Office at the House of Commons and, if necessary, the Printer Paper Office at the House of Lords, with the official NAO request for the accounts to be presented before Parliament. This can only be done on the day of laying. Alternatively, transmission of documents for laying may take place electronically. Where the NAO is responsible for laying accounts on behalf of the audited entity, the engagement team should consult with the Design and Publishing team on the relevant requirements.

53.24 In 2009, the Speaker ruled that printed copies of House of Commons and Command Papers must be made available in the Votes Office on the laying date. Consequently, the version of the accounts that is laid will ideally be the final, printed version of the document. However, proof copies will be acceptable provided the text and pagination is identical to the final published version, and they do not contain manuscript amendments. Pictures do not have to be included in proofs, but captions to them must be.

53.25 Design and Publishing can advise on compliance with publication and laying guidance.

53.26 For Departmental Resource Accounts, the original signed account is retained by Design and Publishing to send to HM Treasury. Departments must also send six copies of the account as certified to the Treasury as the basis for laying. The NAO's Design and Publishing team will not provide copies to the Treasury for laying.

53.27 Where the NAO is responsible for laying (for example, for trading funds and some NDPBs), engagement teams should arrange for the body to provide five copies of the account as signed Where the NAO is not responsible for laying (for example, for Supply financed Executive Agencies and some NDPBs), the bodies should consult their parent department's Parliamentary Clerk about the number of copies required. Where an electronic signed account has been provided for certification, the audited entity does not need to provide any further copies, even in the circumstances where the NAO is responsible for laying.

53.28 When the C&AG has certified an account, but before the account is published, the account must be presented to the relevant addressee(s). Audit certificates are addressed to the person or persons specified by statute or by the terms of engagement, usually to the House of Commons or the Houses of Parliament. Where a certificate is addressed to the House of Commons or the Houses of Parliament, delivery to the addressee is achieved through laying the accounts before the House(s).

53.29 Documents to be laid must conform to a prescribed format, details of which are available on the House of Commons website. The Journal Office will reject accounts not in the prescribed form:

- documents must be A4 portrait;
- the font size must be no smaller than 8 point;
- documents should have a cover and a title page;
- documents should be saddle stitched or perfect bound (not spiral bound) unless transmitted to the Journal Office electronically, in which case this requirement does not apply;
- covers must state the full title of the body and the accounting year;
- there must be no text on the inside cover; and
- the document must have a stand-alone title page which must only contain the full title of the body and the accounting year, the legislation under which the accounts are being laid, a statement that it is, 'ordered by the House of Commons to be printed (date)'; the working 'LONDON: The Stationary Office'; and the HC number.

53.30 Section 88 of the Scotland Act 1998 requires any reports on cross-border bodies that are required to be laid before either or both Houses of Parliament to be laid also before the Scottish Parliament. The engagement team should establish whether a body on which they plan to issue a report is designated as cross-border (see Chapter 59: Reporting to the devolved legislatures and in other UK languages).

Printing and publication by the NAO

53.31 Chapter 22: Finalise, close and destroy audit file includes details of the process where the NAO is responsible for laying and publishing annual reports and accounts.

C&AG's reports on accounts

53.32 Where the C&AG issues a report on the account, the proofs of the report are often dealt with separately from the related account/s, and then merged together before they are cleared for press. The Engagement Manager will therefore have to sign off the proof of the Report separately to confirm that it has been finalised for printing, where the NAO are responsible for laying the accounts.

53.33 Because all accounts with a C&AG's Report must have an agreed publication date and be cleared with the Press Office, Design and Publishing (where applicable), departments and the audited entity, the Engagement Manager should ensure that all these parties are kept informed on the progress of the reports.

53.34 Most reports on accounts require a press notice. The Press Office draft press notices in liaison with the engagement team. The engagement team should inform the Press Office at an early stage of any forthcoming reports on an account.

53.35 The engagement team should clear the draft press note for factual accuracy and presentation with the audited entity alongside the report.

53.36 The engagement team should agree and e-mail the final notice to the Press Office at least three working days before the official publication of the account and report.

53.37 The engagement team should inform the Press Office if audited entities intend to issue their own press notice and ensure that the NAO is given the opportunity to see and comment of the audited entity's draft press notice.

Delegation of signature

53.38 For audits other than those where the C&AG is appointed as the named auditor in primary or secondary legislation, the C&AG may delegate authority to sign the audit certificate. In all such cases, however, a specific delegation from the C&AG is required naming the individual Engagement Director, following the process set out in Chapter 12: Roles, delegations and licences.

53.39 As the C&AG remains ultimately responsible for the audit, the Engagement Director should sign "for and on behalf of the Comptroller and Auditor General", clearly indicating the identity of the signatory.

53.40 Delegation of signing is always subject to the following conditions:

- Where the Engagement Director concludes that a clear audit opinion can be given, with no additional Report of the C&AG, he signs on behalf of C&AG .
- The C&AG will sign any qualified audit certificate.
- The C&AG will sign any substantive critical or major narrative report. In such circumstances the C&AG should also sign the audit certificate.
- The Engagement Director cannot further delegate the signing of an audit certificate to other engagement team members. In the absence of the Engagement Director, the report should be signed by the C&AG.

53.41 In the case of the accounts of profit-making companies audited under the Companies Act 2006, the C&AG may provide Engagement Directors for Companies Act audits with a standing delegation to sign the audit report as Senior Statutory Auditor, for and on behalf of the C&AG. Where the C&AG has a statutory responsibility to sign, then the audit report should be signed by the C&AG personally.

Joint audit reports

53.42 As described in paragraph A64-17 of ISA (UK) 700 (Revised November 2019) (Updated May 2022), in the rare circumstances, where the C&AG has been appointed as a joint auditor or in a two-tier arrangement, both the C&AG and other joint auditor are required to sign the auditors' report in accordance with the requirements of Section 503(4) of the Companies Act 2006.

53.43 As described in paragraph A31-1 of ISA (UK) 700 (Revised November 2019) (Updated May 2022), where an entity appoints joint auditors, each firm is required to agree on the results of the audit and submit a joint auditor's report and opinion. In the case of disagreement, both the C&AG and the firm concerned are required to submit the auditor's opinion in a separate paragraph of the auditor's report and state the reason for the disagreement.

Chapter 54: Overall conclusions and preparing the certificate or report

Relevant standards and guidance

54.1 Paragraphs 25 to 27 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks* and the related application guidance include requirements for the auditor to evaluate the sufficiency and appropriateness of audit evidence.

54.2 Paragraphs 21 to 23 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern* and the related application guidance set out the implications for the auditor's report where the use of the going concern basis of accounting is appropriate and include requirements about communication in the auditor's report relating to going concern. Further guidance may be found in Chapter 27: Going concern.

54.3 Paragraphs 1-142 to 1-181 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 570 (Revised September 2019) (Updated May 2022) in the public sector.

54.4 ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* deals with the auditor's responsibility to form an opinion on the financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

54.5 Paragraphs 1-203 to 1-216 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) in the public sector.

54.6 ISA (UK) 701 (Revised November 2019) (Updated May 2022) *Communicating key audit matters in the independent auditor's report* deals with the auditor's responsibility to communicate key audit matters in the auditor's report. It is intended to address both the auditor's judgment as to what to communicate in the auditor's report and the form and content of such communication.

54.7 Paragraphs 1-217 to 1-218 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 701 (Revised November 2019) (Updated May 2022) in the public sector.

54.8 Paragraphs 10 to 19 of ISA (UK) 710 *Comparative information – corresponding figures and comparative financial statements* includes requirements relating to the implications for the auditor's report of matters relating to comparative information, including a modified opinion in the prior period, prior period misstatements, and where the prior period financial statements were not audited or were audited by a predecessor auditor.

54.9 Paragraphs 21 to 22-1 and 23 to 24 of ISA (UK) 720 (Revised November 2019) (Updated May 2022) *The auditor's responsibilities relating to Other Information* and the related application guidance include requirements about communication in the auditor's report relating to Other Information. Further guidance may be found in Chapter 32: Other information and other reporting responsibilities.

54.10 Paragraphs 2-83 to 2-87 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on the regularity opinion where one is included in the auditor's report.

54.11 Paragraphs 2-88 to 2-91 of Practice Note 10 (Revised 2022) provide guidance on other reporting on regularity.

Concluding on the results of the audit

54.12 In concluding on the results of the audit, the engagement team is required to perform certain procedures which allow them to form an audit opinion. These are listed below and detailed in the indicated paragraphs of the standards, along with the related application guidance; they are also discussed further in the relevant sections below:

- evaluating the sufficiency and appropriateness of the audit evidence (paragraphs 25 to 27 of ISA (UK) 330 (Revised July 2017) (Updated May 2022) *The auditor's responses to assessed risks*);
- considering any inconsistency in, or doubts over, the reliability of evidence (paragraph 11 of ISA (UK) 500 (Updated May 2022) *Audit evidence*);
- performing concluding analytical procedures (paragraph 6 of ISA (UK) 520 (Updated May 2022) *Analytical procedures*);
- completing an overall review of financial statements;
- reconsidering the risk arising from fraud (paragraphs 33-1 to 37 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements*); and
- determining whether relevant ethical requirements, including those related to independence, have been fulfilled (paragraph 21 of ISA (UK) 220 (Revised July 2021) *Quality management for an audit of financial statements*).

Evaluating the sufficiency and appropriateness of the audit evidence

54.13 The engagement team's judgement as to what constitutes sufficient appropriate audit evidence is influenced by such factors as:

- the significance of the potential misstatement and the likelihood of its having a material effect, individually or aggregated with other potential misstatements, on the financial statements;
- the effectiveness of management's responses and controls to address the risks;
- experience gained during previous audits with respect to similar potential misstatements;
- the results of audit procedures performed, including whether such audit procedures identified specific instances of fraud or error;
- the source and reliability of the available information;
- persuasiveness of the audit evidence; and
- understanding of the entity and its environment, including the entity's internal control.

54.14 ***Consultation required*** The Engagement Director, in consultation with the Engagement Manager, should review and assess the audit evidence obtained during the course of the audit and conclude whether this provides a suitable basis for the audit opinion. This can be facilitated by on-going dialogue within the engagement team during the course of the audit and the use of on-site or peer review. Further guidance on considering the sufficiency and appropriateness of audit evidence obtained is provided in Chapter 52: Evaluating the results of procedures, including identified misstatements and irregular transactions. In accordance with paragraph 27 of ISA (UK) 330 (Revised July 2017) (Updated May 2022), if the engagement team has not obtained sufficient appropriate audit evidence related to a relevant assertion about a class of transactions, account balance or disclosure, the engagement team should attempt to obtain further audit evidence. If the

engagement team is unable to obtain sufficient appropriate audit evidence, they should consult FAPQ, as they will be required to express a qualified opinion or disclaim an opinion on the financial statements.

Considering any inconsistency in, or doubts over, the reliability of evidence

54.15 Obtaining audit evidence from different sources or of a different nature may indicate that an individual item of audit evidence is not reliable, such as when audit evidence obtained from one source is inconsistent with that obtained from another. This may be the case when, for example, responses to inquiries of management, internal audit, and others are inconsistent, or when responses to inquiries of those charged with governance made to corroborate the responses to inquiries of management are inconsistent with the response by management.

54.16 Forming an opinion where there is conflicting audit evidence requires careful audit judgement and in such circumstances the Engagement Director may seek advice from FAPQ or an EQR, where applicable.

54.17 ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* includes a specific documentation requirement if information has been identified that is inconsistent with our final conclusion regarding a significant matter, and the consideration of these issues, including any consultation, should be documented accordingly.

Performing concluding analytical procedures

54.18 Concluding analytical procedures are intended to corroborate conclusions formed during the audit of individual components or elements of the financial statements. This enables teams to draw reasonable conclusions on which to base the audit opinion.

54.19 The analytical procedures performed may be similar to those used for preliminary analytical procedures as a part of risk assessment procedures but will reflect the final financial statement position. Considerations when carrying out such procedures may include:

- whether the financial statements adequately reflect the information and explanations previously obtained and conclusions previously reached during the course of the audit;
- whether the procedures reveal any new factors which may affect the presentation of, or disclosures in, the financial statements;
- whether analytical procedures applied when completing the audit, such as comparing the information in the financial statements with other pertinent data, produce results which assist in arriving at the overall conclusion as to whether the financial statements as a whole are consistent with our knowledge of the entity's business;
- whether the presentation adopted in the financial statements may have been unduly influenced by the desire of those charged with governance to present matters in a favourable or unfavourable light; and
- the potential impact on the financial statements of the aggregate of uncorrected misstatements (including those arising from bias in making accounting estimates) identified during the course of the audit and the preceding period's audit, if any.

Completing an overall review of the financial statements

54.20 To the extent that they have not already done so in evaluating presentation and disclosures, and performing concluding analytical procedures, the Engagement Director and Engagement Manager perform an overall review of the financial statements.

54.21 The purpose of this review is to determine whether:

- the financial statements have been prepared using the most appropriate accounting policies and that such policies have been consistently applied;
- the results shown in the financial statements are consistent with our knowledge of the business;
- all necessary disclosures are contained in the financial statements and are appropriately presented and clearly expressed; and
- the uncorrected misstatements and disclosure deficiencies are immaterial to the financial statements.

Reconsidering the risk arising from fraud

54.22 ISA (UK) 240 (Revised May 2021) (Updated May 2022) sets out detailed requirements on the auditor's responsibility to consider fraud at all stages during the course of the audit.

54.23 If the engagement team identifies the possible existence of fraud and consider that this fraud could have a material impact on the financial statements, they must undertake additional testing in order to confirm or dispel the suspicion of fraud. If the additional testing undertaken does not confirm or dispel our suspicions, the engagement team should discuss the issue with the entity's management and consider whether the potential fraud has been properly considered or corrected in the financial statements.

54.24 ***Consultation required*** If senior management are involved in the fraudulent activity, the engagement team should consult with the Money Laundering and Reporting Officer and consider whether a report should be made to the police and/or audit committee. The engagement team should be mindful of the risk of tipping off. Where the engagement team confirms that the financial statements are materially misstated as a result of fraud, or is unable to confirm otherwise, the Engagement Director should consider the implications for the audit opinion, in particular the audit opinion on regularity. Further guidance is provided in Chapter 30: Fraud responsibilities.

54.25 The engagement team cannot assume that an instance of fraud or error is an isolated occurrence. Therefore, the consideration of how the detection of a misstatement affects the assessed risks of material misstatement is important in determining whether the assessment remains appropriate.

54.26 Where the engagement team identifies a misstatement, paragraph 35 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) requires them to obtain an understanding of how the misstatement arose and evaluate whether such a misstatement is indicative of fraud. If there is such an indication, the engagement team should revisit the Engagement Team Discussion on Risk and Fraud and, as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan to reflect any additional risks of material misstatement or risks of material irregular transactions. Further guidance may be found in Chapter 30: Fraud responsibilities.

Determining whether relevant ethical requirements, including those related to independence, have been fulfilled

54.27 The Engagement Director considers the independence and objectivity of the engagement team at the planning stage of the audit. This assessment is documented in the Engagement Risk Assessment Audit Form.

54.28 In addition, the Engagement Director must also consider any independence or ethical issues which arise during the audit and evaluate the impact of any identified breaches of the Office's policies and procedures to determine whether any such breaches represent a threat to the independence and objectivity of the C&AG.

54.29 To demonstrate that this has been done, the Engagement Director should review the Engagement Risk Assessment Audit Form that was completed during the planning process, assess whether the assessment remains valid and record the result in the Apex audit file at the concluding and reporting stage.

Revisiting the risk assessment and response planning

54.30 An audit of financial statements is a cumulative and iterative process. As the engagement team performs the planned audit procedures, the audit evidence obtained may cause them to modify the nature, timing or extent of other planned audit procedures. Information may come to the engagement team's attention that differs significantly from the information on which the risk assessment was based. For example:

- the extent of misstatements detected by performing substantive procedures may alter the engagement team's judgement about the risk assessments and may indicate a significant deficiency in internal control;
- the engagement team may become aware of discrepancies in accounting records, or conflicting or missing evidence; and/or
- concluding analytical procedures may indicate a previously unrecognised risk of material misstatement.

54.31 In such circumstances, the engagement team should, as appropriate, revisit and revise the risk assessment and response plan set out in the Risk Assessment in Apex and the Regularity Testing Plan to ensure it reflects all relevant considerations of which the engagement team is aware as at the conclusion of the audit, including:

- where the engagement team determines it appropriate to revise planned audit procedures;
- any new risks of material misstatement;
- any changes to Inherent Risk Factors (IRFs); and
- any new IRFs.

54.32 Chapter 19: Continuous risk assessment contains further guidance on revising the engagement team's risk assessment.

Quality assurance processes during completion

54.33 At the end of the audit, when work is finished, the Engagement Manager, Engagement Director and (where applicable) the EQR should have reviewed the file and ensured that all issues have been resolved prior to finalising the audit opinion.

54.34 Other than assembling the certification file, the engagement team should not commence the completion process until all levels of review have taken place.

54.35 Each year, FAPQ announces the engagements that have been nominated for a pre-certification technical review of accounts ("accounts review"). Accounts will be selected for review by the Director, Audit Quality, taking into consideration client profile, risk and the nature of the account (for example, whether it is a resource account).

54.36 Where applicable, the engagement team should notify FAPQ in advance when the accounts are expected to be available for review and submit financial statements for a pre-certification technical review only once the following procedures have been completed:

- an initial reconciliation of the financial statements to the audited figures;
- a review of the financial statements against the relevant disclosure guide checklist
- [for resource accounts only] completion of the Resource Accounts Consistency Checklist;
- Engagement Manager, Engagement Director and (where applicable) EQR review of the annual report and accounts.

54.37 If issues are identified in the accounts, the engagement team should use judgement to determine whether they are in an appropriate state for pre-certification review. In general:

- if a number of significant disclosures have not yet been drafted, the accounts are unlikely to be suitable to be submitted for review; but
- minor issues around casting, internal consistency, or support within the audit files should be clearly flagged but do not prevent review.

54.38 Pre-certification technical reviews focus on the adequacy of disclosure of significant issues and judgements.

54.39 ***Consultation required*** The engagement team should submit financial statements for review on a timetable that will enable resolution of issues before the audited entity finalises the financial statements. If, in exceptional circumstances, this is not possible, the engagement team should agree an alternative approach with FAPQ.

54.40 Pre-certification reviews of particular accounts arranged by FA Compass are discussed in Chapter 4: Quality monitoring.

54.41 Requirements for FAPQ review of modified audit certificates and reports are discussed in Chapter 55: Modified certificates and reports. Certificates and reports with unusual circumstances not covered by the guidance within this Manual may also be submitted to FAPQ for review. The engagement team should submit draft certificates to FAPQ as soon as practical, which may be prior to finishing audit work.

54.42 If the engagement team has not issued an audit certificate on the prior year audit, then an audit certificate should not be issued on the current year audit until the audit certificate in relation to the prior year has been issued.

Forming an audit opinion

54.43 Paragraphs 10 to 15 of ISA (UK) 700 (Revised November 2019) (Updated May 2022) and the related application guidance set out how the engagement team should form an opinion on the financial statements.

54.44 Paragraphs 2-83 to 2-87 of Practice Note 10 (Revised 2022) set out how the engagement team should form an opinion on regularity. This should be in the form of a clear written expression, based on the engagement team evaluating the conclusions drawn from the audit evidence obtained, as to whether, in all material respects, the resources have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

54.45 In forming a judgment on the regularity opinion, the engagement team should conclude on whether in all material respects, the transactions presented in the financial statements have been

made in accordance with authorising legislation, regulations issued under governing legislation, Parliamentary authorities and Treasury and related authorities.

54.46 The findings of the audit should be considered in the context of the materiality for the audit not merely in terms of materiality by value, but also in terms of qualitative aspects of materiality. When evaluating audit differences, the engagement team should consider:

- the significance to the readers of the account of the uncorrected difference to the financial statement either for individual line items or the financial statements as a whole;
- the likelihood that the undetected misstatements (when considered with uncorrected misstatements) may exceed materiality by value;
- the cause of the misstatement; for example, has it arisen as a result of fraudulent activity; and
- whether the identified misstatement may indicate a pattern of activity (in such circumstances, the engagement team should consider and document whether it is necessary to undertake additional audit procedures to identify whether other similar audit differences exist).

54.47 ***Consultation required*** It is necessary to exercise a high degree of professional judgment in determining the audit opinion. The engagement team should consult with FAPQ when considering a modified audit opinion or including an Emphasis of Matter paragraph.

54.48 The process of forming an audit opinion brings together all the judgements taken across the audit to support the conclusions communicated through the auditor's report. Irrespective of the quality of the underlying work, there is a risk to the audit opinion presented through:

- not aggregating the results of the audit work appropriately;
- not identifying gaps in the audit assurances obtained; or
- making incorrect judgements on difficult issues.

54.49 For more complex audits, the process of drawing together the results of the work will be more involved and there are likely to be more difficult issues of judgement to consider. Early planning by the engagement team of how to address the risks inherent in concluding and reporting will help to mitigate the risks to the opinion. Appropriate mitigations may include:

- designing procedures and assigning responsibilities at the planning stage for drawing together the results of the audit;
- assigning work where there are synergies between different audit areas and such that the staff with the greatest audited entity knowledge are responsible for those procedures which require it;
- regular meetings with the audited entity to discuss emerging issues;
- early involvement of the Engagement Director in the concluding and reporting procedures;
- timely involvement of the EQR in key judgements (see Chapter 7: Engagement Quality Review); and
- planning early consultation with FAPQ on technical matters (see Chapter 6: Technical support and consultation).

Consistency opinion

54.50 The engagement team's responsibilities extend to the other information disclosed in the annual report and accounts, which they are not required to audit, but for which they are required to consider the consistency with the accounts and with their knowledge of the business. Further details of the engagement team's responsibility in relation to the other information presented with the accounts are given in Chapter 32: Other information and other reporting responsibilities.

54.51 Section 496 of the Companies Act 2006 sets out a requirement for the auditor to report on the consistency of the Strategic Report and Directors' Report. The auditor must state in their report

on the company's annual accounts whether in their opinion the information given in the Strategic Report and Directors' Report for the financial year for which the accounts are prepared is consistent with those accounts.

54.52 For audited entities that prepare their accounts in accordance with the FReM, the Companies Act requirements are applied by analogy. The Director's Report is interpreted to include the Accountability Report and the Performance Report.

54.53 The engagement team's responsibilities in respect of Director's Report information are set out in ISA (UK) 720 (Revised November 2019) (Updated May 2022). This ISA (UK) sets out responsibilities in respect of all the other information which is included in a document containing audited financial statements. The responsibilities are the same, whether the information is explicitly covered by our consistency opinion or not.

54.54 Paragraphs 14 to 15 of ISA (UK) 720 (Revised November 2019) (Updated May 2022) and the related application guidance include requirements for the auditor to read and consider the other information.

54.55 The engagement team's responsibilities do not extend to quality control aspects of the other information, for example commenting on drafting or proofreading. They also do not extend to obtaining assurance to support assertions or figures presented in the other information. If, on reading the other information, a material inconsistency is identified, determine whether the audited financial statements or the other information needs to be revised.

54.56 If revision of the audited financial statements is necessary and management refuses to make the revision, the engagement team should modify the opinion on financial statements in accordance with ISA (UK) 705 (Revised June 2016). If the engagement team is of the opinion that the information in the Directors' Report is materially inconsistent with the financial statements, and has been unable to resolve the inconsistency, they should state that opinion and describe the inconsistency in the auditor's report.

54.57 This requirement is met through the "Opinion on other matters" paragraph in the audit certificate or report which states that: *"In my opinion, based on the work undertaken in the course of the audit:* […] *the information given in the* [sections of the Annual Report on which the auditor provides a positive consistency opinion; for example, the Performance Report and Accountability Report] *for the financial year for which the financial statements are prepared is consistent with the financial statements."*

54.58 In accordance with paragraph 18 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), if revision of the other information is necessary and management refuses to make the revision, the engagement team should:

- communicate this matter to those charged with governance, unless all of them are involved in managing the entity;
- if the other information is still not corrected after this communication, include a description of the material inconsistency in an Other Matter paragraph, or in a substantive C&AG's report, in accordance with ISA (UK) 706 (Revised June 2016); and
- withdraw from the engagement, where withdrawal is possible under applicable law or regulation.

54.59 If, on reading the other information for the purpose of either identifying material inconsistencies or identifying any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by the engagement team in the course of

performing the audit, the team becomes aware of an apparent misstatement of fact, they should discuss the matter with management. Paragraphs 18 to 19 of ISA (UK) 720 (Revised November 2019) (Updated May 2022) explain the process to follow if discussions with management are not sufficient to resolve the identified issues.

54.60 In addition, a specific reference to the Governance Statement is included in the audit certificate, in line with practice in the private sector. The Listing Rules include a requirement for listed companies to ensure their auditor reviews the Governance Statement. For this reason, a specific reference is included within the audit certificate on the scope of that review. This is replicated in the public sector by reporting by exception where the Governance Statement does not reflect compliance with HM Treasury's guidance.

54.61 Whilst the work required to support this statement does not go beyond that required for the negative consistency opinion more generally, the engagement team should consider carefully the consistency, including the completeness, of the Governance Statement with our knowledge of the business.

54.62 The engagement team should consider the nature and severity of the inconsistency or misstatement that exists, and a distinction should be drawn between those issues that are a matter of fact and those issues that are a matter of judgement. It is far more difficult to disagree with a matter of judgement (such as a view on the likely outturn for the following year) than a factual error.

54.63 There may be circumstances in which the engagement team is aware that the expressed view of those charged with governance is significantly at variance with the entity's internal assessment of an issue or is so unreasonable as not to be credible to someone with the engagement team's knowledge. When determining what action should be taken, the engagement team may need to take legal advice, including advice on whether the auditor would be protected by qualified privilege from a defamation claim if they were to refer to the matters in their report or subsequently. All requests for legal advice should be made through the Head of Policy and Legal Advice.

Audit certificates and reports

54.64 The findings of an audit will be reported in with the C&AG's certificate and/or report (or, for Companies Act audits, a report by a Senior Statutory Auditor under a standing delegation from the C&AG) on the relevant financial statements. The nature of the reporting provided on the financial statements is dependent upon the nature of the entity, the basis upon which it prepares its financial statements and the basis upon which the C&AG undertakes the audit.

54.65 Pro-forma audit certificates and reports have been provided for drafting certificates and reports for the audits of the financial statements of the following types of entity/account:

- Arm's length body (not a company)
- Charitable arm's length body (not a company and not registered)
- Charitable company
- Companies Act audit (IFRS or UK GAAP)
- Departmental resource account
- Entity applying FRS 101
- Executive agency
- Extended Auditor Report (company)
- Extended Auditor Report (department)
- GRAA company (IFRS or UK GAAP)

- International body
- Receipts and payments account
- Registered charity
- Pension scheme resource account
- Trading fund
- Trust Statement

54.66 These pro-formas should be used as the basis for drafting all unmodified audit certificates or reports. Where engagement teams are uncertain of which pro-forma to use or there is an entity where these pro-formas are not appropriate, they may consult with FAPQ.

54.67 ***Table 54A*** below provides guidance on the key titles and references which should be used within each pro-forma depending on the circumstances of the entity.

54.68 ***Consultation required*** The guidance in this table reflects typical practice for these types of bodies, but many NAO-audited entities have unusual legislative setups. The engagement team should ensure they are always clear on the basis of preparation and basis for the audit for their audited entity and should check this specifically back to the entity's legislative requirements as part of setting up the audit and while drafting the audit certificate or report. If the engagement team encounters difficulties determining the audited entity's authorising legislation and/or financial reporting framework, or either of these are ambiguous, they should consult FAPQ.

Table 54A: Details to include in pro-forma template audit certificates and reports

Template	Certificate/ Report	Addressee	Legislation	Financial Reporting Framework
Arm's length body (not a company)	Certificate and report/ Audit report	The House of Commons/ The Houses of Parliament/ Other addressee as set out in legislation	Authorising legislation for the entity	UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual or United Kingdom Accounting Standards, including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice)
Charitable arm's length body (not a company and not registered)	Certificate and report/ Audit report	The House of Commons/ The Houses of Parliament/ Other addressee as set out in legislation	Authorising legislation for the entity	United Kingdom Accounting Standards, including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice)

Charitable company	Independent auditor's report	Members of [charitable company name]	Applicable law (audit by agreement)	UK-adopted international accounting standards or United Kingdom Accounting Standards, including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice) (UK GAAP would be a relevant framework for a Charitable Company applying the Charities SORP.)
Companies Act audit (IFRS or UK GAAP)	Independent auditor's report	Members/Shareholders of [company name]	Applicable law (audit by agreement)	UK-adopted international accounting standards or United Kingdom Accounting Standards, including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice)
Departmental resource account	Certificate and report	The House of Commons	Government Resources and Accounts Act 2000	UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual
Entity applying FRS 101	Independent auditor's report	Members of [company name]	Applicable law (audit by agreement)	United Kingdom Accounting Standards, including Financial Reporting Standard 101 *Reduced disclosure framework* (United Kingdom Generally Accepted Accounting Practice)
Executive agency	Certificate and report	The House of Commons	Government Resources and Accounts Act 2000	UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual

Extended Auditor Report (company)	Independent auditor's report	Members/Shareholders of [company name]	Applicable law (audit by agreement)	UK-adopted international accounting standards or • United Kingdom Accounting Standards, including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice)
Extended Auditor Report (department)	Certificate and report	The House of Commons	Government Resources and Accounts Act 2000	UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual
GRAA company (IFRS or UK GAAP)	Certificate and report	Members/Shareholders of [company name]	Government Resources and Accounts Act 2000	UK-adopted international accounting standards or United Kingdom Accounting Standards, including Financial Reporting Standard 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice)
International body	Independent auditor's report	As agreed in the terms of the engagement	None: audit by agreement	As applicable (for example, International Public Sector Accounting Standards)
Receipts and payments account	Certificate and report/ Audit report	The House of Commons/ The Houses of Parliament/ Other addressee as set out in legislation	Authorising legislation for the entity	As specified in the accounts direction and/or underlying legislation
Pension scheme resource account	Certificate and report	The House of Commons	Government Resources and Accounts Act 2000	UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual
Trading fund	Certificate and report	The Houses of Parliament	Government Trading Funds Act 1973	UK-adopted international accounting standards as interpreted by HM Treasury's

				Government Financial Reporting Manual
Trust Statement	Certificate and report/ Audit report	The House of Commons/ The Houses of Parliament	Government Resources and Accounts Act 2000/ Government Trading Funds Act 1973/ Exchequer and Audit Departments Act 1921	UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual

54.69 ***Consultation required*** All certificates with modified, qualified, adverse or disclaimed opinions should be submitted to FAPQ for formal approval by the Director, Audit Quality. The minute from the Director, Audit Quality approving such certificates should be included on the Certification Journal submitted to the C&AG.

54.70 ***Consultation required*** Similarly, where a team proposes that an Emphasis of Matter or Other Matter paragraph is included within the audit certificate, then this should be submitted to FAPQ for approval. A minute from the Director, Audit Quality approving such certificates must be included on the Certification Journal submitted to the C&AG.

54.71 It is important that the form and content of audit certificates and audit reports are presented in a uniform fashion, as this promotes the reader's understanding of the certificate/report and highlights unusual circumstances when they occur. The auditor's certificate/report will therefore include the following elements:

- Title
- Addressee
- Scope paragraph identifying the statements to be audited
- Opinion on financial statements
- Opinion in respect of an additional financial reporting framework
- Opinion on regularity (where applicable)
- Basis for opinion[s]
- Conclusions relating to going concern
- Other Information
- Opinion on Other Matters
- Matters on which [the C&AG] report[s] by exception
- Responsibilities of [management/those charged with governance/the Directors/the Board/the Accounting Officer] for the financial statements
- Auditor's responsibilities for the audit of financial statements
- Explanation of the extent to which the audit was considered capable of detecting irregularities, including fraud (as required by paragraph 29-1 of ISA (UK) 700 (Revised November 2019) (Updated May 2022)
- Report (where no additional observations are given by the C&AG; an additional C&AG's report would be included after the main certificate/report)
- Auditor's signature
- Auditor's address
- Date of the report

54.72 Further guidance on the contents of the sections of audit certificates and reports is provided in ***Table 54B*** below.

Table 54B: Sections of audit certificates or reports and their contents

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
Title	21 A20	The title used for the auditor's report should adopt the wording used in the legislation appointing the C&AG as auditor. Where there is a statutory requirement for his examination to be certified, an audit report containing the opinion of the C&AG on financial statements is entitled 'Audit Certificate'. Use of the word 'certificate' clearly differentiates the audit report from any other report of the C&AG. Where the C&AG undertakes the audit by statutory appointment, the terms of the statute may require him to examine, certify and report on the financial statements. Where a separate substantive report is not required, the report will be included within the body of the audit certificate. In such cases, the document will be entitled 'The Certificate and Report of the Comptroller and Auditor General'. Where the C&AG is the appointed auditor in legislation (or under circumstances equivalent to legislation such as by International Treaty) but there is no statutory requirement to "certify", the title of the audit report should be "Audit report of the Comptroller and Auditor General to *[addressee of audit report]*." For audits performed by agreement, the title used for the auditor's report should be the "Independent Auditor's Report".
Addressee	22 A21 to A21-1	The certificate should be appropriately addressed as required by the circumstances of the engagement and any local regulations. The addressee would normally be the person on whose behalf the audit was undertaken. For central government entities, the audit is usually undertaken on behalf of Parliament or the House of Commons (as dictated by governing legislation, such as the GRAA 2000). The legislation appointing the C&AG should be consulted to determine the appropriate addressee(s), based on where the financial statements will be laid. The exceptions to this are where: • legislation requires the appointment of the auditor and specifies the person or persons to whom the auditor shall report. For example, for some non-departmental public bodies the governing legislation requires the auditor to report to the relevant Secretary of State; or • the audited financial statements are not required to be laid before Parliament. In such cases it is necessary to consider on whose behalf the audit is being

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		undertaken. Although this is normally the person, or persons, making the appointment, the engagement team may need to look behind this. For example, HM Treasury may appoint the auditor on behalf of a Secretary of State. This would need to be reflected in the Letter of Understanding or Letter of Engagement.
Scope paragraph identifying the statements to be audited	24	The auditor's report should identify the financial statements of the entity that have been audited, including the date of, and period covered by, the financial statements. It should also refer to the notes to the financial statements. This section should specify that the financial reporting framework that has been applied in their preparation is applicable law and one of the following, as appropriate: • UK-adopted international accounting standards as interpreted by HM Treasury's Government Financial Reporting Manual; • UK-adopted international accounting standards; • United Kingdom Accounting Standards, including *Financial Reporting Standard 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland* (United Kingdom Generally Accepted Accounting Practice); or • United Kingdom Accounting Standards, including *Financial Reporting Standard 101 Reduced disclosure framework* (United Kingdom Generally Accepted Accounting Practice).
Opinion on financial statements	23 to 27 A22 to A31-1	The opinion paragraph of the auditor's report should clearly state the auditor's opinion as required by the relevant financial reporting framework used to prepare the financial statements, including applicable law. In central government, these requirements are usually set out in an accounts direction issued by HM Treasury, or in guidance provided in the Government Financial Reporting Manual (FReM). Where such an accounts direction refers to primary statements required by the Companies Acts and the further primary statements required by accounting standards, the engagement team must refer to all such statements when expressing the audit opinion. However, where the audit opinion states that the financial statements have been prepared in accordance with a particular financial reporting framework, this does not represent a restriction on the scope of the opinion but instead clarifies the context in which it is expressed. Across the public sector, most financial statements include an opinion as to whether the financial statements give a true and fair view.

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		Consultation required However, there are instances where the auditing framework requires an opinion as to whether the financial statements present fairly or properly present the entity's transactions or balances. Whichever wording is used for the opinion on the financial statements, this will not have an impact on the extent to which the engagement team observes the requirements of auditing standards. For engagements which fall outside the scope of the ISAs, FAPQ guidance must be sought prior to submitting a proposal to accept the engagement. For audits undertaken under the Companies Act 2006, the audit opinion should state clearly the matters listed in paragraph A24-1 of ISA (UK) 700 (Revised November 2019) (Updated May 2022). The above reporting requirements will also apply to audits undertaken under the Government Resources and Accounts Act 2000 or where the entity prepares their financial statements in accordance with the FReM.
Opinion in respect of an additional financial reporting framework	A13-A15	When the C&AG is engaged to issue an opinion on the compliance of the financial statements with an additional financial reporting framework, the second opinion should be clearly separated from the first opinion on the financial statements, by use of an appropriate heading. The C&AG may only provide an opinion regarding compliance of financial statements with two separate financial reporting frameworks in a single audit report where the engagement team is satisfied that there are no differences between the two financial reporting frameworks which affect the financial statements which are being reported on.
Opinion on regularity (where applicable)	43	The opinion on regularity is given in accordance with the guidance on reporting on regularity provided in paragraphs 2-83 to 2-87 of Practice Note 10 (Revised 2022) and the requirements of applicable legislation. In the public sector there is often an explicit statutory requirement to express an opinion on regularity in the audit certificate. The concept of regularity addresses Parliament's concern to ensure that public money is only used for the purposes intended by Parliament. Regularity is reported on as a separate audit opinion, and a separate report will normally be made to Parliament on a regularity issue which results in a qualification. For financial

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		statements prepared on an accruals basis, the regularity opinion will be expressed as follows: *"In my opinion, in all material respects:* • [for departmental resource accounts only]][*the Statement of Outturn against Parliamentary Supply properly presents the outturn against voted Parliamentary control totals for the year ended* [reporting date] *and shows that those totals have not been exceeded; and* • *the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament and the financial transactions recorded in the financial statements conform to the authorities which govern them."* When determining the authorities that are within the scope of the auditor's regularity opinion, engagement teams should refer to Chapter 11: Determining the framework of authorities. For financial statements prepared on a cash basis, the regularity opinion will be expressed as follows: *"In all material respects the payments (expenditure) and receipts have been applied to the purposes intended by Parliament and conform to the authorities which govern them".* Whether the word "payments" or "expenditure" is used is dependent upon the statute or other authority that requires a regularity opinion to be given.
Basis for opinion[s]	28 A32 to A39	The certificate or report should include the following statement: *I conducted my audit in accordance with International Standards on Auditing (ISAs) (UK), applicable law and* [for all audits where it is applied – i.e. all except Companies Act audits: *Practice Note 10 'Audit of financial statements and regularity of public sector bodies in the United Kingdom'*] [for charity audits: *Practice Note 11 'The audit of charities in the United Kingdom'*]. *My responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of my [certificate/report].* *Those standards require me and my staff to comply with the Financial Reporting Council's Revised Ethical Standard 2019.* [For Public Interest Entities or listed entities; otherwise, omit this sentence: *I have also elected to apply the ethical standards relevant to* [as appropriate, *"public interest entities"* or *"listed entities"*].] *I am independent of* [audited entity] *in accordance with the ethical requirements*

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		that are relevant to my audit of the financial statements in the UK. My staff and I have fulfilled our other ethical responsibilities in accordance with these requirements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. Where there is a statutory requirement for the C&AG to "examine, certify and report", the responsibility of the C&AG in this paragraph of the certificate will be described as *"audit, certify and report on the financial statements"*. Otherwise, the description of the C&AG's responsibilities will be *"audit and express an opinion on the financial statements"*. Where the C&AG is appointed by legislation to audit an entity which is not a company, the applicable legal requirements are contained in the appointing legislation. Therefore, the responsibility of the C&AG will be described as being in accordance with the relevant Act, rather than *"applicable legal requirements and International Standards on Auditing (UK)"*. Where there is no statutory basis for the audit, the equivalent sentence will end after *"on the financial statements"*. For non-company audits, the C&AG chooses to audit in accordance with International Standards on Auditing, so this section will state that *"I conducted my audit in accordance with International Standards on Auditing (UK)."* There are exceptions for international audits, where the relevant standards are those issued by the IAASB. Engagement teams should note in preparing the basis for opinion[s] that paragraph 20 of ISA (UK) 200 (Revised June 2016) (Updated May 2022) *Overall objectives of the independent auditor and the conduct of an audit in accordance with International Standards on Auditing (UK)* requires that the auditor shall not represent compliance with ISAs (UK) in the auditor's report unless the auditor has complied with the requirements of and all other ISAs (UK) relevant to the audit.
Conclusions relating to going concern	29	Where the engagement team has followed the "continued provision of service approach" to going concern described in paragraphs 1-153 to 1-164 of Practice Note 10 (Revised 2022), this section should include the following statement: *The going concern basis of accounting for* [audited entity] *is adopted in consideration of the requirements set out in* [financial reporting framework]*, which require entities to adopt the going concern basis of accounting in the preparation of the financial statements where it anticipated that the services which they provide will continue into the future.*

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
Other Information	32	Audit reports issued by the C&AG should include (as required by paragraphs 21 to 22-1 of ISA (UK) 720 (Revised November 2019) (Updated May 2022)), a description of the responsibilities of both management and the auditor for the Other Information published alongside the financial statements as follows: *"The other information comprises information included in the* [annual report], *but does not include the parts of the* [Accountability Report/Remuneration Report] *described in that report as having been audited, the financial statements and my auditor's* [certificate/report] *thereon. The* [the Directors/Board/Trustees] [and the Accounting Officer] [is/are] *responsible for the other information. My opinion on the financial statements does not cover the other information and except to the extent otherwise explicitly stated in my* [certificate/report], *I do not express any form of assurance conclusion thereon. In connection with my audit of the financial statements, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit or otherwise appears to be materially misstated. If I identify such material inconsistencies or apparent material misstatements, I am required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact.* [I have nothing to report in this regard.]" The Other Information section of the audit report/certificate should also identify the other information that has been read by the auditor (in accordance with ISA (UK) 720 (Revised November 2019) (Updated May 2022)) to identify material inconsistencies with the financial statements or information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired in the course of the audit. This should describe all the information expected to be published in the same document as the financial statements and the audit report. Where the term "annual report" is not an accurate description of this information, the titles of the individual sections will need to be specified. Where entities prepare Statutory Other Information, the C&AG's report should state whether based upon the work undertaken in the course of the audit, the Statutory Other Information for the financial year for which the accounts are prepared is consistent with those

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		accounts and has been prepared in accordance with the applicable legal requirements. Where the C&AG is required to report on the statutory other information in accordance with law or regulation, the engagement team should, in accordance with paragraph 22-1 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), include in the auditor's report: • a description of the auditor's responsibilities relating to the statutory other information; and • a conclusion thereon. ***Consultation required*** Where the engagement team has identified a material uncorrected misstatement in the Other Information in relation to these matters, a statement that describes the uncorrected material misstatement of the other information should be included within the Other Information section of the audit report. The engagement team must consult with FAPQ where they identify any such matters which may be required to be reported on. ***Consultation required*** Where the engagement team has identified anything material to add or draw attention to in respect of these elements of the Other Information, the Other Information section of the auditor's report should include a statement that describes any other material information that the engagement team considers it appropriate to add or draw attention to. The engagement team must consult with FAPQ where they identify anything related to these matters which may be required to be reported on. ***Consultation required*** Where the engagement team proposes a modified opinion on the financial statements, they must consider the implications of this for the opinion to be provided on the Other Information in consultation with FAPQ.
Opinion on Other Matters	43 A58 to A60	When other reporting responsibilities are also addressed within the auditor's report on the financial statements, the opinion arising from such other responsibilities should be set out in a separate section of the auditor's report following the opinion(s) on the financial statements or, where there is one, the opinion on regularity. For central government entities, under the Companies Act 2006, as interpreted for the public sector context by the FReM, the engagement team is required to audit the parts of the Accountability Report specified in paragraph 6.2.1 of the FReM (2021-22 version issued in December 2021) and provide an

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		opinion on whether they have been properly prepared in accordance with the relevant framework. Where there is no requirement to provide an opinion on the remuneration report, an opinion may be provided where it is prepared in accordance with a recognisable framework and included within the agreed terms of engagement. This requirement is met through the "Opinion on other matters" in audit certificate or report which states that: "*the parts of the* [report name; for example, Accountability Report] *to be audited has been properly prepared in accordance with* [insert appropriate authority] *directions made under* [legislation]". As stated in paragraph A60-3 of ISA (UK) 700 (Revised November 2019) (Updated May 2022), Section 498(2) of the Companies Act 2006 also requires the auditor of a quoted company to form an opinion as to whether the auditable part of the company's directors' remuneration report is in agreement with the accounting records and returns. If the engagement team is of the opinion that the auditable part of the report is not in agreement with the accounting records and returns then this fact should be stated in the auditor's report. This also applies to Remuneration and Staff Reports prepared under the FReM. Where the entity has not complied with the requirements of the relevant reporting framework in preparing its Remuneration Report, this should be stated in the auditor's report. Furthermore, as stated in paragraph A60-4 of ISA (UK) 700 (Revised November 2019) (Updated May 2022), Section 498(4) of the Companies Act 2006 requires the auditor to disclose any particulars which have been omitted from the Remuneration Report by management where practicable to do so. This also applies to Remuneration and Staff Reports prepared under the FReM. Only a limited number of disclosures included within the Remuneration and Staff Report and the Parliamentary Accountability Report are subject to audit. The engagement team should, therefore, in accordance with paragraph A60-7 of ISA (UK) 700 (Revised November 2019) (Updated May 2022), make arrangements with management, well in advance of the year-end, to ensure that the audited disclosures will be clearly distinguished from those that have not been audited. Where this does not occur, the auditor's report should clearly distinguish those disclosures which have been subject to audit. Section 496 of the Companies Act 2006 sets out a requirement to report on the consistency of the Strategic Report and

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		Director's Report. For the bodies complying with the FReM, the Director's Report is interpreted to include the Accountability report and the Performance report. This Companies Act requirement is met through the opinion on other matters in the audit certificate which states that: *"the information given in* [list elements as appropriate] *for the financial year for which the financial statements are prepared is consistent with the financial statements"*. The elements referred to in the positive consistency opinion should not include all the information in the annual report or other document to be published. The reference in the positive consistency opinion should always be a subset of the information that is described in the scope paragraph of the audit report (which describes the auditor's responsibility to read all the information to be published with the financial statements, not only the Director's Report). Such information is known as the Statutory Other Information. Further guidance may be found in Chapter 32: Other information and other reporting responsibilities.
Matters on which the auditor reports by exception	43-1	If the C&AG is required to report on certain matters by exception the C&AG's responsibilities should be described under the heading "Matters on which we are required to report by exception" and incorporate a suitable conclusion in respect of such matters. By analogy to the requirements of the Companies Act, the following matters are reported on by exception: • management's use of the going concern basis of accounting in the preparation of the entity's financial statements; • the disclosure in the financial statements of any identified material uncertainties that may cast significant doubt about the entity's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from when the financial statements are authorised for issue; • adequate accounting records have not been kept, or returns adequate for [the C&AG's] audit have not been received from branches not visited by [the C&AG's] staff; • the financial statements are not in agreement with the accounting records or returns; and • all of the information and explanations required for [the C&AG's] audit have not been received. For all audits on which the C&AG's opinion is qualified on the basis of a limitation of scope, engagement teams should consider whether they need to state that they were unable to obtain all the information and explanations necessary for the

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		purposes of the audit and that audit proper accounting records have not been kept. Similarly, where the engagement team identifies a matter on which the C&AG is required to report by exception, they should consider whether this may also give risk to a modification of the C&AG's opinion on the financial statements. For example, if adequate accounting records have not been maintained and as a result it proves impracticable for the engagement team to obtain sufficient appropriate evidence concerning material matters in the financial statements, the auditor's report on the financial statements includes a qualified opinion or disclaimer of opinion arising from that limitation in accordance with ISA (UK) 705 (Revised June 2016). In addition, for entities reporting under the FReM which prepare a Governance Statement, by agreement with HM Treasury, the C&AG reports by exception on whether the Governance Statement does not reflect compliance with Treasury's guidance.
Responsibilities of [management/those charged with governance/the Directors/the Board/the Accounting Officer] for the financial statements	33 to 36	The auditor's report should include a statement that those charged with governance are responsible for the preparation of the financial statements and in accordance with the applicable financial reporting framework, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error and provide a true and fair view. The statement regarding management's responsibility for internal control is not required for auditor's reports prepared for entities who prepare their financial statements in accordance with the FReM. This section of the auditor's report should also state that management are responsible for assessing the entity's ability to continue as a going concern and whether the use of the going concern basis of accounting is appropriate as well as disclosing, if applicable, matters relating to going concern. The explanation of management's responsibility for this assessment shall include a description of when the use of the going concern basis of accounting is appropriate. For central government entities, those charged with governance will usually be the Accounting Officer. Where the audited entity is a body corporate and its Board (or equivalent) has a statutory responsibility to prepare the financial statements, the responsibilities paragraph should refer to the responsibilities of the Board (or equivalent) as well as those of the Accounting Officer.

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
Auditor's responsibilities for the audit of financial statements	37 to 42	Audit reports issued by the C&AG should include the following description of the scope of an audit: *"My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue a* [certificate/report] *that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements."* The option provided in paragraph 41(c) of ISA (UK) 700 (Revised November 2019) (Updated May 2022) to include the description of the auditor's responsibilities for the audit of the financial statements by cross-referring to the applicable version of a "Description of the Auditor's Responsibilities for the Audit of the Financial Statements" that is maintained on the website of an appropriate authority should be exercised by including the following cross-reference: *"A further description of my responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of my* [certificate/report]." Where a regularity opinion is provided, the following paragraph should be included within the description of the scope of an audit: *"In addition, I am required to obtain evidence sufficient to give reasonable assurance that the* [income and expenditure/receipts and payments] *reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them."* Paragraph 28 of ISA (UK) 705 (Revised June 2016) and the related application guidance include requirements to amend the description of the auditor's responsibilities where the auditor disclaims an opinion on the financial statements due to an inability to obtain sufficient appropriate audit evidence. In accordance with paragraph 28 of ISA (UK) 705 (Revised June 2016), in circumstances where the audit opinion is disclaimed, the "Auditor's responsibilities for the audit of the financial statements" section of the auditor's report should be amended to only:

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		• note the auditor's responsibilities to conduct the audit in accordance with the ISAs (UK); • draw attention to the fact that due to the matter in the "Basis for Disclaimer of Opinion" section, the auditor has not been able to obtain sufficient appropriate evidence to provide the basis for an opinion; and • note the auditor's compliance with independence and ethical requirements.
Explanation of the extent to which the audit was considered capable of detecting irregularities, including fraud	29-1 A39-1 to A39-6	The laws and regulations referenced in this section of the certificate or report should be consistent with those whose consideration the engagement team has documented on the audit file. Any specific procedures referenced in this section should be consistent with those the engagement team has documented on the audit file. The section should reflect all procedures the engagement team has performed to address risks of non-compliance with laws and regulations (including procedures in support of the regularity opinion and to address fraud risk). In explaining the extent to which the audit was considered capable of detecting irregularities, including fraud, the engagement team should consider how their approach to the audit has affected the likelihood of detection. This will be affected by the inherent difficulty in detecting them, the effectiveness of the entity's controls, and the nature, timing and extent of the audit procedures performed. Irregularities that result from fraud might be inherently more difficult to detect than irregularities that result from error. The engagement team's responsibilities for the engagement will mean that detection of those types of irregularity which give rise to a risk of material misstatement are those on which the auditor is able to provide the most comprehensive explanation. For the purpose of the explanation of the extent to which the audit was considered capable of detecting irregularities, including fraud disclosed within the audit certificate, the NAO uses the definition of an irregularity given in paragraph 12 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements* to mean a non-compliance with relevant laws and regulations relevant to the audit, including fraud and matters included within the entity's framework of authorities for the purpose of the regularity opinion.

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		The engagement team may find it helpful, in developing their explanation, to review the documentation covering the following matters: • The engagement team's assessment of the susceptibility of the entity's financial statements to material misstatement, including how fraud might occur, as documented in the Engagement Team Discussion on Risk and Fraud. • The engagement director's assessment of whether the engagement team collectively had the appropriate competence and capabilities to identify or recognise non-compliance with laws and regulations, and details of those matters about non-compliance with laws and regulations and fraud that were communicated to the engagement team. This will be documented in the Engagement Risk Assessment Audit Form. • The engagement team's understanding of the entity's current activities, the scope of its authorisation and the effectiveness of its control environment where the entity is a regulated entity. • Communications with component auditors to request identification of any instances of noncompliance with laws and regulations that could give rise to a material misstatement of the group financial statements. This will be documented in the Group Audit Instructions. The engagement team may also have determined that certain matters relating to non-compliance with laws and regulations are key audit matters. This does not exempt the engagement team from also including the required explanation, in their report, as to what extent the audit was considered capable of detecting irregularities, including fraud.
Report (where no additional observations are given by the C&AG; an additional C&AG's report would be included after the main certificate/report)		See Chapter 58: Reporting to Parliament.
Auditor's signature	47 A64 to A65	For most audits carried out by the NAO, the audit certificate is signed by the C&AG. Where responsibility for signing the certificate is delegated by the C&AG to the Engagement Director, the Engagement Director should sign personally, with the words *"for and on behalf of the Comptroller and Auditor General"* appearing below the Director's name.

Section	ISA (UK) 700 paragraph reference(s)	Additional comments
		In the case of audits carried out by the NAO under the Companies Act 2006, the audit report is signed by the Senior Statutory Auditor, for and on behalf of the Comptroller and Auditor General.
Auditor's address	48 A65-1	The report should name the location of the office where the auditor is based. The C&AG includes the full address which will be 157-197 Buckingham Palace Road, Victoria, London, SW1W 9SP.
Date of the certificate or report	49 to 49-2 A66 to A69	If the certificate is signed at a date later than that on which the Accounting Officer approved the financial statements, the Engagement Director should obtain assurance that the Accounting Officer would have approved the financial statements at the certification date and ensure that the review of post balance sheet events covers the period up to the date of signature. Such assurance must be obtained from or directly on behalf of the Accounting Officer.

Extended Auditor Reporting

54.73 The NAO's policy is that audits of the following entities must prepare extended auditor reports:

- listed companies;
- Public Interest Entities;
- entities that are required, and those that chose voluntarily, to report on how they have applied the UK Corporate Governance Code; and
- other entities as determined by the C&AG.

54.74 ***Consultation required*** All Extended Auditor Reports must be submitted to FAPQ for review, but only require a DAQ minute where the report is modified. Unmodified Extended Auditor Reports do not require a DAQ minute but must still be submitted to FAPQ for review.

54.75 Pro-forma Extended Auditor Reports have been provided for engagement teams to draft their Extended Auditor Reports. These pro-formas are available for both Departments and Companies.

54.76 It is important that the form and content of Extended Auditor Reports are presented in a uniform fashion, as this promotes the reader's understanding of the report, and highlights unusual circumstances when they occur. An Extended Auditor Report should therefore include the following elements:

- Title
- Addressee
- Introductory paragraph identifying the statements to be audited
- Opinion on the financial statements
- Opinion in respect of an additional financial reporting framework (where applicable)
- Opinion on regularity (where applicable)

- Basis for opinion(s)
- Conclusions relating to going concern
- Key Audit Matters
- Application of materiality
- Audit scope
- Other Information
- Opinion on other matters
- Matters on which [the C&AG/the Senior Statutory Auditor] report[s] by exception
- [for entities which report on how they have applied the UK Corporate Governance Code only] Corporate governance statement
- Responsibilities of [management/those charged with governance/the Directors/the Board/the Accounting Officer] for the Financial Statements
- Auditor's responsibilities for the audit of the financial statements
- [for company audits] Other matters which [the Senior Statutory Auditor is] required to address
- Auditor's signature
- Auditor's address and
- Date of the report

Extended Auditor Reporting – key audit matters

54.77 A description of the key audit matters which arose during the course of the audit of the financial statements and how they have been addressed by the engagement team should be provided in the "Key Audit Matters" section of the auditor's report.

54.78 Paragraphs 8 and 11 of ISA (UK) 701 (Revised November 2019) (Updated May 2022) define key audit matters as those matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditor, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. Key audit matters are selected from matters communicated with those charged with governance.

54.79 Paragraph A28-1 of ISA (UK) 701 (Revised November 2019) (Updated May 2022) requires the auditor to use their judgement to determine which, if any, of the significant risks and which, if any, of the other identified risks should be included as key audit matters. Accordingly, the engagement team should ensure they have:

- considered all significant risks for whether they are key audit matters; and
- for any significant risks that are not treated as key audit matters, documented their consideration as to why not.

54.80 The presumed significant risks of material misstatement and material irregular transactions would normally constitute key audit matters to be reported in the auditor's report. However, ISA (UK) 701 (Revised November 2019) (Updated May 2022) does provide for these significant risks not to be reported as key audit matters. Where this is the case, the team should ensure that they have clearly documented in the audit file why the significant risks of material misstatement do not constitute key audit matters.

54.81 Most of the key audit matters communicated in the audit of the parent would likely also be key audit matters in the audit of the group financial statements, subject to any differences in

quantitative materiality considerations that may apply in those audits. However, there may be key audit matters that only arise in relation to the audit of the parent financial statements.

54.82 Where there are no key audit matters to report, a statement to this effect should be included within the key audit matters section.

54.83 In accordance with paragraph 14 of ISA (UK) 701 (Revised November 2019) (Updated May 2022), each key audit matter should be described in the audit report unless law or regulation precludes disclosure about the matter or, in extremely rare circumstances, the engagement team determines that the matter should not be communicated in the auditor's report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication. The latter circumstance shall not apply if the entity has publicly disclosed information about the matter. Where such circumstances apply, the engagement team may consult with FAPQ.

54.84 In accordance with paragraph 12 of ISA (UK) 701 (Revised November 2019) (Updated May 2022), where a matter has led to a modification of the audit opinion, it should not be reported within the key audit matters section.

54.85 The engagement team should clearly document their rationale for why the key audit matters being reported on in the audit report are key audit matters within their audit documentation. Similarly, where no key audit matters have been identified, the rationale to support this assessment should be documented.

Extended Auditor Reporting – key audit matters – going concern

54.86 As described in paragraph A1 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern*, matters relating to going concern may be determined to be key audit matters and a material uncertainty related to going concern is, by its nature, a key audit matter.

54.87 However, even where the engagement team has concluded that management's use of the going concern basis of accounting is appropriate in the circumstances and no material uncertainty has been identified, the engagement team may still decide to report the work which has been undertaken surrounding the going concern assumption as a key audit matter. This is particularly likely to be the case where the use of the going concern assumption has been identified as a significant risk.

Extended Auditor Reporting – materiality

54.88 The explanation of the significant judgements made by the auditor in determining materiality and performance materiality, which is required to be included by paragraph 16-1 of ISA (UK) 701 (Revised November 2019) (Updated May 2022), should focus on the needs of the users of the accounts.

54.89 In addition to the matters suggested to be included in the explanation of how the auditor applied the concept of materiality in planning and performing the audit in paragraph A59-2 of ISA (UK) 701 (Revised November 2019) (Updated May 2022), the engagement team should also consider including, as appropriate, the approach to setting materiality in the context of the regularity opinion.

Extended Auditor Reporting – audit scope

54.90 In addition to the matters suggested to be included in the overview of the scope of the audit in paragraph A59-3 of ISA (UK) 701 (Revised November 2019) (Updated May 2022), the engagement team should also consider including, as appropriate:

- the approach taken to address risks of non-compliance with the entity's framework of authorities; and
- a summary of the engagement's team's approach to the audit of the Statement of Outturn against Parliamentary Supply.

Extended Auditor Reporting – Corporate Governance Statement

54.91 For entities that are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, in accordance with paragraph 22-3 of ISA (UK) 720 (Revised November 2019) (Updated May 2022), the auditor's report should include a separate section with a heading "Corporate Governance Statement" for entities that report on how they have applied the UK Corporate Governance Code.

54.92 Where the engagement team has nothing material to draw the attention of the users of the financial statements attention to in respect of these matters, a statement should be included that the auditor has nothing to report in respect of these matters.

Summary financial statements

54.93 In some cases, entities may wish to publish a document in addition to its annual report and accounts that contains summary financial statements. The Companies Act 2006 sets out requirements which should be complied with in the production of summary financial statements; these requirements also apply for bodies reporting under the FReM. Summary financial statements must state in a prominent note that the data is a summary and may not contain sufficient information to give a full understanding of the entity's performance and financial position. This note should also state how the reader can obtain a full copy of the audited financial statements.

54.94 The Companies Act 2006 stipulates that summary financial statements should be followed by an auditor's statement as to whether, in their opinion, the summary information is consistent with the full financial statements. This statement should be signed by the Engagement Director, "for and on behalf of the Comptroller and Auditor General".

54.95 Where an entity requests that a report is provided on a set of summary financial statements, standard engagement approval processes should be followed to obtain C&AG approval. If approved, the terms of our engagement should be set out within our letter of engagement or understanding. Guidance on the proposed wording of the auditor's statement is provided in the Auditing Practices Board Bulletin 2008/03. Further guidance may be sought from FAPQ.

54.96 Summary statements should not be published in advance of the full annual report and accounts being laid before Parliament as to do so would be a breach of parliamentary privilege. Further financial information is not subject to audit unless a separate assurance engagement is agreed to.

Interim financial statements

54.97 There is currently no statutory requirement for entities audited by the C&AG to produce interim financial statements. If an entity wishes to produce interim financial information which is subject to auditor review ISRE (UK) 2410 *Review of interim financial information performed by the*

independent auditor of the entity, engagement teams will need to consider the acceptance of this additional engagement. Further guidance may be sought from FAPQ.

Reporting to regulators

54.98 When reviewing the evidence in support of the C&AG's opinions on the audits of Public Interest Entities and other regulated entities in the financial sector, the engagement team should consider if the cumulative effective of matters noted during the course of the audit is of material significance to the regulator. Where the cumulative effect of such matters are of material significance to the functions of the regulator, the engagement team should make a report to the regulator in accordance with ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector*. Further guidance on such reports may be found in Chapter 31: Consideration of laws and regulations and reporting to regulators.

Electronic publication

54.99 If the annual financial statements and the audit certificate are to be included on a website or distributed electronically, paragraphs A4 and A19 of ISA (UK) 720 (Revised November 2019) (Updated May 2022) provide guidance on the consideration of other information.

54.100 The publication on an entity's website of a PDF version of the published accounts is not electronic publication as defined in Auditing Practices Board Bulletin 2001/01 *The electronic publication of auditors' reports* because it retains the integrity of the original document; therefore, there is no requirement to add an additional paragraph to the audit opinion in the PDF version of the accounts. However, the engagement team is still required to take steps to ensure that the PDF version is identical to the manually-signed version, in accordance with ISA (UK) 720 (Revised November 2019) (Updated May 2022).

54.101 In respect of electronic publication of the annual report and accounts, the engagement team should:

- review the process by which the electronic version of the financial statements is extracted from the information contained in the manually-signed version;
- check that the proposed electronic version is identical in content to the manually signed version; and
- check that the conversion into electronic format has not distorted the overall presentation of the financial information, such as by highlighting certain information to give it more prominence.

54.102 If the audited entity intends to include the audit certificate or report when publishing their annual report and accounts electronically, then in line with the principles described in Auditing Practices Board Bulletin 2001/01[10], the engagement team should:

- include the following clarification within the Letter of Understanding or Letter of Engagement (reissuing this prior to certification where necessary – for example, if the audited entity informs the engagement team of their intention to publish the annual report and accounts electronically late in the audit process; if the intention to publish electronically comes to light after certification, the Letter will still need to be re-issued) and also within the 'Responsibilities of the [Board/Accounting Officer/Directors, etc.] for the financial statements' section of the electronically-published version

[10] Auditing Practices Board (APB) Bulletins have been withdrawn because of outdated references to auditing standards, law and regulations. However, guidance from the Financial Reporting Council indicates that the substantive guidance may still be useful, if used in the knowledge that the detailed references are likely to be out of date. The procedures outlined here have been designed with the principles set out in APB Bulletin 2001/01 in mind, but the FAM does not require full compliance with the Bulletin.

(not the original) of the audit certificate or report: "*Management is responsible for the maintenance of, and controls underpinning, the web page upon which the electronic version of the* [describe the content being published electronically; for example, the annual report and financial statements] [is/are] *published.*";

- ask management to include a disclaimer on the web page upon which the electronic version is published to the effect that management is responsible for the maintenance of, and controls underpinning, that web page; and
- include the following 'Bannerman' paragraph within the 'Other auditor's responsibilities' sub-section of the 'Auditor's responsibilities for the audit of the financial statements' section of the audit certificate or report: *"To the fullest extent permitted by law, I do not accept or assume responsibility to* [client name]*,* [addresse(s) of the audit certificate or report: for example, the Houses of Parliament] *or any third party for reviewing the operation of controls underpinning the web page upon which the electronic version of the* [describe the content being published electronically; for example, the annual report and financial statements] [is/are] *published."* The Bannerman paragraph should be included only in the electronically-published version of the certificate or report, not in the original version.

54.103 Alternatively to the procedures described in the preceding paragraph, the engagement team may agree with the audited entity that the audit certificate or report will not be included where the annual report and accounts are published electronically. If this approach is taken, the engagement team should ensure the audited entity removes all references to information within the annual report and accounts being audited (for example, the parts of the Remuneration and Staff Report and the Accountability Report marked as subject to audit for entities with the FReM as their financial reporting framework) – for clarity, this does not extend to tangential references to the audit, such as references in the governance statement to the C&AG or the NAO being the entity's external auditor or descriptions of responses to external audit recommendations.

Chapter 55: Modified certificates and reports

Relevant standards and guidance

55.1 Paragraphs 21 to 24-2 of ISA (UK) 570 (Revised September 2019) (Updated May 2022) *Going concern* and the related application guidance set out the implications for the auditor's report where the use of the going concern basis of accounting is inappropriate, or it is appropriate but a material uncertainty related to going concern exists.

55.2 Paragraphs 1-142 to 1-181 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 570 (Revised September 2019) (Updated May 2022) in the public sector.

55.3 ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* deals with the auditor's responsibility to form an opinion on the financial statements. It also deals with the form and content of the auditor's report issued as a result of an audit of financial statements.

55.4 Paragraphs 1-203 to 1-216 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 700 (Revised November 2019) (Updated May 2022) in the public sector.

55.5 ISA (UK) 705 (Revised June 2016) *Modifications to the opinion in the independent auditor's report* deals with the auditor's responsibility to issue an appropriate report in circumstances when, in forming an opinion in accordance with ISA (UK) 700 (Revised November 2019) (Updated May 2022), the auditor concludes that a modification to the auditor's opinion on the financial statements is necessary. ISA (UK) 705 (Revised June 2016) also deals with how the form and content of the auditor's report is affected when the auditor expresses a modified opinion.

55.6 ISA (UK) 706 (Revised June 2016) *Emphasis of Matter paragraphs and Other Matter paragraphs in the independent auditor's report* deals with additional communication in the auditor's report when the auditor considers it necessary to:

- draw users' attention to a matter or matters presented or disclosed in the financial statements that are of such importance that they are fundamental to users' understanding of the financial statements; or
- draw users' attention to any matter or matters other than those presented or disclosed in the financial statements that are relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report.

55.7 Paragraphs 1-219 to 1-220 of Practice Note 10 (Revised 2022) provide guidance on applying ISA (UK) 706 (Revised June 2016) in the public sector.

55.8 Appendices 1 and 2 to ISA (UK) 706 (Revised June 2016) identify ISAs (UK) that contain specific requirements for the auditor to include Emphasis of Matter paragraphs or Other Matter paragraphs in the auditor's report.

55.9 Paragraphs 10 to 19 of ISA (UK) 710 *Comparative information – corresponding figures and comparative financial statements* includes requirements relating to the implications for the auditor's report of matters relating to comparative information, including a modified opinion in the prior period,

prior period misstatements, and where the prior period financial statements were not audited or were audited by a predecessor auditor.

55.10 Paragraphs 2-83 to 2-87 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on the regularity opinion where one is included in the auditor's report.

55.11 Paragraphs 2-88 to 2-91 of Practice Note 10 (Revised 2022) provide guidance on other reporting on regularity.

Modifications to the audit opinion

55.12 In accordance with paragraph 4 of ISA (UK) 705 (Revised June 2016), the opinion in the auditor's report should be modified when the engagement team concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement; or the engagement team are unable to obtain sufficient appropriate audit evidence to conclude that the financial statements as a whole are free from material misstatement.

55.13 To ensure that modified certificates are clear and easy to understand, it is important to maintain as much uniformity as possible in the content and style of the certificates. Accordingly suggested wording has been given in ISA (UK) 705 (Revised June 2016). Engagement teams may make reference to the FRC's Bulletins on illustrative auditor's reports.

55.14 ISA (UK) 705 (Revised June 2016) establishes three types of modified opinions:

- Qualified opinion
- Disclaimer of opinion
- Adverse opinion

55.15 The engagement team's judgement of the nature of the matter giving rise to the opinion and the pervasiveness of its effects on the financial statements affects the type of the opinion to be expressed:

55.16 A material misstatement of the financial statements may arise in relation to:

- the appropriateness of the selected accounting policies;
- the application of the selected accounting policies; or
- the appropriateness or adequacy of disclosures in the financial statements.

55.17 A limitation on scope may arise from:

- circumstances beyond the control of the entity;
- circumstances relating to the nature and timing of the engagement team's work; or
- limitations imposed by management.

55.18 The term "pervasive" is defined in paragraph 5(a) of ISA (UK) 705 (Revised June 2016).

55.19 Reporting objectives for financial statements in the public sector, and the sensitivity of users to misstatement, are not generally linked to single figure such as profit or loss or net assets to the same extent as for private sector entities. Consequently, it is rarer that a misstatement or a limitation on scope would be deemed to be pervasive to the financial statements as a whole. It would be more common to issue an opinion containing multiple qualifications or limitations in scope.

55.20 Paragraphs 15 and A16 of ISA (UK) 705 (Revised June 2016) set out that an adverse opinion or disclaimer of opinion should not be accompanied by an unmodified opinion with respect to the same financial reporting framework on a single financial statement or one or more specific elements, accounts or items of a financial statement.

Types of audit opinion

55.21 ***Table 55A*** and the following sections set out the different types of audit opinion and when they arise.

Table 55A: Types of audit opinion

Nature of matter giving rise to the modification	Engagement team's judgement about the pervasiveness of the effects or possible effects on the financial statements	
	Material but not pervasive	**Material and pervasive**
Financial statements are materially misstated	Qualified opinion – except for disagreement	Adverse opinion
Inability to obtain sufficient appropriate audit evidence	Qualified opinion – except for limitation of scope	Disclaimer of opinion

55.22 ***Consultation required*** The engagement team should discuss any proposed modifications to the audit certificate with FAPQ at an early stage. A minute from the Director, Audit Quality or a named deputy confirming the form of the certificate or report is required to be included in the certification journal of all accounts with modified opinions.

Qualified opinion

55.23 Paragraph 7 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out when the auditor should express a qualified opinion.

55.24 Similarly, where a regularity opinion is provided as part of the audit engagement, a qualified opinion on regularity should be expressed when:

- having obtained sufficient appropriate audit evidence, the engagement team concludes that irregular transactions, individually or in the aggregate, are material to the financial statements. (disagreement); or
- the engagement team is unable to obtain sufficient appropriate audit evidence on which to base the regularity opinion (limitation of scope).

55.25 Paragraph 17 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out the form and content of the auditor's opinion when the auditor expresses a qualified opinion.

Adverse opinion

55.26 Paragraph 8 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out when the auditor should express an adverse opinion.

55.27 Similarly, where a regularity opinion is provided as part of the audit engagement, the engagement team should express an adverse opinion on regularity when the auditor, having obtained sufficient appropriate audit evidence, concludes that the irregular transactions, individually or in the aggregate, are both material and pervasive to the financial statements.

55.28 Paragraph 18 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out the form and content of the auditor's opinion when the auditor expresses an adverse opinion.

Disclaimer of opinion

55.29 Paragraphs 9 to 10 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out when the auditor should disclaim an opinion.

55.30 Similarly, where a regularity opinion is provided as part of the audit engagement, the engagement team should disclaim the opinion on regularity when the auditor is unable to obtain sufficient appropriate audit evidence on which to base the regularity opinion, and the auditor concludes that the possible effects on the transactions covered by the regularity opinion of undetected irregular transactions, if any, could be both material and pervasive.

55.31 Paragraph 19 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out the form and content of the auditor's opinion when the auditor disclaims an opinion.

Limitation on scope

55.32 Where a limitation is imposed by the entity prior to the acceptance of an audit engagement, the engagement team should consider whether it is appropriate to accept the engagement (referring to Chapter 9: Engagement acceptance (statutory and non-statutory)). If a limitation is imposed by the entity after accepting the audit engagement, and the entity will not remove the limitation, the engagement team should consider if it is appropriate to resign from the engagement.

55.33 Paragraphs 11 to 14 of ISA (UK) 705 (Revised June 2016) and the related application guidance set out the consequences of an inability to obtain sufficient appropriate audit evidence due to a management-imposed limitation after the auditor has accepted the engagement.

55.34 Where the C&AG is appointed under statute, it is not possible to decline or withdraw from the engagement. In these circumstances, the C&AG has the statutory authority to report such matters to Parliament (see Chapter 58: Reporting to Parliament).

Breaches of voted control totals

55.35 A qualification resulting from a breach of voted control total is particular to departmental accounts and is a form of disagreement qualification on the opinion on regularity. A breach of a voted control total arises in a departmental account where the amount of resources, capital and/or cash voted in Supply Estimates has been exceeded by outturn. If a department exceeds its Administration Cost Limit it is usually treated in the same way as a breach of a voted total.

55.36 Where a breach of a voted control total occurs, the regularity opinion in the audit certificate is qualified. No materiality threshold is applied and qualification is made regardless of the amounts involved. Qualification, which is in the form of an 'except for' opinion, may be in respect of one or more kinds of breach.

Impact of a prior year qualification

55.37 If the auditor's report on the prior period, as previously issued, included a qualified opinion, a disclaimer of opinion, or an adverse opinion and the matter which gave rise to the modification is unresolved, the C&AG will modify the auditor's opinion on the current period's financial statements.

55.38 The engagement team should follow the requirements of paragraph 11 of ISA (UK) 710 and the related application guidance on modifying the opinion on the current year financial statements.

55.39 If the matter that gave rise to the modified opinion has been resolved and properly corrected in the prior year comparatives in the financial statements, the current certificate does not need to refer to the previous modification. However, if the matter is material to the current period, the engagement team may wish to include an Emphasis of Matter paragraph to give further information about the situation.

Communicating with those charged with governance regarding a proposed modified opinion

55.40 The engagement team should follow the requirements of paragraph 30 of ISA (UK) 705 (Revised June 2016) and the related application guidance on communicating with those charged with governance regarding the proposed modified opinion and its wording.

Documentation requirements relating to modified opinions, Emphasis of Matter or Other Matter paragraphs

55.41 Matters relating to the modification of the audit opinions, or inclusion of an Emphasis of Matter or Other Matter paragraph will in all cases be significant documentation matters for the purpose of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation*.

55.42 Documentation of the professional judgments made, where significant, serves to explain the engagement team's conclusions and to reinforce the quality of the judgment in the file.

Emphasis of Matter, Other Matter and Material uncertainty related to going concern paragraphs

55.43 ISA (UK) 706 (Revised June 2016) explains when an Emphasis of Matter or an Other Matter paragraph should be included in the auditor's report.

55.44 ISA (UK) 570 (Revised September 2019) (Updated May 2022) explains when a Material uncertainty related to going concern paragraph should be included in the auditor's report. Further guidance is available in Chapter 27: Going concern.

55.45 ***Consultation required*** Engagement teams must consult with FAPQ at the earliest opportunity where they are considering the inclusion of an Emphasis of Matter, Other Matter or Material uncertainty related to going concern paragraph in the certificate.

55.46 An Emphasis of Matter paragraph would be included in the audit certificate directly after the opinion paragraph to which it relates and would refer to the fact that the auditor's opinion is not qualified in respect of the matter.

55.47 The use of an Emphasis of Matter paragraph should not be routine as this diminishes the effectiveness of our communication of such matters. In addition, it should not be used to compensate for inadequate disclosure by the reporting body – the absence of disclosures required to provide a true and fair view would lead to a qualified opinion. Emphasis of Matter paragraphs are generally considered where:

- there is a significant uncertainty relating to a future action or event which is outside the reporting entity's control and which, potentially, has a material impact on the financial statements; or

- the prior year accounts were qualified and the matter giving rise to the qualification has been resolved with appropriate disclosures or adjustments made to the corresponding figures, but the prior period financial statements have not been reissued.

55.48 Uncertainties are regarded as significant when they involve a significant level of concern about matters whose potential effect on the financial statements is unusually great, or about the validity of the going concern basis. However, the opinion will be unqualified where the engagement team considers that appropriate estimates and disclosures have been included in the financial statements. A common example of a significant uncertainty is the outcome of on-going major litigation.

55.49 Uncertainty contained within an accounting estimate, such as an actuarial valuation, will not necessarily give rise to an Emphasis of Matter. Uncertainties inherent in accounting estimates should be considered in accordance with ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures*. Where the engagement team considers that the accounting estimate is reasonable in the circumstances, an Emphasis of Matter paragraph would not routinely be included in the certificate.

55.50 Where the entity has prepared their financial statements on a basis other than going concern and the engagement team has concluded that this is appropriate, this will be highlighted through reporting in the Conclusions on going concern paragraph of the audit certificate.

55.51 The following are examples of where it may be appropriate to include an Other Matter paragraph:

- where the C&AG is unable to withdraw from an engagement even though the possible effect of an inability to obtain sufficient appropriate audit evidence due to a limitation on the scope of the audit imposed by management is pervasive, the engagement team may consider it necessary to include an Other Matter paragraph in the auditor's report to explain why it is not possible to withdraw from the engagement;
- where there is a material inconsistency between the financial statements and the surrounding information arising from a misstatement in the surrounding information;
- where the terms of the engagement allow for a separate C&AG's report, issues that may give rise to Other Matter paragraphs may instead be disclosed in a substantive C&AG's report (further guidance may be found in Chapter 58: Reporting to Parliament); or
- in exceptional cases when management or those charged with governance do not take the remedial action that the engagement team considers appropriate to address and instance of actual or suspected non-compliance with laws and regulations and withdrawal from the engagement is not possible.

55.52 The Emphasis of Matter paragraph should give details of the matter giving rise to the significant uncertainty, and its possible effects on the financial statements, including quantification if possible. Where it is not possible to quantify the effects on the financial statements, a statement to this effect should be included. Clarity for the reader is enhanced by using an appropriate sub-heading in the report to differentiate the Emphasis of Matter paragraph from other paragraphs in the audit certificate. In determining whether an uncertainty is significant, the engagement team should consider:

- the risk that an estimate included in financial statements may be subject to change; and
- the range of possible outcomes.

Chapter 56: Management representations

Relevant standards and guidance

56.1 ISA (UK) 580 (Updated May 2022) *Written representations* deals with the auditor's responsibility to obtain written representations from management and, where appropriate, those charged with governance in an audit of financial statements.

56.2 Paragraphs 1-182 to 1-185 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 580 (Updated May 2022) in the public sector.

56.3 Appendix 1 to ISA (UK) 580 (Updated May 2022) lists other ISAs (UK) containing subject-matter specific requirements for written representations.

Background

56.4 During an audit, management and those charged with governance will make a number of representations concerning matters relating to the financial statements. A robust control environment should prevent or detect and correct material misstatements in the financial statements.

56.5 Written representations are obtained on matters which are material to the financial statements, in addition to a number of standard representations such as management acknowledging responsibility for the preparation of financial statements that give a true and fair view.

56.6 It is NAO policy to request representations from those charged with governance. Therefore, for entities where there is an Accounting Officer, obtain written representations from the Accounting Officer; for entities without an Accounting Officer, obtain written representations from the board. References throughout this Chapter to "management" refer to either the Accounting Officer or the board, depending upon an audited entity's governance arrangements.

56.7 For most public bodies, the Accounting Officer is both charged with governance (assisted by the audit committee) and part of management. It is therefore requested that the Accounting Officer signs the management representation letter.

56.8 For companies and charities, the board is charged with governance, as well as including members of management, and so a director or trustee is usually requested to sign on behalf of the board.

56.9 Although written representations are an important source of audit evidence, they supplement but do not replace other audit procedures – receiving representations does not affect the nature or extent of our other audit procedures.

Application guidance

56.10 Management make representations on an "informed basis". As such, the standard NAO Letter of Representation includes confirmation that management have made appropriate inquiries to be able to make the requested written representations. In most cases, such inquiries do not require a formal internal process beyond those already established by the entity.

56.11 Management may wish to include in the representations qualifying language to the effect that representations are made to the best of its knowledge and belief. Such wording can be accepted if the engagement team are satisfied that the representations are being made by those with appropriate responsibilities and knowledge of the matters included in the representations.

56.12 If, when drafting the Letter of Representation, the engagement team considers that the Letter of Understanding or Engagement Letter gives an inappropriate description of management's responsibilities, they should consider whether it is appropriate to issue a revised Letter of Understanding or Engagement Letter and may consult with FAPQ.

56.13 In some circumstances, management may not believe that certain uncorrected misstatements are misstatements. For that reason, they may want to add to their written representation words such as: *"We do not agree that* [specified items] *constitute misstatements because* [description of reasons]*."* Obtaining this representation does not, however, relieve the engagement team of the need to form a conclusion on the effect of uncorrected misstatements.

56.14 If there are material balances arising from litigation and claims then the engagement team will usually need to request specific representations about these balances.

56.15 Balances relating to litigation and claims are usually accounting estimates, and so the engagement team should also obtain representations about the significant assumptions used in making the estimates, as discussed below.

56.16 Depending on the nature, materiality and extent of estimation uncertainty, written representations about accounting estimates recognised or disclosed in the financial statements may include representations:

- about the appropriateness of the measurement processes, including related assumptions and models, used by management in determining accounting estimates in the context of the FReM (or other applicable financial reporting framework), and the consistency in application of the processes;
- that the assumptions appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the entity, where relevant to the accounting estimates and disclosures;
- that disclosures related to accounting estimates are complete and appropriate under the FReM (or other applicable financial reporting framework); and
- that no subsequent event requires adjustment to the accounting estimates and disclosures included in the financial statements.

56.17 For those accounting estimates not recognised or disclosed in the financial statements, written representations may also include representations about:

- the appropriateness of the basis used by management for determining that the recognition or disclosure criteria of the applicable financial reporting framework have not been met; and
- the appropriateness of the basis used by management to overcome the presumption relating to the use of fair value set forth under the applicable financial reporting framework, for those accounting estimates not measured or disclosed at fair value.

56.18 The engagement team may also decide to obtain written representations regarding specific assertions that management have made, such as a representation that specific related party transactions do not involve undisclosed side agreements.

56.19 An entity may require its management and those charged with governance to sign individual declarations in relation to related party matters. It may be helpful if any such declarations are

addressed jointly to a designated official of the entity and also to the NAO. In some circumstances, the engagement team may wish to obtain written representations directly from each of those charged with governance and from members of management.

56.20 For entities reporting applying the 'continued provision of service' approach to going concern, the financial reporting framework provides specific guidance on the interpretation and application of the going concern concept for public sector entities. This recognises that for sponsored entities and other entities reliant on continued government support, Government policy will be a key consideration in determining whether the going concern basis remains appropriate. Consequently, when indicators of uncertainty are present, it would usually be expected that management would obtain direct confirmation from the department or executive body responsible for providing sponsorship. Without this, management may not be in a position to provide a representation.

56.21 In particular, engagement teams may consider it necessary to obtain a written representation when management's intentions are relevant to the recognition or valuation of a balance.

56.22 If engagement teams are reporting under a financial reporting framework which requires them to refer to comparative information in the audit opinion, then written representations should be obtained for all periods referred to in the opinion. This will not apply to entities preparing accounts under the FReM or IFRS.

56.23 Management may request amendments to the letter of representations that the engagement team have drafted. This does not necessarily mean that management did not provide the written representations, and engagement teams should consider the reasons for the changes requested. In certain circumstances, the underlying reason for such modification may affect the opinion in the C&AG's report, such as due to a limitation in scope as to the information available to both management and the engagement team.

56.24 The NAO has developed a standard template for the Letter of Representation, which can be used as the basis for all Letters of Representation and tailored to reflect the circumstances of the entity and any specific representations required. The Engagement Manager is normally responsible for preparing the letter of representation and should ensure that all representations that are material and relevant to the financial statements are included. Where possible and appropriate the representations should be quantified.

56.25 The engagement team may have identified significant issues relating to the competence, integrity, ethical values or diligence of management, or about its commitment to or enforcement of these, but concluded that the written representations are nevertheless reliable. If this is the case, then this should be documented as a significant matter in accordance with the requirement of ISA (UK) 230 (Revised June 2016) (Updated May 2022) *Audit documentation* to document significant matters arising during the audit, the conclusions reached thereon, and significant professional judgments made in reaching those conclusions.

56.26 Engagement teams should take care in drafting the Letter of Representation so that:

- it clearly sets out the issues that the engagement team are requesting representations in respect of;
- the engagement team are only asking for representations to supplement other audit evidence, rather than as our sole source of evidence;
- the engagement team is asking for representations that they would expect management to be in a position to provide; and
- the engagement team are not asking for representations that contradict other evidence.

56.27 It may be appropriate to request evidence through confirmations or representations from other parties, rather than from management, where they are more likely to be in a position to provide reliable evidence (such as requesting management confirm with their funding body its intentions, or obtaining a confirmations from a counterparty as to their interpretation of a contract).

56.28 As the audit progresses, it is often efficient for team members to consider whether specific representations will be required in respect of their areas, and flag proposed wording in the Apex audit file to assist the Engagement Manager in drafting the letter of representation.

Accounting policies

56.29 The engagement team should obtain written representations that management considers the selection and application of accounting policies to be appropriate to the entity's circumstances and its in-year transactions, and that the following matters have been appropriately recognised, measured, presented or disclosed in accordance with the applicable financial reporting framework:

- plans or intentions that may affect the carrying value or classification of assets and liabilities;
- liabilities, both actual and contingent;
- title to, or control over, assets, the liens or encumbrances on assets, and assets pledged as collateral; and
- aspects of laws, regulations and contractual agreements that may affect the financial statements, including non-compliance.

Internal controls

56.30 The engagement team should obtain written representations that management acknowledges its responsibility for designing and maintaining the system of internal control, and that it has communicated to the engagement team all deficiencies in internal control of which they aware.

Information provided and completeness of transactions

56.31 The engagement team should obtain written representations that management has provided the engagement team with all relevant information and access as agreed in the terms of the audit engagement and that all transactions have been recorded and are reflected in the financial statements.

Description of management's responsibilities in the written representations

56.32 The engagement team should obtain written representations that describe management's responsibilities in the same way that these responsibilities are described in the Letter of Understanding or Engagement Letter.

Fraud

56.33 As required by paragraph 39 of ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial* statements, the engagement team should obtain written representations that management:

- acknowledge their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and believe they have appropriately fulfilled those responsibilities;
- have disclosed to the auditor the results of management's assessment of the risk that the financial statements may be materially misstated as a result of fraud;

- have disclosed to the auditor their knowledge of fraud or suspected fraud affecting the entity involving:
    - management;
    - employees who have significant roles in internal control; or
    - others where the fraud could have a material effect on the financial statements; and
- have disclosed to the auditor their knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

Laws and regulations

56.34 As required by paragraph 17 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements*, the engagement team should obtain written representations that management has disclosed all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements to the engagement team.

56.35 Where non-compliance with regulations is suspected or discovered, the engagement team should consider the wider implications for the financial statements as a whole. This will also include consideration of the implications for our assessment of risks and controls in relation to material irregularities, and the reliance the engagement team can place on the overall control environment and representations from management. Further guidance is provided in Chapter 31: Consideration of laws and regulations and reporting to regulators.

56.36 Paragraph A24 of ISA (UK) 250A (Revised November 2019) (Updated May 2022) includes examples of circumstances that may cause the auditor to evaluate the implications of identified or suspected non-compliance with laws and regulations on the reliability of written representations.

Uncorrected misstatements

56.37 As required by paragraph 14 of ISA (UK) 450 (Revised June 2016) (Updated May 2022) *Evaluation of misstatements identified during the* audit, the engagement team should obtain written representations that management believes the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole.

56.38 The engagement team should request that management explain the reasons for not correcting any identified unadjusted misstatements. Written representations should include a summary of identified unadjusted misstatements along with this rationale.

Litigation and claims

56.39 The engagement team should obtain written representations from management that all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements have been disclosed to the engagement team and accounted for and disclosed in accordance with the applicable financial reporting framework.

Accounting estimates

56.40 As required by paragraph 37 of ISA (UK) 540 (Revised December 2018) (Updated May 2022) *Auditing accounting estimates and related disclosures*, the engagement team should obtain

written representations that management believes all significant assumptions used in making accounting estimates are reasonable.

Related parties

56.41 As required by paragraph 26 of ISA (UK) 550 *Related parties*, the engagement team should obtain written representations that management have disclosed to the engagement team the identity of the entity's related parties and all the related party relationships and transactions of which they are aware; and that they have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the applicable financial reporting framework.

Subsequent events

56.42 The engagement team should obtain written representations from management that all events occurring subsequent to the date of the financial statements, and for which the applicable financial reporting framework requires adjustment or disclosure, have been adjusted or disclosed.

Going concern

56.43 The engagement team should obtain written representations from management that they consider that the entity is a going concern. If events or conditions that may cast significant doubt on the entity's ability to continue as a going concern are identified, the engagement team should obtain written representations from management regarding their plans for future action and the feasibility of these plans.

Restatements

56.44 If there is a restatement to correct a material misstatement in prior period financial statements that affect the comparative information, the engagement team should obtain written representations from management in respect of the restatement.

Regularity

56.45 Where the engagement requires a regularity opinion, the engagement team should obtain written representations from management on the discharge of its responsibility for the regularity of transactions.

Other Information

56.46 As required by paragraph 13(c) of ISA (UK) 720 (Revised November 2019) (Updated May 2022) *The auditor's responsibilities relating to Other Information*, when some or all of the document(s) comprising the annual report will not be available until after the date of the auditor's report, the engagement team should request management to provide a written representation that the final version of the document(s) will be provided to the auditor when available, and prior to its issuance by the entity, such that the auditor can complete the procedures required by ISA (UK) 720 (Revised November 2019) (Updated May 2022).

Public Interest Entities and other entities operating in the regulated sector

56.47 For Public Interest Entities and other entities operating in the regulated sector, the engagement team should obtain written representations from management regarding compliance with anti-money laundering legislation.

Requesting representations for other issues

56.48 If it is necessary to obtain additional written representations to support other audit evidence relevant to the financial statements, or to specific assertions in the financial statements, the engagement team should obtain appropriately-tailored written representations from management. Where possible, these should include quantification of the issues identified.

Date of and period(s) covered by written representations

56.49 The date of and period(s) covered by written representations are dealt with in paragraph 14 of ISA (UK) 580 (Updated May 2022) and the related application guidance.

56.50 On the day that the accounts are submitted to the C&AG for certification, the Engagement Director or Engagement Manager must contact a responsible officer of the audited entity to confirm that:

- the Letter of Representations remains valid; and
- no event(s) have occurred since it was signed which would impact on the representations provided.

56.51 The Letter of Representation should cover both group and entity-only accounts.

Form of written representations

56.52 In accordance with paragraph 15 of ISA (UK) 580 (Updated May 2022), the engagement team should ensure that management makes its representations in a letter addressed to the C&AG. An NAO standard template for the Letter of Representation is available.

Problems with written representations

56.53 ***Consultation required*** Paragraphs 16 to 20 of ISA (UK) 580 (Updated May 2022) deal with the situation where management does not provide one or more of the requested representations and/or there are doubts about the integrity of management such that the written representations are not reliable and/or written representations are inconsistent with other audit evidence. In these circumstances, the engagement team should consult FAPQ.

Communication with management and those charged with governance

56.54 The engagement team should communicate to those charged with governance the written representations that are being requested, prior to their approval of the financial statements.

56.55 Where there is an Accounting Officer, assisted by an audit committee, this is done by providing a copy of the draft Letter of Representation in our Audit Completion Report, which is addressed to the Accounting Officer and the audit committee. The Accounting Officer should sign the final letter. Any changes between the draft and final letters should be highlighted to the Accounting Officer before they sign.

56.56 Where there is not an Accounting Officer, a copy of the draft Letter of Representation should be provided to the audit committee in our Audit Completion Report. A member of the Board should

sign the final letter. If there are changes between the draft and final letters the engagement team should consider whether to communicate these to those charged with governance, or whether it is sufficient to highlight them to the board member before they sign.

Chapter 57: Reporting to those charged with governance

Relevant standards and guidance

57.1 ISA (UK) 260 (Revised November 2019) (Updated May 2022) *Communication with those charged with governance* deals with the auditor's responsibility to communicate with those charged with governance in an audit of financial statements. The objectives of the auditor under ISA (UK) 260 (Revised November 2019) (Updated May 2022) are:

- to communicate clearly with those charged with governance the responsibilities of the auditor in relation to the financial statement audit, and an overview of the planned scope and timing of the audit;
- to obtain from those charged with governance information relevant to the audit;
- to provide those charged with governance with timely observations arising from the audit that are significant and relevant to their responsibility to oversee the financial reporting process; and
- to promote effective two-way communication between the auditor and those charged with governance.

57.2 Appendix 1 to ISA (UK) 260 (Revised November 2019) (Updated May 2022) lists specific requirements inISAs (UK) that refer to communications with those charged with governance.

57.3 Paragraphs 1-61 to 1-71 of Practice Note 10 (Revised 2022) *Audit of financial statements of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 260 (Revised November 2019) (Updated January 2020) in the public sector.

57.4 ISA (UK) 265 (Updated May 2022) *Communicating deficiencies in internal control to those charged with governance and management* deals with the auditor's responsibility to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditor has identified in an audit of financial statements. The objective of the auditor under ISA (UK) 265 (Updated May 2022) is to communicate appropriately to those charged with governance and management deficiencies in internal control that the auditor has identified during the audit and that, in the auditor's professional judgement, are of sufficient importance to merit their respective attentions.

Background

57.5 Paragraph 10(a) of ISA (UK) 260 (Revised November 2019) (Updated May 2022) defines "those charged with governance" as the person(s) or organisation(s) with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity. This includes overseeing the financial reporting process. For some entities in some jurisdictions, those charged with governance may include management personnel, for example, executive members of a governance board of a private or public sector entity, or an owner-manager. In the UK, those charged with governance include the directors (executive and non-executive) of a company and the members of an audit committee where one exists. For other types of entity it usually includes equivalent persons such as the partners, proprietors, committee of management or trustees.

57.6 For NAO-audited central government departments, agencies and arm's-length bodies, those charged with governance are generally the members of the audit committee or equivalent.

57.7 Communication with those charged with governance is an important element of fulfilling the engagement team's responsibilities in an audit. Effective two-way communications assists:

- the engagement team and those charged with governance in understanding matters related to the audit in context, and in developing a constructive working relationship; and
- the engagement team in obtaining information relevant to the audit from those charged with governance. For example, those charged with governance may assist the NAO in understanding the entity and its environment, in identifying appropriate sources of audit evidence, and in providing information about specific transactions or events; and
- those charged with governance in fulfilling their responsibility to oversee the financial reporting process, thereby reducing the risks of material misstatement of the financial statements.

57.8 Communications will usually involve:

- inquiries at the planning phase of the audit to identify risks;
- reporting of our planned audit approach;
- discussion and reporting of issues through the audit;
- reporting and discussion of our findings, the principal issues and judgements at the completion of our audit; and
- reporting and discussion of control deficiencies identified at each stage of the audit.

57.9 This Chapter sets out the specific matters which need to be communicated with those charged with governance, including communicating deficiencies in internal control.

Identifying those charged with governance and communication with a subgroup

57.10 The engagement team should determine who are "those charged with governance" by reference to the persons or organisations with responsibility for overseeing the strategic direction of the entity and obligations related to the accountability of the entity, including overseeing the financial reporting process.

57.11 In accordance with paragraph 11 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), the engagement team should determine the appropriate person(s) within the entity's governance structure with whom to communicate. This is normally the entity's audit committee, as a subcommittee of the board.

57.12 If issues are communicated to a subgroup of those charged with governance, for example an audit committee or an individual, paragraph 12 of ISA (UK) 260 (Revised November 2019) (Updated May 2022) requires the engagement team to determine whether it is necessary to communicate to other members of those charged with governance. Where there is an effective audit committee and governance structure in place, this will not be necessary unless the issues identified are particularly significant. Further guidance is provided in paragraphs A5 to A7 of ISA (UK) 260 (Revised November 2019) (Updated May 2022).

57.13 Audit committees report to the board on various matters related to the discharge of their responsibilities, including those related to the financial statements, the annual report and the audit process. The engagement team, when assessing whether there is a need to communicate with the full board regarding matters communicated by the engagement team to the audit committee, should take into consideration the adequacy of the communications between the audit committee and the board, including whether they appropriately address relevant matters communicated to the audit committee by the engagement team.

57.14 Although rare in a public sector context, all of those charged with governance may be sometimes involved in managing the audited entity. Where this is the case, in accordance with paragraphs 13 and A8 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), the engagement team may fulfil some of the requirements to report to those charged with governance through discussions with them in their management role. However, the engagement team still need to be satisfied that this communication adequately informs all of those with whom the engagement team would otherwise communicate in their governance capacity. For example, if an entity has a chief executive and a finance director, communication of an issue with the finance director may not suffice to fulfil our obligations.

57.15 ***Table 57A*** below summarises who will usually make up management and those charged with governance for most of the NAO's audited entities and with whom the engagement team would normally communicate.

Table 57A: Make-up of management and those charged with governance in most NAO-audited entities

	Public bodies	Companies
Management	Senior management (including members of the board, but not including non-executive board members).	Executive directors and other senior management.
Those charged with governance	The Accounting Officer, supported by an audit committee. The latter will usually include the non-executives on the Board.	The Board as a whole, with the role typically delegated to an audit committee. The latter will usually include the non-executives on the Board. Only formally includes the Accounting Officer if the AO is a director.

Reporting to those charged with governance – planning

57.16 As required by paragraph 15 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), the engagement team should communicate with those charged with governance an overview of the planned scope and timing of the audit. The following are relevant matters to communicate;

- how the engagement team proposes to address the significant risks of material misstatement
- (for engagements where an Extended Auditor Report is expected to be issued) the Key Audit Matters identified by the engagement team at the planning stage in accordance with ISA (UK) 701 (Revised November 2019) (Updated May 2022), or else a confirmation that the significant risks reported constitute the entirety of the Key Audit Matters to be considered during the course of the audit;
- the engagement team's approach to internal control;
- the concept of materiality in the context of an audit;
- the engagement team's approach to the use of the work of internal audit;
- matters those charged with governance consider may influence the audit of the financial statements;
- the attitudes, awareness, and actions of those charged with governance concerning the entity's internal control and the detection of possibility of fraud;
- the nature and extent of specialised skill or knowledge needed to perform the planned audit procedures or evaluate the audit results, including any use of an auditor's expert;
- the planning inquiries that are required to be made of those charged with governance;
- the actions of those charged with governance in response to developments in accounting standards, corporate governance practices and related matters;
- the responses of those charged with governance to previous communications with the auditor;

- details of the planned timing of audit work; and
- where the engagement team anticipates limitations being placed upon their work, including limitations imposed by management, these limitations should be reported at the planning stage.

57.17 For group audits, communications with those charged with governance are discussed in ***Table 25P*** in Chapter 25: Group audit procedures.

57.18 It is NAO policy to communicate the planned scope and timing of the audit through an Audit Planning Report to those charged with governance. To fulfil the requirements of paragraph 15 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), reporting to those charged with governance on key audit matters, incorporating communication about the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditor, including those that had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team, is included in the template Audit Completion Report.

57.19 The engagement team's responsibilities in relation to an audit of financial statements should be included in the Letter of Understanding or Letter of Engagement, which records the agreed terms of the engagement. Providing a copy to the audit committee can be an appropriate way to communicate with those charged with governance regarding the auditor's responsibilities.

57.20 As stated in paragraph A13-1 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), the nature and detail of the planning information communicated to those charged with governance reflects the size and nature of the entity and the manner in which those charged with governance operate. It is expected that teams will tailor their Audit Planning Reports on this premise.

57.21 The engagement team should take care when communicating with those charged with governance about the planned scope and timing of the audit not to compromise the effectiveness of the audit. For example, communicating the nature and timing of detailed audit procedures may reduce the effectiveness of those procedures by making them too predictable.

Reporting to those charged with governance – the communication process

57.22 The engagement team should communicate the planned form, timing and expected general content of communications for all initial engagements, and as engagement teams deem required thereafter. Effective communication may require structured presentations and written reports, as well as less structured communications, including discussions.

57.23 In addition to the significance of a particular matter, the form of communication may be affected by such factors as those listed in paragraph A47 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), as well as the evaluation of the adequacy of the communication process between the NAO and those charged with governance for the purpose of the audit.

57.24 As far as appropriate, teams should provide summarised information in their reports to allow focus on the key message. Further information can be provided to the audit committee orally, as necessary. Factors for the Engagement Director to consider when evaluating the adequacy of communications with those charged with governance include the examples given in paragraph A51 of ISA (UK) 260 (Revised November 2019) (Updated May 2022).

57.25 As set out in paragraph 7 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), in some circumstances, law or regulation may restrict the auditor's communication of certain matters with those charged with governance. Law or regulation may specifically prohibit a communication, or

other action, that might prejudice an investigation by an appropriate authority into an actual, or suspected, illegal act, including alerting the entity. In these circumstances, the issues considered by the engagement team may be complex and it may be necessary to consult with FAPQ and obtain legal advice.

57.26 Inadequate two-way communication may indicate an unsatisfactory control environment and influence the engagement team's assessment of the risks of material misstatement. There is also a risk that sufficient appropriate audit evidence may not have been obtained to form an opinion on the financial statements. Where the engagement team finds the two-way communication to be inadequate, they should revisit their assessment in the Understanding the Entity's Information Systems and Communications template of the audited entity's communication and, as appropriate, update the risk assessment and response plan in the Risk Assessment in Apex and the Regularity Testing Plan.

57.27 Good communication is an essential feature of all NAO audits, which helps to drive improvement in public services through positive change in the audited entity's financial management and accounting. Improvements in control processes can also drive future audit efficiencies.

57.28 Effective two-way communication with those charged with governance can help the NAO to obtain assurance over key judgements and assist audit committees in holding management to account.

57.29 Timely, effective communication of control deficiencies is also an important part of our audit. Engagement team members should consider carefully as the audit progresses whether they have identified any areas for improvement in the entity's controls.

57.30 The engagement team should, therefore, consider how best to communicate their findings. In particular for complex issues, they may need to consider how to summarise and present the issue in a way that enables an effective dialogue with the audit committee.

57.31 Engagement teams may find it useful to discuss the best approach for communicating issues with other teams, who have reported similar issues in the past, and with FAPQ.

57.32 The Engagement Manager and Engagement Director will typically be closely involved in considering how best to communicate the principal points identified and assessing how these impact upon our consideration of the Governance Statement.

57.33 The appropriate timing for communications depends upon the issues identified and the expectations of those charged with governance. The engagement team should communicate significant findings relevant to the financial statements prior to their approval. If significant findings are communicated at a stage where a number of items remain outstanding, the engagement team should confirm the following to those charged with governance prior to approval of the financial statements:

- whether or not any further matters have arisen, including any further unadjusted errors, and
- that all outstanding matters have been completed.

57.34 Where communications are made orally, the engagement team should include on the audit file the matters communicated, with whom they were communicated and the time of the communication. This may be in the form of a copy of audited entity-prepared minutes, if they are an appropriate record of the discussion.

57.35 If the Engagement Director deems the two-way communication inadequate and the situation cannot be resolved, the engagement team may consult FAPQ. Possible responses include:

- modifying the C&AG's opinion on the basis of a limitation of scope;
- obtaining legal advice about the consequences of different courses of actions;
- communication with higher authorities in the governance structure that are outside the entity, such as the sponsoring department of to Parliament; and/or
- withdrawing from the engagement, where withdrawal is possible.

Reporting to those charged with governance – early communication

57.36 The purpose of early communication with those charged with governance regarding potential modifications to the C&AG's opinion is to:

- give advance notification of the reasons or circumstances for the modification;
- agree the facts of the matter leading to the modification or confirm those matters over which there is disagreement; and
- provide those charged with governance with an opportunity to provide further information and explanations.

Reporting to those charged with governance – significant matters arising during the audit

57.37 Other than the examples given in paragraph A22 of ISA (UK) 260 (Revised November 2019) (Updated May 2022), significant matters may include material misstatements of fact or material inconsistencies in information accompanying the audited financial statements that have been corrected.

Reporting to those charged with governance – proposed wording of the auditor's report

57.38 The proposed form of wording of the auditor's report should be included in the Audit Completion Report. This requirement should not preclude the engagement team from communicating with those charged with governance on a timely basis where there is a gap between the identification of issues which may lead to a modification of the opinion, or Emphasis of Matter paragraph, and the completion of the audit.

Reporting to those charged with governance – significant findings

57.39 In most cases, the significant findings required to be communicated by paragraph 16 of ISA (UK) 260 (Revised November 2019) (Updated May 2022) will be communicated through an Audit Completion Report. Where appropriate, the engagement team should provide additional interim update reports.

57.40 The engagement team should communicate the audit risks that were given special audit consideration, even when the results of our work indicated that these are no longer significant risks.

57.41 The engagement team should communicate all corrected and uncorrected misstatements or irregularities, including extrapolated figures and excluding those that are clearly trivial.

57.42 Where necessary, the engagement team should request further information from those charged with governance when communicating our findings to those charged with governance. For example, the engagement team should confirm that they have the same understanding of the facts and circumstances relevant to specific transactions or events that have given rise to significant issues.

57.43 The engagement team should include in the Audit Completion Report our views about significant qualitative aspects of the entity's accounting practices, including accounting policies, accounting estimates and financial statement disclosures. Appendix 2 to ISA (UK) 260 (Revised November 2019) (Updated May 2022) identifies relevant examples.

57.44 The engagement team should communicate significant findings from the audit:

- after the Engagement Director has evidenced their review of audit procedures undertaken in respect of all significant risks
- after the Engagement Director has evidenced their review of all key audit judgements; and
- prior to the approval of the financial statements.

Reporting to those charged with governance – significant difficulties

57.45 In certain circumstances, significant difficulties represent a limitation of scope on our audit, requiring a modification to our audit opinion. Where a significant difficulty arises, the engagement team should document clearly how this has been resolved.

57.46 Significant difficulties encountered during the audit normally constitute a significant documentation matter. Documentation of these matters should enable an experienced auditor, having no previous connection with the audit, to:

- understand the issues;
- understand the conclusions reached; and
- understand any significant professional judgements made in reaching those conclusions.

Reporting to those charged with governance – key audit matters

57.47 Where an Extended Auditor Report is prepared for the entity, in accordance with paragraphs 17 and A9-1 of ISA (UK) 701 (Revised November 2019) (Updated May 2022) *Communicating key audit matters in the independent auditor's report*, the key audit matters disclosed within that report should also be reported to those charged with governance (or the determination that there are no key audit matters to communicate). This reporting should be consistent with the reporting in the extended auditor report.

Reporting to those charged with governance – auditor independence

57.48 The communication required by paragraph 17 of ISA (UK) 260 (Revised November 2019) (Updated May 2022) is required for listed entities, but paragraph A32 notes that this may also be appropriate in the case of some other entities, including those that may be of significant public interest. NAO policy is to include these communications for all NAO-audited entities.

57.49 For group audits, the statement required by paragraph 17(a) of ISA (UK) 260 (Revised November 2019) (Updated May 2022) should extend to component auditors within the group.

57.50 The communication required by paragraph 17(b)(i) of ISA (UK) 260 (Revised November 2019) (Updated May 2022) should additionally cover any assistance which the NAO has provided, or will provide, that might present a self-review threat.

Reporting to those charged with governance – control deficiencies

57.51 ISA (UK) 265 (Updated May 2022) includes requirements to communicate significant deficiencies in internal control to those charged with governance.

57.52 In addition to the definition in paragraph 6(a) of ISA (UK) 265 (Updated May 2022), NAO engagement teams should treat as a deficiency in internal control a situation where controls required under legislation are either deficient or missing.

57.53 Paragraphs A5 to A11 of ISA (UK) 265 (Updated May 2022) include application guidance on determining whether control deficiencies are significant. In addition to the examples given, the engagement team should consider susceptibility to irregular transactions.

57.54 Significant deficiencies in internal control may become apparent to the engagement team following the identification of material misstatements, material irregular transactions, material disclosure deficiencies, and any absence of controls to address a significant risk.

57.55 Where significant deficiencies have been communicated orally to management or those charged with governance, they should still be communicated in writing or else a note of the meeting or discussion where the communication occurred should be retained on the audit file as evidence that the matter has been communicated.

57.56 The engagement team should, prior to the approval of the financial statements, communicate to those charged with governance in the Audit Completion Report any significant deficiencies in internal control.

57.57 Where it is impracticable to report on significant deficiencies in writing before the issue of the financial statements, the engagement team should report orally to those charged with governance before the date of the audit report and document this.

57.58 Where significant deficiencies identified in prior years have not been remedied, the engagement team should re-communicate the issue, either by repeating the description from the previous communication or by referencing the previous communication. The engagement team should ask management or those charged with governance why the significant deficiency has not been remedied.

57.59 Failure to act, in the absence of an explanation, may represent a significant deficiency in itself. In some circumstances, a significant deficiency may be of sufficient severity that the C&AG reports to Parliament (further guidance is included in Chapter 58: Reporting to Parliament).

57.60 The engagement team may communicate non-significant deficiencies in writing through a Management Letter or equivalent communication. This will include (as applicable):

- a follow-up on points raised in the previous year;
- details of relevant control deficiencies identified in our audit work and suggestions for the improvement to the design and operation of the accounting and internal control systems;
- constructive advice on ways to improve the economy, efficiency and effectiveness of the entity;
- details of non-compliance with the requirements of regularity and propriety and, as appropriate, Managing Public Money or other relevant guidance;
- details of non-compliance with financial requirements set out in a framework document governing the operations of the audited entity; and
- communication on any other relevant matters.

57.61 Where a separate Management Letter is issued, the team must take care to ensure that all information required to be reported to those charged with governance under ISA (UK) 260 (Revised November 2019) (Updated May 2022) and ISA (UK) 265 (Updated May 2022) is included in the Audit Completion Report issued to those charged with governance prior to certification.

57.62 Before issuing a final version of the Management Letter (or equivalent communication), which is normally sent to the Accounting Officer and audit committee, the engagement team should issue and agree a draft with the audited entity 's senior financial officer and obtain responses to the points raised. It is effective practice to raise the points identified with the audited entity on an on-going basis during the course of the audit and to obtain their responses as the audit progresses. The final Management Letter issued to the audited entity should incorporate the audited entity's responses.

57.63 Certain identified significant deficiencies in internal control may call into question the integrity or competence of management. For example, there may be evidence of fraud, irregular transactions or intentional non-compliance with laws and regulations by management, or management may exhibit an inability to oversee the preparation of adequate financial statements that may raise doubt about management's competence. Accordingly, it may not be appropriate to communicate such deficiencies directly to management. The engagement team should consider the requirements of ISA (UK) 250A (Revised November 2019) (Updated May 2022) *Consideration of laws and regulations in an audit of financial statements*, ISA (UK) 240 (Revised May 2021) (Updated May 2022) *The auditor's responsibilities relating to fraud in an audit of financial statements* and Part 2 of Practice Note 10 (Revised 2022) on the audit of regularity. The engagement team may consult with FAPQ in these circumstances.

57.64 In deciding whether a control deficiency has been identified it will usually be appropriate to discuss the relevant facts and circumstances of our findings with an appropriate level of management. This discussion provides an opportunity to alert management on a timely basis to the existence of deficiencies of which management may not have been previously aware.

57.65 The appropriate level of management is one that is familiar with the internal control area concerned and that has the authority to take remedial action on any identified deficiencies in internal control. For example, minor issues in Accounts Payable might be discussed with the Accounts Payable supervisor or the Financial Controller.

57.66 As set out in paragraph A20 of ISA (UK) 265 (Updated May 2022), in some circumstances, it may not be appropriate to discuss audit findings directly with management, such as if the findings appear to call management's integrity or competence into question.

57.67 In discussing findings with management, the engagement team may obtain other relevant information for further consideration, such as:

- management's understanding of the actual or suspected causes of the deficiencies;
- exceptions arising from the deficiencies that management may have noted, for example, misstatements that were not prevented by the relevant IT controls; and/or
- a preliminary indication from management of its response to the findings.

57.68 The engagement team should communicate relevant control deficiencies identified to colleagues within the Group. This should enable teams to identify where follow-up work, outside of the financial audit job and budget, may be appropriate.

57.69 The engagement team should consider whether control deficiencies are indicative of issues relevant to our strategic themes and how best to communicate these issues to help identify areas for cross-cutting work.

57.70 When communicating deficiencies in internal control, the engagement team should include in the written communication:

- a description of the deficiencies and an explanation of their potential effects;
- sufficient information to enable those charged with governance and management to understand the context of the communication, in particular that;
    - the purpose of the audit was for the C&AG to express an opinion on the financial statements;
    - the audit included consideration of internal control relevant to the preparation for the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and
    - the matters being reported are limited to those deficiencies that have been identified during the audit and that the engagement team has concluded are of sufficient importance to merit being reported to those charged with governance; and
- a statement that the communication has been provided for the purposes of, as appropriate, management or those charged with governance and that it may not be suitable for other purposes.

57.71 A statement might be included that, if the engagement team had performed more extensive procedures on internal control, they might have identified more deficiencies to be reported, or concluded that some of the reported deficiencies need not, in fact, have been reported.

57.72 The engagement team should include in written communication of significant control deficiencies to management:

- suggestions for remedial action on the deficiencies;
- management's actual or proposed responses to the deficiencies; and
- a statement as to whether or not any steps have been undertaken to verify whether management's responses have been effective.

Reporting to those charged with governance – reporting of matters beyond the scope of auditor's responsibilities under ISAs (UK)

57.73 The NAO's audit procedures and responses are designed solely to comply with ISAs (UK) and to address the C&AG's other statutory responsibilities. In doing so, the engagement team may identify matters to report which extend beyond the normal requirements of the ISAs (UK). In such circumstances, where the engagement team wishes to report either publicly (for example, with a C&AG's Report) or privately (for example, in a communication to the Accounting Officer or those charged with governance), the engagement team may wish to perform additional procedures to support such reporting by exception. However, where the engagement team performs such additional procedures, these procedures are performed optionally and not in order to comply with the requirements of the ISAs (UK).

Other considerations

57.74 The engagement team should communicate regularity-related issues, including control deficiencies relating to the regularity of transactions, in the same way as other required communications. The potential for material irregular transactions due to a control deficiency may indicate that it is a significant deficiency.

57.75 The engagement team should communicate IT-related issues, including IT control deficiencies, in the same way as other required communications.

57.76 The engagement team should use the standard templates when preparing the Audit Planning Report, Audit Completion Report and any separate Management Letter.

57.77 The Engagement Director should ensure that all significant matters arising have been identified for communicating to those charged with governance.

57.78 The engagement team should include a copy of all written communications with those charged with governance, including the Audit Completion Report and Management Letter, on the audit file. If a Management Letter is issued after the file closure period, the engagement team should not re-open the Apex audit file but should instead store the Management Letter in an appropriate folder on Sharepoint.

Additional matters to be communicated with those charged with governance for entities which are required, and those that choose voluntarily to report on how they have complied with, the UK Corporate Governance Code

57.79 Paragraphs 16-1 and A28-1 to A28-4 of ISA (UK) 260 (Revised November 2019) (Updated May 2022) set out information that the auditor is required to communicate to the audit committee in the case of entities that are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code.

57.80 For entities which are required, and those that choose voluntarily, to report on how they have applied the UK Corporate Governance Code, the responsibilities of the directors under Code provision 27 include making a statement that they consider the annual report and accounts taken as a whole is fair, balanced and understandable and provides the information necessary for shareholders to assess the entity's position, and performance, business model and strategy.

57.81 The responsibilities of the audit committee under Code provision 25 include, where requested by the board, providing advice in relation to that statement. The responsibilities of the board under Code provision 29 include monitoring the entity's risk management and internal control systems and, at least annually, carrying out a review of their effectiveness and reporting on that review in the annual report.

57.82 The responsibilities of the board under Code provisions 28 and 31 include:

- Providing a robust assessment of the emerging and principal risks facing the entity. The board should confirm in the annual report that it has completed this assessment, including a description of its principal risks, what procedures are in place to identify emerging risks, and an explanation of how these are being managed or mitigated.
- Providing an explanation in the annual report as to how they have assessed the prospects of the entity, over what period they have done so and why they consider that period to be appropriate.

57.83 The responsibilities of the audit committee under Code provision 25 include:

- monitoring the integrity of the financial statements of the entity and any formal announcements relating to the entity's financial performance, reviewing significant financial reporting judgments contained in them;

- reviewing the entity's internal financial controls and internal control and risk management systems, unless expressly addressed by a separate board risk committee composed of independent non-executive directors or by the board itself; and
- reporting to the board on how it has discharged its responsibilities.

57.84 In fulfilling these responsibilities, the audit committee and the board will be assisted by an understanding of issues that involve significant judgment and other matters communicated to them by the engagement team relevant to those responsibilities.

57.85 This will include an understanding of the rationale and supporting evidence for the significant professional judgments made in the course of the audit and in reaching the opinion on the financial statements, and of other matters communicated to the audit committee by the engagement team as set out above.

57.86 The engagement team's communications should include information regarding separate components of a group where relevant.

Chapter 58: Reporting to Parliament

Printing and publication

58.1 Chapter 22: Finalise, close and destroy audit file includes guidance relating to situations where the NAO is responsible for printing, publishing and/or laying the accounts.

C&AG's reports

58.2 Where the opinion on the financial statements is qualified, a C&AG's report will normally be presented. A separate report will nearly always be required where:

- a scope limitation is so pervasive as to necessitate a disclaimer of opinion;
- a disagreement is so fundamental as to lead to an adverse opinion;
- a Parliamentary control total has been exceeded on a resource account; and/or
- the qualification is in respect of another material irregularity.

58.3 ***Consultation required*** Where the C&AG issues a qualified opinion for reasons other than those above, the Engagement Director, in consultation with the Director, Audit Quality and the Audit Panel, will make recommendations to the C&AG on whether a separate report is necessary.

58.4 The C&AG may also issue reports with financial statements when the opinion is not qualified. The Engagement Director will be concerned with matters which have arisen during the course of the audit which although not material to the opinion are of sufficient importance to draw to the attention of Parliament.

58.5 All C&AG's reports should be approved by Director, Audit Quality and then the C&AG before being sent to the entity's Accounting Officer. This "clearance" process with the Accounting Officer will ensure that:

- all material and relevant facts have been included;
- the facts are not in dispute;
- the presentation and conclusions drawn from the facts are fair;
- the report distinguishes clearly between the facts and the conclusions drawn from them; and
- any disagreement with the conclusions on the part of the Accounting Officer are properly presented.

58.6 Draft reports that refer to third parties should be cleared at an appropriate level with the organisation or person concerned. When the C&AG will issue a report with the financial statements the engagement team should allow sufficient time within certification schedule.

58.7 The C&AG has wide ranging powers to report to Parliament. Such powers to report should be used to draw to the attention of Parliament matters which are necessary for the understanding of the financial statements or the entity's stewardship of public funds. It may also be used where there are other significant matters associated with the financial statements which he believes should be brought to Parliament's attention, even in circumstances where his opinion has not been qualified.

58.8 Where a scope limitation is so pervasive as to necessitate a disclaimer of opinion or a disagreement is so fundamental as to lead to an adverse opinion, it suggests either a fundamental breakdown in control or disagreement on a matter which could render the financial statements totally misleading. In either case Parliament would expect a detailed explanation beyond that which could be given in the certificate and which could form the basis of a hearing by the Committee of Public Accounts.

58.9 Where a Parliamentary control total has been exceeded on a resource account, there will have been a breach of Parliamentary control and, regardless of the amounts involved, Parliament will wish to be informed of the background and reasons. Further guidance is available in the section in this Chapter entitled 'Reports on excess votes'.

58.10 Similarly, with the qualification is in respect of another material irregularity, there will have been a breach of Parliamentary control and Parliament will wish to be informed as to the nature of the breach, the reasons for this and the action taken by the entity to prevent a re-occurrence. The principles underlying the irregularity may also have a wider impact on the central government sector.

58.11 Historically C&AG's reports on unqualified financial statements have normally fallen into one of the following categories:

- Lifting of prior year qualification – where the C&AG has qualified his opinion on the financial statements in the previous year but the qualification has been removed, the C&AG issues a report to explain why this is the case.
- Improprieties – although propriety is not expressly covered in the audit opinion, Parliament has clear expectations as to the way in which public business should be conducted. Significant improprieties which could be covered in a separate report might include matters such as a failure to make a proper distinction between private and public business, failure to demonstrate fair competition in the appointment of staff or the letting of contracts, and extravagant hospitality or expenses.
- Inadequate financial control – the C&AG is not required to give an opinion on financial control but would be expected to draw to the attention of Parliament control weaknesses which placed public funds at significant risk either through fraud or error.

58.12 However, the ability of the C&AG to report is not limited to these circumstances. The C&AG may wish to report other matters that may be of interest to Parliament and other users of the accounts, including (but not limited to) analysis and interpretation of the financial statements and matters that would be required to be included in an auditor's report under ISA (UK) 700 (Revised November 2019) (Updated May 2022) *Forming an opinion and reporting on financial statements* if the entity were listed.

58.13 ***Consultation required*** Each C&AG's report will need to be tailored to the circumstances of each case, and so a standard pro-forma is not given. FAPQ reviews all draft reports prior to submission to the C&AG and should be provided with an early draft.

58.14 'Parliamentary privilege' is the term commonly accorded to the legal protection afforded to proceedings in Parliament. Article IX of the Bill of Rights 1688 prevents proceedings in Parliament from being 'impeached or questioned' in any court or place out of Parliament. The C&AG's reports are ordered to be printed by the House of Commons and are thus considered 'proceedings in Parliament' and attract Parliamentary privilege.

58.15 'Qualified Privilege' arises when a statement is made under a properly exercised (free of improper motive or malice) privilege in the performance of a legal or moral right or duty. The concept of this type of qualified privilege has its origins in common law and is distinct from the Parliamentary privilege. The principle underlining qualified privilege is that it is in the public interest that persons should be allowed to speak freely on occasions when it is their duty to do so.

58.16 Essentially, Parliamentary privilege confers absolute immunity whereas qualified privilege protects the maker of a defamatory statement only if the maker acted honestly and without malice.

The Legal and Policy team is able to advise on more detailed issues relating to privilege, for example correspondence and issues arising in draft reports.

58.17 In respect of sub-judice matters (matters awaiting judgement in the Courts), there is a long-standing rule of the House of Commons that they should not impede the Courts by referring to matters which are sub-judice. The C&AG's reports are not covered by such guidelines. Nevertheless, the engagement team needs to be aware of the risk that references in the C&AG's reports to matters which are subject to legal action could prejudice the fair trial of those involved. In making judgements about the degree of disclosure engagement teams will need to strike a balance between the risk of prejudicing any legal proceedings and the concern that the NAO do not appear to be holding back information unnecessarily from either Parliament or the public. An agreed report properly scoped which deals in undisputed facts should not present a risk to legal proceedings.

58.18 Qualified accounts will usually have a press notice, and the Press Office should be informed of all accounts which will be qualified. The decision on whether to have a press notice is usually taken by the engagement team in consultation with the Press Office and depends on factors including the reasons for the qualification and the profile of the audited entity. Where a press notice is deemed necessary, the Press Office draw up a communications plan and draft a press notice for the engagement team's approval. The press notice should subsequently be cleared by the engagement team with the Accounting Officer. The cleared press notice is then issued to the media by the Press Office, along with the report on accounts.

58.19 Some unqualified accounts will also attract a press notice, depending on the profile of the audited entity and the expected level of interest in issues raised in the report, with the decision taken by the team in consultation with the Press Office. The communications plan and press notice are put together as for qualified accounts.

58.20 The Press Office will draft press notices and discuss these with the engagement team. They will need early sight of draft reports on accounts in order to perform their role.

Reports on excess votes

58.21 A C&AG's report on an excess vote will set out the details and reasons for the excess vote and any departmental actions proposed or taken. The Department is required to explain the excess as part of its 'explanation of variations' on the Statement of Outturn against Parliamentary Supply of the financial statements and refer to it in the annual report. The Department should be encouraged to make full disclosure, which may be made in the Governance Statement and a note to the accounts to support the more limited explanation on the Statement of Outturn against Parliamentary Supply. Appropriate references to this should be made in the report by the C&AG.

58.22 As well as providing Parliament with an explanation of excesses on individual accounts, the C&AG's reports on those accounts form the basis for a submission to, and examination by, the Committee of Public Accounts (PAC) as part of Parliament's processes for authorising the excesses. Following this examination, the PAC publishes a report covering each of the excess votes arising in year.

58.23 There is a statutory requirement each year for Parliament to be notified of resources and cash expended by departments in excess of the approved limits set out in the Supplementary Estimates. This is done by way of an annual Statement of Excesses, prepared and laid by Treasury following the publication of the corresponding PAC report. House Standing Orders provide that if the Committee raises no objection to the excesses, the motion to authorise their making good is taken

without debate. The Committee's scrutiny therefore represents an important function on behalf of Parliament.

58.24 The C&AG's reports provide information necessary for HM Treasury to prepare its Statement of Excesses, on which the House votes approval. For these reasons it is important that sufficient, accurate information is provided. The C&AG's reports on accounts are available to the PAC; hence it is desirable to ensure consistency of structure and analysis across these reports. Engagement teams should follow the structure of similar recent reports unless advised by FAPQ to do otherwise.

Chapter 59: Reporting to the devolved legislatures and in other UK languages

Relevant standards and guidance

59.1 Paragraph 1-132 of Practice Note 10 (Revised 2022) *Audits of financial statements and regularity of public sector bodies in the United Kingdom* sets out that, in central government, the financial statements of most reporting entities are generally laid before: the House of Commons; the House of Lords; both of these Houses of Parliament; the Welsh Parliament (Senedd Cymru); the Northern Ireland Assembly or the Scottish Parliament.

Annual reports and accounts laid before the devolved legislatures

59.2 Legislation may provide that NAO-audited entities must lay their annual report and accounts before one of the devolved legislatures. For example, Section 88 of the Scotland Act 1998 requires any reports on cross-border bodies that are required to be laid before either or both Houses of Parliament to be laid also before the Scottish Parliament. The engagement team should establish whether a body on which they plan to issue a report is designated as cross-border.

59.3 The engagement team should address the audit certificate to the person or persons specified by statute or by the terms of engagement. This may include one of the devolved legislatures in addition to the UK Parliament.

Non-English language accounts and audit certificates

59.4 In some parts of the UK, English is not the primary language used by public bodies for the conduct of business including preparation of the accounts (for example, as a result of applying options available under the Welsh Language Act 1993 and Welsh Language (Wales) Measure 2011).

59.5 Where this occurs, the engagement team should ensure that the auditor's responsibilities under auditing standards can be properly discharged through, for example, including staff with the appropriate language skills in the engagement team and the use of translation services.

The annual report is presented for audit solely in English but the audited entity translates the annual report and accounts and audit report into Welsh

59.6 Where the annual report and account is presented for audit solely in English and there is no legal requirement for the C&AG to report in Welsh or on the Welsh version of the annual report and account but the entity decides to translate the annual report and accounts into Welsh and includes the translated version of the audit certificate or report therein, the engagement team should:

- ***Consultation required*** contact FAPQ to arrange translation of the audit certificate and/or report; and
- include the following paragraph as a disclaimer on the Welsh translation of the annual report and accounts below the report and above the signature plate:

  Cyfieithiad Cymraeg
  Rwyf wedi ardystio ac adrodd ar y datganiadau ariannol hyn yn eu ffurf wreiddoil. Mae'r fersiwn hon yn gyfieithiad o'r fersiwn Saesneg wreiddiol. Mae [audited entity] *yn gyfrifol am gywirdeb y cyfieithiad hyn.*

The annual report is presented for audit in English and Welsh or legislation requires certification in Welsh

59.7 Where either:

- the audited entity provides the annual report and account for audit in both English and Welsh or only Welsh; or
- legislation explicitly requires the annual report and account to be laid or published in Welsh (regardless of whether or not there is a complementary requirement to lay or publish in English),

both the English and Welsh annual report and account must be certified simultaneously.

59.8 ***Consultation required*** The engagement team must also perform appropriate procedures over the translation and consult with FAPQ.

59.9 The requirement to certify, lay and/or publish the annual report and account in Welsh must be documented in the Engagement Risk Assessment Audit Form.

Chapter 60: Reporting to the members or shareholders of a company and filing with Companies House

Relevant standards and guidance

60.1 Chapter 3 of Part 16 of the Companies Act 2006 sets out the functions of the auditor of a company, including making the auditor's report on the company's annual accounts.

60.2 Guidance is available on gov.uk on filing accounts with Companies House.

Companies audit guidance

60.3 Further guidance on audits of companies is available in Chapter 42: Companies.

Concluding, reporting and filing for companies

60.4 When written representations are obtained from the Board, the Letter of Representation should be signed by a director on behalf of the Board or the company secretary.

60.5 For non-GRAA companies, the engagement team should present the audit opinion either to the company's members or shareholders in an Audit Report, not a 'Certificate and Report', in accordance with the requirements of the Companies Act. For companies limited by guarantee, the engagement team should present the report to the Members, as there are not shareholders; only present the report to the Members or Shareholders where the company is limited by shares, as the shareholders are also the members.

60.6 Where companies chose to apply the FReM, do not comment on any non-compliance with HM Treasury directions in the audit report as they are not statutory requirements.

60.7 If the company voluntarily prepares a Remuneration Report, the engagement team should add an additional bulleted paragraph to the audit opinion as follows:

- for companies that choose to prepare a Remuneration Report in accordance with the FReM: *"The audited part of the remuneration report has been properly prepared in accordance with the Government Financial Reporting Manual issued by HM Treasury"*; or
- for companies that choose to follow the Companies Act 2006*: "The part of the directors' remuneration report described as having been audited, has been prepared in accordance with the requirements of the Companies Act 2006 that would have applied if* [company name] *were a United Kingdom incorporated quoted company"*.

60.8 If a company prepares a Remuneration Report instead of the statutory note disclosures, the engagement team should confirm that:

- the Remuneration Report includes all of the required statutory disclosures, including any supplemental to the requirements of the FReM; and
- it is cross-referenced as appropriate from the financial statements.

60.9 Where the company has prepared a Remuneration Report in a separate document from the financial statements, the engagement team's responsibilities for auditing the Remuneration Report, where relevant, will continue to apply. In such circumstances, the auditor's report should continue to include the references to the Remuneration Report noted above.

60.10 Where the company has prepared a Remuneration Report in a separate document form the rest of the Annual Report and the opinion on that Remuneration Report is unmodified, the company should ensure that a reference is made to the auditor's report on the Annual Report as a whole within the separate Remuneration Report.

60.11 Where the auditor's opinion on a Remuneration Report which is published in a separate document from the financial statements is modified, the engagement team should ensure that the directors publish the relevant section of the auditor's report alongside the separate Remuneration Report. Where the directors refuse to do so, the engagement team should consider resigning or taking other appropriate action. All such circumstances may be referred to FAPQ.

60.12 If a company prepares a Governance Statement, no drafting modification to the standard company audit report is required. The engagement team should limit their work to that implied by the negative consistency paragraph before the opinion itself starting: "I read other information…".

60.13 There is no restriction on the ability to include an opinion on regularity in the audit report if this has been agreed as appropriate.

60.14 The relevant Companies Act director signs the audit report as Senior Statutory Auditor on behalf of the C&AG as the Statutory Auditor.

60.15 Companies Act directors have the following three options for signing the accounts electronically/ remotely:

- signature of the audit report is as normal following transmission of hard copy annual report and accounts in the post (or other courier service) between the Company and auditors; or
- the RI physically signs the audit report and scans it in, returning the signed version to the Company, making sure to copy in the company Secretary and any Directors who have signed the document; or
- the RI adds a signature to a pdf of the accounts which includes the Director's signature. This copy is then returned to the Company, making sure to copy in the company Secretary and any Directors who have signed the document.

60.16 For non-GRAA companies, statutory auditors, including the C&AG, may not issue a separate report on the accounts, for example in the event of a modification of the audit opinion. The engagement team should report such matters to management and those charged with governance by other means. The engagement team should not include a statement at the bottom of the audit report to the effect that the C&AG has no observations to make on the financial statements.

60.17 The engagement team should not mark-up any amendments to errors on the accounts which are to be filed in Companies House. Where errors are identified, the engagement team should request amended pages from the audited entity. The audited entity only needs to include the approved date and does not need to sign a new set of accounts with a different date, even when the signed page is amended. The engagement team should update the letter of representation to clear the amendment.

60.18 Prior to the audited entity filing the accounts with Companies House, where possible, the engagement team should compare the final audited accounts to version for filing. This comparison should ensure that the versions are consistent, that the document is of a sufficient quality to be read when scanned in and complies with Companies House filing requirements.

60.19 The engagement team should plan audit work so that it is completed well in advance of the Companies House filing deadline, which Companies House sets at nine months after the year-end. For bodies with a 31 March year-end, this would be 31 December. Public limited companies are required to file accounts within six months on the year-end.

60.20 The engagement team should agree with the audited entity the number of copies of accounts required for signature and retain the original signed version of the accounts. The C&AG has agreed to sign a maximum of 3 sets of accounts in the case of GRAA company audits.

60.21 The copy of the financial statements filed at Companies House no longer requires the auditor's signature. It remains good practice to file a signed copy as a check that the correct version is being filed.

60.22 Engagement teams should ensure that companies are aware of the Companies House requirements and deadlines for filed accounts. Where deadlines are missed, ensure that the relevant financial penalties are recognised as liabilities where applicable.

60.23 Where a conflict arises between a GRAA company's requirement to file accounts at Companies House or circulate them to an AGM, and the requirement to lay accounts before the House of Commons without causing 'discourtesy to the House', the engagement team should:

- discuss the potential conflicts with the audited entity in advance and conclude on a mutually agreeable timetable;
- where client relations and governance procedures are not jeopardised, delay certification, laying, filing and any other form of publication until the new Parliamentary session; and
- where this is not desirable, certify during recess and return the certified accounts to the audited entity, requesting that they limit distribution to the Board and the owner, with laying, filing and any other form of publication delayed until the new session.

60.24 Ensure that GRAA company audited entities are aware that, once the certified accounts are returned to the audited entity, they are responsible for any breach of Parliamentary protocol.

60.25 If any information comes to light between certification and laying that may have a material impact on the accounts or disclosures, consider the implications for the audit opinion.

60.26 ***Consultation required*** If the audited entity wishes to prepare revised financial statements, the engagement team should consult FAPQ to discuss the form of the C&AG's audit report.

60.27 The requirements for the signature of a company's accounts come from the Companies Act and are different to those for non-company audited entities. Under Section 414 of the Companies Act 2006, a company's annual accounts must be signed on behalf of the board by a director of the company and the signature must be on the company's balance sheet. Under Sections 414D, 419, 419A and 422 of the Act, a company's strategic report and director's report, any separate corporate governance statement and the directors' remuneration report must each be signed on behalf of the board by a director or the secretary of the company.

60.28 The Companies Act 2006 does not require the accounts and strategic report, directors' report, separate corporate governance statement and directors' remuneration report to all be signed on the same date or to be dated. However, the financial statements should disclose the date that the board authorised and approved the accounts, which may be different from the date the director signed them.

60.29 Requirements for filing accounts with Companies House, either online or on paper can be found on the gov.uk website. A guide to common reasons for accounts being rejected by Companies House is available here, along with guidance published by the ICAEW on:

- using electronic signatures; and
- which documents in annual accounts need a signature.

60.30 GRAA companies must also lay their accounts as House of Commons papers.

60.31 It is 'discourteous to the House' if accounts are published before laying and such a practice could result in the relevant minister having to write to the Speaker to apologise. No exception can be made for GRAA companies.

60.32 However, GRAA companies have obligations to distribute accounts under Companies House filing rules and, potentially due to requirements under the Articles of Association to submit audited accounts to the AGM. This could cause conflict with the protocols for laying accounts.

60.33 Copies of signed accounts, but not formally printed copies, may be provided to AGMs on the agreement that they are not submitted to Companies House until they have been laid and have an H/C number, and that they limit circulation to the entity and its owners. Once certified, accounts are live and could not be presented at an AGM or be filed without discourtesy to the House.

60.34 Non-GRAA companies may lay their accounts in the name of the relevant Minister, but there is no statutory basis for this and it must be done by Command Paper. Further guidance on this is available from the NAO's Publications section.

60.35 Should a company wish to issue revised financial statements, it must comply with the detailed regulations governing revised financial statements and directors' reports in Section 454 of the Companies Act. In summary:

- if a company has approved accounts which the directors consider did not comply with the requirements of the Companies Act, or if applicable Article 4 of the IAS regulation, the directors may prepare revised financial statements;
- if the accounts have been issued, the directors may only make amendments to correct the accounts for the aspects which did not comply with the Companies Act, or IAS regulation. More general changes are not permitted.

60.36 Therefore, after the date of issue of the financial statements, it is generally not possible to revise the financial statements to reflect subsequent events.

Chapter 61: Events after the auditor's report but before issue of the financial statements

Relevant standards and guidance

61.1 ISA (UK) 560 *Subsequent events* deals with the auditor's responsibilities relating to subsequent events in an audit of financial statements. Paragraphs 10 to 13 and the related application guidance include requirements relating to facts that become known to the auditor after the date of the auditor's report but before the date the financial statements are issued.

61.2 Paragraphs 1-120 to 1-141 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 560 in the public sector.

Background

61.3 "Subsequent events" are events (both favourable and unfavourable) occurring between the date of the financial statements i.e. the reporting date and the date of the C&AG's report, and facts that become known to the engagement team after the date of the C&AG's report.

61.4 Events and facts that become known prior to the certification of the financial statements may require adjustments to the financial statements or additional disclosures therein.

61.5 Although, in general, financial statements cannot be revised once they have been certified by the C&AG, the engagement team may still need to consider whether the C&AG has a responsibility to report to Parliament or take other actions if events or facts become known to him that would have required adjustment or disclosure in the financial statements if known before certification. This is a passive responsibility to respond if the engagement team become aware of issues, as opposed to the active responsibility to perform procedures to identify subsequent events up to the date of certification.

Determining the relevant dates

61.6 Paragraph 5(a) of ISA (UK) 560 defines the "date of the financial statements" as the date of the end of the latest period covered by the financial statements (i.e. the period-end date – for the majority of NAO-audited entities this is 31 March).

61.7 Paragraph 5(b) of ISA (UK) 560 defines the "date of approval of the financial statements" as the date on which all the statements that comprise the financial statements, including the related notes, have been prepared and those with the recognized authority have asserted that they have taken responsibility for those financial statements (for NAO-audited entities, this will usually be the date the Accounting Officer or other responsible officer of the client signs the annual report and accounts).

61.8 Paragraph 5(c) of ISA (UK) 560 defines the "date of the auditor's report" as the date the auditor dates the report on the financial statements in accordance with ISA (UK) 700 (Revised November 2019) (Updated May 2022). The C&AG's report cannot be dated earlier than the date that sufficient appropriate audit evidence has been obtained on which to base the C&AG's opinion on the financial statements and cannot be earlier than the date of approval of the financial statements.

61.9 Paragraph 5(d) of ISA (UK) 560 defines the "date the financial statements are issued" as the date that the auditor's report and audited financial statements are made available to third parties. Paragraph A5 of ISA (UK) 560 states that for public sector entities, the date the financial statements are issued may be the date the audited financial statements and the auditor's report thereon are presented to the legislature or otherwise made public.

61.10 Paragraph 1-131 of Practice Note 10 (Revised 2022) clarifies that the financial statements of central government entities where the financial statements are laid in one or both of the Houses of Parliament are considered to be issued on the date the financial statements are laid before the House(s), and correspondingly for financial statements laid in one of the devolved legislatures; it further states that where the financial statements are laid before multiple legislatures and the laying takes place on different dates, the financial statements are considered to be issued on the date of laying before the first legislature where the financial statements are laid. Further guidance is provided in the bullet points below:

- Where the NAO is responsible for printing the document containing the audited financial statements, this is the date they are dispatched to the Clerk of the House for laying before Parliament. This is normally the same date as the C&AG's report and certificate.
- Where the financial statements are laid before Parliament by the Secretary of State of the sponsoring department or by Treasury, or where the accounts are otherwise considered by an intermediate body before being laid before Parliament, this is the date of despatch by those charged with governance to the relevant body.
- For other audits, this will be the date at which the audited entity makes available to third parties (including their sponsoring department) a copy of the certified financial statements.

Respective responsibilities of the auditor and those charged with governance

61.11 Engagement teams should consider the effect of subsequent events on the financial statements and on the audit opinion.

61.12 Those charged with governance are responsible for the preparation of the financial statements, including compliance with the requirements of the financial reporting framework relating to events after the reporting period.

61.13 The engagement team's responsibility is to provide reasonable assurance that the financial statements have been "properly prepared" and give a "true and fair" view.

61.14 However, as per paragraph 6 of ISA (UK) 560, the engagement team is not expected to perform additional audit procedures on matters to which previously applied audit procedures have provided satisfactory conclusions.

Regularity considerations for subsequent events

61.15 ***Consultation required*** The engagement team should treat subsequent events involving regularity in the same manner as other subsequent events. Given Parliament's concern that public money is only used for purposes approved by Parliament, the C&AG is more likely to report to Parliament in respect of regularity matters that arise once the financial statements have been issued than in respect of other issues. The engagement team should consider carefully whether such matters need to be drawn to the attention of Parliament, or other stakeholders, in these circumstances and consult FAPQ as appropriate.

Events occurring between the date of the financial statements and the date of the C&AG's report

61.16 Paragraphs 6 to 8 of ISA (UK) 560 and the related application guidance include requirements relating to events occurring between the date of the financial statements and the date of the auditor's report.

61.17 If the result of the engagement team's determination under paragraph 8 of ISA (UK) 560 is that an identified subsequent event has not been appropriately reflected in the financial statements, the engagement team should evaluate the misstatement and determine the impact on the C&AG's opinion.

61.18 The engagement team should confirm with a responsible officer of the audited entity on the day that the account is to be certified that the Letter of Representation remains valid and that no event(s) have occurred since it was signed which would impact on the representations provided. This should be undertaken by the Engagement Director or Engagement Manager.

Facts which become known after the date of the C&AG's report but before the date the financial statements are issued

61.19 Paragraphs 10 to 13 of ISA (UK) 560 and the related application guidance include requirements relating to facts that become known after the date of the auditor's report but before the date the financial statements are issued.

61.20 There is no obligation to perform any audit procedures regarding the financial statements after the date of the C&AG's report. Accordingly, after this date, there is no requirement for the engagement team to seek out information that may have implications for the audit opinion that has already been given (as per paragraph 1-134 of Practice Note 10 (Revised 2022)).

61.21 As accounts cannot be laid before Parliament during recess, it is possible for a significant period of time to elapse between the date of the audit certificate and the laying of the financial statements. To mitigate the risk of subsequent events occurring between the date of the C&AG's report and the date the financial statements are laid in Parliament, the C&AG will not certify financial statements during recess. In exceptional circumstances, where the C&AG certifies a set of financial statements during recess, the engagement team should update the subsequent events review up to the date of laying.

61.22 If the audited entity decides to amend the financial statements, the engagement team should:

- undertake audit procedures necessary in the circumstances on the amendment;
- extend the audit procedures on subsequent events discussed above to the date of the new C&AG's report, including obtaining an updated letter of representation; and
- provide a new C&AG's report on the amended financial statements. The new C&AG's report should not be dated earlier than the date of approval of the amended financial statements.

61.23 In the UK, any amendments to the financial statements will involve amendment of the financial statements as a whole. For the NAO's international audited entities, it may be possible for those charged with governance to separately approve an amendment to the financial statements at a later date – if so, the engagement team may restrict their procedures to the amendment only, as per paragraph 12 of ISA 560 *Subsequent events* (the non-UK-adapted version, although this paragraph also appears in both the UK and international versions of the standard).

61.24 ***Consultation required*** In the circumstances envisaged by paragraph 13 of ISA (UK) 560 (management does not amend the financial statements in circumstances where the auditor believes they need to be amended), the engagement team should consult FAPQ.

61.25 Actions which may be taken in the circumstances envisaged by paragraph 13(b) of ISA (UK) 560 (the auditor's report has already been provided to the entity, the auditor has asked the entity not to issue the financial statements to third parties before the necessary amendments have been made, but the financial statements are nevertheless subsequently issued without the necessary amendments) include the following:

- If the financial statements are considered by an intermediate body before being despatched to the Secretary of State of the sponsor department and before being laid before Parliament, the engagement team should consider making a statement to that body, depending on our relationship with the intermediate body as set out in the Letter of Understanding (or Letter of Engagement), and in the light of any legal advice the engagement team may take on the position.
- If there is no intermediate body, and the entity has despatched the financial statements to the Secretary of State of the sponsor department but they have yet to be laid before Parliament, then subject to any legal advice on our position, the engagement team should consider reporting our concerns to the department. The C&AG will normally have right of access to report to the department any matters of importance arising out of our work.
- If the subsequent event occurred after the date of the C&AG's report, the engagement team should take legal advice and discuss with the entity's Chief Executive and with the sponsor department to establish whether it might be possible to withdraw the C&AG's report before the financial statements are laid before Parliament. The entity is likely to revise the financial statements in these circumstances, as they could not lay the account if the C&AG withdrew his opinion.
- Where the entity is a Public Interest Entity or a regulated entity in the financial sector, the engagement team could consider reporting the matter to the regulator in accordance with ISA (UK) 250B (Revised November 2019) *The auditor's statutory right and duty to report to regulators of Public Interest Entities and regulators of other entities in the financial sector*. Further guidance on such reports may be found in Chapter 31: Consideration of laws and regulations and reporting to regulators.

61.26 The engagement team should consider reporting separately to Parliament on the implications of the subsequent event for the financial statements and the C&AG's report, referring to Chapter 58: Reporting to Parliament.

Application guidance

61.27 Inquiries as to whether any subsequent events have occurred which might affect the financial statements may include:

- whether new commitments, borrowings or guarantees have been entered into;
- whether disposals or acquisitions of assets have occurred or are planned;
- whether there have been increases in capital or issuance of debt instruments;
- whether there have been any plans or agreement made for machinery of government changes or otherwise to merge or liquidate;
- whether any assets have been destroyed, such as by fire or flood;
- whether there have been any developments regarding contingencies;
- whether any unusual accounting adjustments have been made or are contemplated;
- whether any events have occurred or are likely to occur that will bring into question the appropriateness of accounting policies used in the financial statements, as would be the case, for example, if such events call into question the validity of the going concern assumption;

- whether any events have occurred that are relevant to the measurement of estimates or provisions made in the financial statements; and/or
- whether any events have occurred that are relevant to the recoverability of assets.

61.28 Additional procedures to identify whether any subsequent events have occurred which might affect the financial statements may include:

- reading the entity's latest available budgets, cash flow forecasts and other related management reports for periods after the date of the financial statements;
- inquiring, or extending previous oral or written inquiries, of the entity's legal counsel concerning litigation and claims;
- considering whether written representations covering particular subsequent events may be necessary to support other audit evidence and thereby obtain sufficient appropriate audit evidence; and/or
- reading the official records of relevant proceedings of Parliament and inquiring about matters addressed in proceedings for which official records are not yet available.

61.29 If, as a result of any of the engagement team's procedures, subsequent events are identified requiring adjustment or disclosure which management have not already identified, the engagement team should consider whether this is indicative of a control deficiency in management's procedures to identify subsequent events. The engagement team should assess whether any such deficiencies in controls are significant deficiencies and communicate in writing any significant deficiencies in internal control to those charged with governance in accordance with ISA (UK) 265 (Updated May 2022).

61.30 Engagement teams should document the procedures performed and that they have obtained sufficient, relevant and reliable audit evidence in support of their review and have complied with ISA (UK) 560.

61.31 The Engagement Director and Engagement Manager should plan subsequent events review procedures which reflect the risks of the entity. In particular for entities with significant accounting estimates, it may be appropriate to perform more extensive subsequent events procedures.

61.32 Engagement team members conducting subsequent events reviews should ensure that the have an adequate understanding of the entity and the amounts reflected in the financial statements to enable them to identify issues which may require disclosure or adjustment.

Chapter 62: Events after issue of the financial statements

Relevant standards and guidance

62.1 ISA (UK) 560 *Subsequent events* deals with the auditor's responsibilities relating to subsequent events in an audit of financial statements. Paragraphs 14 to 17 and the related application guidance include requirements relating to facts that become known to the auditor after the financial statements have been issued.

62.2 Paragraphs 1-120 to 1-141 of Practice Note 10 (Revised 2022) *Audit of financial statements and regularity of public sector bodies in the United Kingdom* provide guidance on applying ISA (UK) 560 in the public sector.

Determining the date of issue of the financial statements

62.3 The engagement team should refer to the section in Chapter 61: Events after the date of the financial statements but before issue of the financial statements entitled 'Determining the relevant dates' in order to determine the date of issue of the financial statements (for the majority of NAO-audited entities, this will be the date the annual report and accounts are laid before Parliament or otherwise published).

Corrections to published accounts

62.4 Chapter 22: Finalise, close and destroy audit file includes guidance relating to situations where audited entities amend the published annual report and accounts or the engagement team considers they should be amended.

Version control sheet

Version description	Details of changes	Date issued
Version 1 for 2021-22 pilot audits (November 2021)	Issued the following Chapters: 1: Using the FAM 2: Compliance with standards 3: Status and functions of the Comptroller and Auditor General 4: Quality monitoring 5: Direction and review of the engagement 6: Technical support and consultation 7: Engagement Quality Review 8: Ethical considerations 9: Engagement acceptance (statutory and non-statutory) 10: Determining the form of opinion 11: Determining the framework of authorities 12: Roles, delegations and licences 13: Process summary for NAO audits of financial statements 14: Audit engagement approval 15: Gathering entity initial information 16: Materiality, performance materiality and trivial threshold 17: Risk assessment and response planning 18: Regularity risk assessment and response planning 19: Continuous risk assessment 20: Evidence assessment and evaluation 21: Perform certification activities 22: Finalise, close and destroy audit file 23: Follow-up: Ensure continuous improvement of the audit 24: File management: Store documents and information and manage evidence 26: Going concern 27: Related parties 28: Comparative information 29: Fraud responsibilities 30: Consideration of laws and regulations and reporting to regulators 35: Accounting estimates	26 November 2021
Version 2 for 2021-22 pilot audits (January 2022)	Issued the following Chapters: 31: Other information and other reporting responsibilities 32: Analytical procedures 33: Tests of detail	28 January 2022

	34: Controls testing 36: Other specific audit procedures 45: Service organisations and shared service centres 48: Assessing the need for an auditor's expert 49: Obtaining internal expertise 50: Obtaining external expertise 51: Scoping and evaluating the work of an expert 52: Evaluating the results of procedures, including identified misstatements and irregular transactions 53: Submission, signing and printing of annual reports and accounts 54: Overall conclusions and preparing the certificate or report 55: Modified certificates and reports 56: Management representations 57: Reporting to those charged with governance 58: Reporting to Parliament 59: Reporting to the devolved legislatures and in other UK languages 60: Reporting to the members or shareholders of a company and filing with Companies House 61: Events after the auditor's report but before issue of the financial statements 62: Events after issue of the financial statements Updated for newly-issued Chapters: • ***Table 2A*** (list of ISAs (UK) and where guidance is provided in the FAM); • ***Table 6A*** (circumstances when engagement teams must consult with FAPQ or others as indicated); and • ***Table 6B*** (circumstances when the engagement team must obtain approval from the Director, Financial Audit Practice and Quality or a named deputy). Amended paragraphs 8.19 and 8.160 to specify the requirement to report any breaches of the FRC Ethical Standard to the Financial Reporting Council and to disclose them in the audit certificate or report. Added paragraphs 22.7 and 22.8 to describe information and documents which the engagement team is required to ensure are included in Audit Management in Pentana as part of the assembly of the final audit file. Added paragraph 24.6 to state that the engagement team should not modify documentation or add new documentation after the final audit file is archived and	

	describe the steps to be taken in the exceptional circumstances where this is required.	
Version 3 for 2022-23 audits (September 2022)	Issued the following Chapters: 25: Group audit procedures 26: Combined financial statements of components with no parent 38: Contracting with partner organisations 39: Role of the contractor auditor 40: Role of the NAO engagement team in contracted-out audits 41: Parliamentary Supply 42: Companies 43: Charities 44: Pension schemes 45: Public Interest Entities 47: Hard close audits Changed Chapter number of Chapter 46: Service organisations and shared service centres. Removed previous paragraph 2.4 on ISAs (UK) that had not yet come into effect, as those standards are now effective from 2022-23. Added paragraphs 2.12 to 2.14 and 2.36 requiring consultation with FAPQ: • where reasonable assurance cannot be obtained and a qualified opinion in the auditor's report is insufficient in the circumstances for purposes of reporting to the intended users of the financial statements; • wherean objective in a relevant ISA (UK) cannot be achieved and the engagement team's evaluation under paragraph 24 of ISA (UK) 200 (Revised June 2016) (Updated May 2022) has concluded that this prevents them from achieving the overall objectives of the auditor; or • where the engagement team judges it necessary to depart from a relevant requirement in an ISA (UK). Added paragraph 2.23 on the adoption of the Financial Reporting Council's professional judgement framework. Added paragraph 2.38 on the interpretation of the term 'firm'.	23 September 2022

	Added paragraph 4.12 to clarify where engagement teams are entitled to rely on the NAO's system of internal control. Amended paragraph 4.14 to clarify the statutory basis for the C&AG's being eligible for appointment as a statutory auditor. Amended paragraph 4.65 to clarify that all cold reviews will be considered and moderated by a Review Panel. Added paragraph 6.3 referring to the Financial Reporting Council's guidance on the role of consultation in making professional judgements. Updated for newly-issued Chapters: • ***Table 2A*** (list of ISAs (UK) and where guidance is provided in the FAM); • ***Table 6A*** (circumstances when engagement teams must consult with FAPQ or others as indicated); and • ***Table 6B*** (circumstances when the engagement team must obtain approval from the Director, Financial Audit Practice and Quality or a named deputy). Added paragraph 6.17 referring to the Financial Reporting Council's guidance on structuring the way in which a judgemnet is carried out and documented. Added paragraphs 6.30 to 6.32 on resolving differences of opinion between the engagement team and FAPQ. Amended paragraphs 8.16 to 8.18 to clarify judgements relating to ethical safeguards in respect of transactions entered into by the NAO, NAO staff, their closely connected family members and staff of firms undertaking contracted-out audits on behalf of the NAO with entities involved in managing or administering the Civil Service pension arrangements or other pension schemes employed by the NAO and with HMRC. Amended paragraphs 8.29 and 8.38 to state that the FAPQ Ethics function's log of conflicts of interest, ethical issues and safeguards is shared with the Financial Reporting Council, and the central register of interests is maintained and updated, regularly rather than on a monthly basis.	

	Amended paragraph 8.59 to state that one (rather than both) of the Director, Financial Audit Practice and Quality or the Director, Value for Money Practice and Quality should be notified of potential applications for roles within NAO audited entities. Amended paragraph 8.64 to state that the requirement for re-review and approval of the audit file where the Engagement Director takes up employment at the audited entity only applies where they have been a covered person for an engagement related to that entity. Amended paragraph 8.71 to refer to a person closely associated with the Engagement Director who has acquired a financial interest in an entity, rather than a close family members. Amended paragraph 8.74 to extend the requirement to disclose arrears on a loan to an entity to a person associated with a covered person as well as the covered person themselves. Amended paragraph 8.158 to clarify that communication of ethical considerations should take place following consultation with the Ethics Function. Amended paragraph 9.50 and added paragraph 9.52 to include consultation requirements relating to non-standard terms of engagement or amendment to the terms of the engagement during its course. Amended paragraph 10.8 to require FAPQ consultation where law or regulation prescribes the layout or wording of the auditor's report in a form or in terms that are significantly different from the requirements of ISAs (UK). Amended paragraph 12.6 to clarify that the requirement not to delegate Engagement Director or Engagement Manager roles to Audit Principals and Audit Managers with less than one year's service in the grade applies normally (previously an absolute requirement). Amended paragraph 12.8 to clarify that assignment of an Engagement Lead role to an individual without a General Audit Licence should be submitted to the Director, Audit Quality for approval.	

	Amended paragraph 12.13 to clarify that the requirement for Engagement Leads, Engagement Managers and Engagement Directors to hold a General Audit Licence applies to all financial audit engagements. Updated the list of mandatory Pentana work programme templates in ***Table 14A*** (as well as work programme template references elsewhere in the FAM). Amended paragraph 15.44 to clarify that the inability to decline appointment or to resign once appointed relates to the C&AG not the NAO. Added paragraph 15.47 to require the engagement team to investigate the reasons for inconsistent inquiries of management, those charged with governance or others within the entity or responses to these that are implausible. Removed previous paragraph 15.66 as the toolkit referred to is no longer extant. Amended paragraph 15.109 to clarify that the statutory other information for entities other than departments, executive agencies and companies will vary depending upon the basis for the audit, in addition to the basis of preparation of their annual report and accounts. Amended paragraphs 16.17 and 16.43 to 16.46 to reflect the terminology in ISA (UK) 320 (Revised June 2016) (Updated May 2022) relating to particular classes of transactions, account balances or disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements. Amended the examples given in paragraph 16.18 of considerations relating to materiality for classes of transactions, account balances and disclosures for which misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to influence the decisions of users taken on the basis of the financial statements.	

	Amended paragraph 16.27 and deleted previous paragraph 16.28 to reflect the revised approach to performance materiality in the new methodology. Amended paragraph 16.28 to add additional examples of situations where the engagement team may determine a different materiality threhsold for the audit of regularity from that for the true and fair opinion. Amended paragraphs 16.42 to 16.45 and 16.63 to reflect policy decisions relating to materiality, including that materiality is not set for disclosures in the other information and that the audit fee is not qualitatively material, for clarity of drafting and consistency of terminology with ISA (UK) 320 (Revised June 2016) (Updated May 2022). Amended paragraph 17.24 to explain that requests for additional content should be raised through the Financial Audit Support Tool (FAST). Amended ***Table 17B*** to: • remove the presumed significant risk relating to material misstatement in outturn against Parliamentary Supply; • add requirements for the engagement team to document within the RAPT their assessment/justification when asssessing the inherent risk associated with a RoMM; • reflect the revised Additive Method for calculating a RoMM's Likelihood placement on the spectrum of inherent risk; • add a requirement to consult FAPQ where the engagement team considers that, in relation to a scoped-in RoMM, there is no reasonable possibility of material misstatement due to the values involved and the RoMM's placement of the spectrum of inherent risk is considered to be inappropriate as a result of the effect of IRFs on the RoMM's Likelihood placement; • reflect the revised process for determining a RoMM's Financial Statement Impact (magnitude) placement on the spectrum of inherent risk; and • explain the application of the stand-back assessment on the appropriateness of the determination of material COTABDs as non-significant.	

	Amended paragraphs 17.28 and 19.16 to remove references to the income planning tool. Amended paragraph 17.31 to state that some FSRAs should be marked as relevant for all engagements comprising an audit of financial statements. Amended paragraph 17.33 to clarify that the auditor should identify the COTABDs that make up each FRA that is relevant to the audit. Added paragraphs 17.47 to 17.49 and ***Table 17F*** setting out considerations for when engagement teams should consult with IT audit specialists. Amended paragraphs 17.50 to 17.51 to provide updated lists of Inherent Risk Factors that may be relevant to NAO-audited entities. Amended paragraph 17.61 to remove the requirement to document the linkages between the procedures and the assertions affected in the testing plan for a significant risk. Added and amended paragraphs 17.128 to 17.136 to reflect revised requirements relating to journals testing. Amended paragraphs 17.138 to 17.142 for readability. Added paragraph 17.177 and amended paragraph 17.178 to reflect revised requirements relating to the stand-back assessment. Added paragraph 18.4 to require the engagement team to assess and categorise risks of material irregular transactions within the Regularity Risk Assessment template. Added paragraphs 20.23 to 20.24 relating to the NAO's policy on professional scepticism. Added paragraph 24.16 to include documentation requirements where the engagement team performans new or additional audit procedures or draws new conclusions after the date of the auditor's report.	

	Added paragraphs 27.18 and 31.17 relating to the scoping of related parties and compliance with laws and regulations as FSRAs within the RAPT. Amended paragraph 29.80 to clarify that the C&AG's exemptions from the Money Laundering, Terrorist Financing and Transfer of Funds Regulations 2017 do not extend to audits undertaken by agreement (i.e., "non-statutory" audits) – previously this only referred to audits undertaken under the Companies Act. Amended paragraphs 34.62 and various figures in Chapter 34 to reflect changes to the sampling methodology. Added paragraphs 34.88 to 34.89 and amended paragraph 34.90 to include expanded requirements on batched populations. Amended paragraph 34.131 to reflect amended sample sizes for judgemental cut-off samples. Added paragraphs 34.141 to 34.144 setting out the approach for sample testing of items that are individually accounting estimates with tolerable estimation uncertainty. Added paragraphs 34.145 to 34.148 and ***Table 34N*** setting out the approach for sample testing of contracts (or similar documents) to assess whether or not a method or requirements specified in the audited entity's financial reporting framework has been applied correctly. Added and amended paragraphs 37.58 to 37.62 to clarify external confirmation requirements for Government Banking Service accounts. Amended paragraphs 54.101 to 54.103 to provide updated guidance on electronic publication of annual reports and accounts, including where the audited entity intends to include the audit certificate or report within the electronic publication.	
Version 4 for 2022-23 audits (February 2023)	Updated references to ISQC (UK) 1 to reflect instead the requirements of ISQM (UK) 1. Updated references to Engagement Quality Control Review(er)(s) (EQCR) to Engagement Quality Review(er)(s) (EQR).	9 February 2023

	Redrafted Chapter 4 to reflect the implementation of the system of quality management which has been put in place in accordance with ISQM (UK) 1. Amended paragraph 8.21 to include a requirement to carry out Root Cause Analysis on any identified breaches of the Ethical Standard. Added paragraphs 9.57 and 9.58 and amended paragraph 42.145 to require consultation with FAPQ where the engagement team decides not to re-accept and engagement or the NAO otherwise ceases to hold office as statutory auditor and applying the procedures for sharing information with successor auditors to all audits, not merely company audits. Amended ***Table 10B*** to require FAPQ review of any reports issued under ISAE 3000 or ISRS 4400. Added paragraphs 12.19 to 12.23 setting out the requirement to document who is the Key Audit Partner for each engagement and whether they are eligible for appointment as a statutory auditor. Amended the requirements within ***Table 17B*** relating to situations where the engagement team considers that, in relation to a scoped-in estimates-related RoMM, there is no reasonable possibility of material misstatement due to the values involved and the RoMM's placement of the spectrum of inherent risk is considered to be inappropriate as a result of the effect of IRFs on the RoMM's Likelihood placement (including removing the requirement to consult FAPQ). Updated ***Figures 17E, 32A*** and ***35A*** to revise the levels of inherent assurance against each level of inherent risk. Added paragraph 24.17 setting out the appropriate steps when a Pentana audit file needs to be re-opened after it has been closed. Amended paragraphs 25.36 to 25.38 to align the scope of the requirement to review the component auditor's RAPT or equivalent risk assessment documentation to the Group Engagement Team review requirement in SGN 02/2018. Added paragraph 25.68 requiring a quality management point to be raised on FAST where the	

	Group Engagement Team has concerns regardiing the quality of work performed by a component auditor. Amended paragraph 25.86 to refer to requirements regarding requests to be made of component auditors for documentation requested by the Financial Reporting Council as part of a quality assurance review or an investigation. Added paragraphs 33.70 to 33.76 (cross-referenced from new paragraphs 20.19 and 33.77) setting out requirements for testing of staff reports used in payroll SAPs as Information Produced by the Entity. Updated ***Table 35B*** to reflect revised controls sample sizes and to rename “ad hoc” controls as “demand-led” controls. Added paragraphs 45.46 to 45.49 and 45.55 to 45.56 to highlight requirements within ISA (UK) 250A (Revised November 2019) (Updated May 2022) and ISA (UK) 250B (Revised November 2019) relating to reporting to the regulator of a PIE or other regulated entity. Amended paragraph 57.16 to reflect the requirement for engagements where an Extended Auditor Report is expected to be issued to communicate to those charged with governance as part of the overview of the planned scope and timing of the audit the Key Audit Matters identified at the planning stage or else a confirmation that the significant risks reported constitute the entirety of the Key Audit Matters to be considered during the course of the audit. Removed previous paragraphs 57.22 and 57.23.	
Version 5 for 2022-23 audits (May 2023)	Revised Chapter 8 Amended paragraph 10.9 to reflect the NAO policy to prepare an Extended Auditor’s Report for all Ministerial Government Departments. Updated ***Figure 34G*** and ***Figure 34L*** to reflect amended requirements on sub-sampling and re-defined attribute sampling sample sizes. Amended paragraph 35.10 to define when a deficiency in internal control exists.	25 May 2023

	Amended paragraph 45.58 to require FAPQ review of additional reports to the audit committee of a PIE where the audit is contracted out or a two-tier or joint audit. Added new paragraph 45.68 to reflect the requirement to discuss key matters arising with the audit committee of a Public Interest Entity on request. Amended paragraph 46.26 to remove reference to a Generic Inherent Risk Factor regarding the use of service organisations. Amended paragraph 57.18 to refer to the inclusion of reporting to those charged with governance on key audit matters in the Audit Planning Report and Audit Competion Report. Amended paragraph 57.55 to clarify that where signficant deficiencies are communicated to those charged with governance orally, subsequent communication in writing may be omitted in favour of a note of the meeting or discussion where the communication occurred being retained on the audit file as evidence that the matter has been communicated. Added new paragraph 57.73 regarding procedures performed in relation to reporting of matters which go beyond the scope of the auditor's responsibilities under ISAs (UK). Other amendments to reflect changes in the NAO's grade structure.	
Version 6 for 2023-24 audits (September 2023)	Amended paragraphs 9.21 and 9.31 to require engagement acceptance requests to be copied to Executive Directors and to require the resourcing and staffing implications of prospective new engagements to be discussed with the Director, Financial Audit Operations. Updated Chapters 2, 4, 5, 6, 7, 8, 9, 12, 14, 15, 17, 19, 21 39, 40, 41, 45, 48, 49, 50, 51 and 54 to reflect the adoption of ISA (UK) 220 (Revised July 2021). Updated Chapters 2, 5, 7, 17 and 45 to reflect the adoption of ISQM (UK) 2. Updated Chapters 17 and 30 to reflect that the presumed risk of fraud in revenue recognition is	29 September 2023

	considered as part of the engagement team discussion on fraud. Updated terminology and workflow references to reflect the launch of Apex.	
Version 7 for 2023-24 audits (January 2024)	Amended paragraph 1.7 to clarify that queries relating to the FAM that relate to a specific engagement should be raised using the Consultation functionality in Apex. Amended paragraph 2.35 to note that if is it necessary to depart from a relevant requirement in an ISA (UK), the engagement team should document any proposed modifications to the audit certificate or report, which are to be discussed with FAPQ. Amended paragraph 7.18 to note that upon appointment of a replacement EQR, discussion of the key issues on the engagement with the C&AG is not required, but the EQR may consult the C&AG. Amended Chapter 12 to reflect revised policies relating to role assignments for 2023-24. Amended ***Table 17B*** and paragraph 35.21 to reflect revised application of paragraph 26 of ISA (UK) 315 (Revised July 2020). Amended ***Table 17C*** to add definitions for 'Assertions' and 'Relevant assertions'. Amended paragraph 25.25 to revised procedures for the designation of Key Audit Partners for group audits. Amended paragraphs 42.141 and 42.142 to clarify that these requirements only apply where the company has included its required Corporate Governance Statement as a separate report. Amended references to "Engagement Lead" to read "Engagement Team-Leader" throughout.	4 January 2024
Version 8 for 2023-24 audits (April 2024)	Amended paragraph 2.3 to clarify that NAO engagement teams conducting audits under ISAs (UK) must comply with all ISA (UK) requirements unless the entire ISA (UK) is not relevant or the requirement is conditional and the condition does not exist.	19 April 2024

	Updated paragraph 5.18 to include a policy on documentation of review of individual attachments in Apex. Amended Chapter 7 to reflect central considerations of ISQM (UK) 2 application in the NAO's methodology. Amended the list of covered persons in paragraph 8.13 to include members of the ATS team and certain members of the ATP team, as well as the Director, Audit Risk and Compliance. Amended paragraph 8.33 to reflect that the Director, Audit Risk and Compliance now leads the NAO's Ethics Function. Amended paragraph 8.98 to clarify the policy on requests for an individual to act as an Engagement Director for longer than a period of five continuous years for listed entites. Amended paragraphs 17.41, 35.18, 35.24 and 35.46 to note that NAO engagement teams are not permitted to place reliance on the operating effectiveness of budgetary controls. Added new section on 'Boundary of the audit file' to Chapter 24. Updated ***Figure 34D*** to reflect a revised standard substantive sampling frame. Added paragraph 49.9 requiring engagement teams to consult the Financial Instruments Centre of Expertise in respect of certain categories of financial instrument balances. Amended Chapter 53 to reflect the new Certification functionality in Apex, replacing the previous certification journal process. Amended ***Table 54B*** to: • highlight that engagement teams should note in preparing the basis for opinion[s] that the auditor shall not represent compliance with ISAs (UK) in the auditor's report unless the auditor has complied with the requirements of and all other ISAs (UK) relevant to the audit; and	

	• remove the previous reference to Practice Note 15 to align with the corresponding change to certificate templates. Amended references to Director, Financial Audit Practice and Quality; Director, Financial Audit Operations; and Director, Compliance and Quality Unit to, respectively: Director, Audit Quality; Director, Audit Operations; and Director, Audit Risk and Compliance throughout. Amended certain references on quality management responsibilities to reflect the creation of the positions of Executive Director of Financial Audit and Deputy Head of Financial Audit, as well as the transfer of responsibility for the Ethics Function to the Director, Audit Risk and Compliance.	
Version 9 for 2024-25 audits (October 2024)	Updated definitions of 'Engagement Quality Review' and 'Engagement Quality Reviewer' in paragraph 2.36 to align with ISA (UK) 220 (Revised July 2021) and clarified that 'Engagement team' includes component auditors. Added interpretations of the terms 'partner', 'personnel' and 'staff' in ISA (UK) 220 (Revised July 2021) as new paragraphs 2.38 to 2.40. Made amendments to reflect transfer of responsibilities from CQU to FA Compass; transfer of responsibilities for ethical matters from the Director, Audit Quality to the Director, Audit Risk and Compliance; and transfer of responsibilities for AQR reviews from the Director, Audit Risk and Compliance to the Director, Audit Quality. Added details of the engagement team's responsibilities for quality within the context of the NAO's system of quality management to paragraph 4.4. Added details of the Engagement Director's responsibilities in relation to information that may be relevant to the NAO's monitoring and remediation process as new paragraph 4.19. Noted the Engagement Director's responsibilities in relation from information from the NAO's monitoring and remediation process as new paragraph 4.41. Added details of the Engagement Director's responsibilities in relation to using the resources	30 October 2024

	assigned or made available to the engagement team to paragraph 5.3. Added details of the Engagement Director's responsibilities for managing and achieving quality on audits and for relevant ethical requirements, including those related to independence, to ***Table 5A***. Added details of the Engagement Director's responsibilities for determining that they have taken overall responsibility for managing and achieving quality on the audit engagement to paragraph 5.17. Moved various responsibilities to consult with the Director, Audit Risk and Compliance from ***Table 6A*** to ***Table 6C***. Added details of the Engagement Director's responsibilities for differences of opinion as new paragraph 6.38. Added context for the role of an Engagement Quality Review from paragraph 7 of ISQM (UK) 2 to paragraph 7.5. Made various amendments to Chapter 8 to reflect implementation of the Revised Ethical Standard 2024, superseding the Revised Ethical Standard 2019. Clarified in paragraph 14.25 that the engagement team should not progress the audit further until the Engagement Director has approved and reviewed the Setup workflow. Clarified in paragraph 16.10 that the engagement team should revisit the Risk Assessment in Apex as necessary where a lower materiality than intially determined is appropriate. Amended ***Table 17B***, paragraphs 17.30 and 17.32 to reflect the new scoping question in the Risk Assessment at the FRSA level scoping out estimates where there is no reasonable possibility that a material misstatement could occur. Clarified in paragraph 17.83 that the engagement team should explicitly consider whether external confirmation procedures should be performed as a substantive audit response.	

	Updated paragraph 18.4 to reflect that risks of material irregular transactions may be categorised as Low risk within the Regularity Risk Assessment. Added Certification records to the definition of the boundary of the audit file in paragraph 24.3. Added policies on the timeliness of audit documentation as new paragraphs 24.7 to 24.9. Redrafted Chapter 25 and updated various other references relating to group audits to reflect the revised ISA (UK) 600. Clarified that the consultation referred to in paragraphs 30.46 and 30.47 (where, as a result of a misstatement resulting from fraud or suspected fraud, the auditor encounters exceptional circumstances that bring into question the auditor's ability to continue performing the audit) is a mandatory consultation requirement. Updated Chapter 33 and Chapter 34 to reflect revised sampling policies in the following areas: • performance of SAPs to obtain a Low level of assurance (paragraph 33.63); • sample testing to support a payroll SAP (paragraph 33.73); • low volume populations (50 items or fewer) (new paragraph 34.81 and ***Figure 34D-a***)); • substantive tests of detail over payroll employees (***Table 34E***); • sampling batched populations (***Figure 34G***); • process where Upper Error Limit exceeds materiality (***Figure 34J***); • selection of sampling approaches (***Figure 34L***); • cut-off testing (paragraphs 34.132 to 34.137, ***Figure 34M-a*** and ***Figure 34M-b***); • contracts and leases sampling (***Table 34N***); and • deleted ***Figure 34P*** (sample sizes and associated precisions). Noted in paragraph 35.8 that testing the operating effectiveness of controls is a required procedure in situations where substantive procedures alone cannot provide sufficient appropriate audit evidence at the assertion level.	

	Added definitions relating to external confirmations (per paragraph 6 of ISA (UK) 505 (Updated May 2022)) as new paragraph 37.21. Added requirements where management refuses to allow the auditor to send a confirmation request as new paragraphs 37.51 and 37.52. Clarified in paragraph 37.81 to note procedures where the engagement team is unable to attend the year-end physical inventory count due to unforeseen circumstances. Added a mandatory consultation requirement to paragraph 37.90 (where attendance at physical inventory counting is impracticable). Added requirements for communication to those charged with governance where the engagement team identifies or suspects fraud as new paragraph 45.52. Noted in paragraph 46.1 circumstances to which ISA (UK) 402 (Updated May 2022) does not apply. Added background information on outsourcing arrangements and the relevance of services provided by a service organisation to the audit of a user entity's financial statements as new paragraphs 46.5 and 46.6. Added requirement for the engagement team to evaluate whether a Type 2 report covers the relevant risks of material misstatement per the Risk Assessment in Apex to paragraph 46.44. Added requirements where the engagement team plans to use audit evidence provided by a Type 1 or Type 2 report as new paragraphs 46.52 and 46.53. Added requirements where the engagement team has not obtained sufficient appropriate audit evidence related to a relevant assertion about a class of transactions, account balance or disclosure to paragraph 54.14, including a requirement to consult FAPQ where the engagement team is unable to obtain sufficient appropriate audit evidence. Added details of the objectives of the auditor to references to various ISAs (UK).	