



ADDRESSING THE LOCAL AUDIT BACKLOG IN ENGLAND: REGULATORY CHANGES

Issued 7 March 2024

ICAEW welcomes the opportunity to comment on the consultation by the Department for Levelling Up, Housing and Communities (DLUHC) dated 8 February 2024 on *Addressing the Local Audit Backlog in England*, a copy of which is available from this [link](#).

ICAEW supports the proposed backstop dates and other regulatory changes

- Restoring timely reporting is critical to restoring financial accountability to the local government sector in England. The current delays in publishing financial statements have led to unacceptably low levels of accountability of some local authorities.
- Resetting the audits of financial statements is an important step to restoring credibility and to preventing backlogs recurring in the future. This needs to happen as soon as is possible.
- We agree that larger local authorities should publish audited financial statements by the proposed backstop dates, with one suggested accommodation.
- DLUHC will need to support local authorities who may incur reputational damage from qualified audit opinions.

Local finance teams and their auditors will need support to get back on track

- Local authority finance teams are likely to need additional resources to catch up on the preparation of financial statements, working papers, and to respond to audit queries.
- We recommend extending the deadline for preparing unaudited accounts to June of each year, to initially mitigate conflict with the backstop date of 31 May 2025 for 2023/24 audited accounts and to give local authorities more time to concentrate on the quality of their underlying working papers. Many finance teams are small and are likely to be stretched if there are conflicting priorities.
- It is important that the measures do not deter audit firms from continuing to operate in the local audit market or prevent new audit firms from entering the market. Consideration needs to be given to this when reviewing the consequences for auditors or local authority finance teams if deadlines are missed.

Preventing a recurrence and the need for long-term reform

- Long-term reform of the sector is essential to address the systemic challenges which have contributed to the current situation.
- Within our [Vision for Local Audit](#), we made the case for ensuring better quality timely financial reporting, stronger financial management and governance, and developing a thriving profession which is highly valued.
- We believe that such reform is essential for the crisis to be resolved over the longer term.
- We welcome Phase 3 of the proposals which set out some propositions to reform the sector over the long-term, however we would underline the importance of ensuring that these measures are implemented in a timely manner.

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This response has been prepared by ICAEW's Public Sector team in consultation with ICAEW's Public Sector Advisory Group. ICAEW's Public Sector team supports members working in and with the public sector to deliver public priorities and sustainable public finances, including over 13,000 in ICAEW's Public Sector Community. ICAEW engages with policy makers, public servants, and others to promote the need for effective financial management, audit and assurance, financial reporting and governance and ethics across the public sector to ensure public money is spent wisely.

For questions on this submission please contact our Public Sector team at representations@icaew.com quoting REP 25/24

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INTRODUCTION

WE WELCOME THIS CONSULTATION ON ADDRESSING THE LOCAL AUDIT BACKLOG IN ENGLAND

1. ICAEW welcomes the opportunity to respond to this consultation on addressing the local audit backlog in England.
2. The local audit crisis is undermining public trust in local authority finances, with only 1% of English councils publishing audited financial statements by the 30 September 2023 target date for 2022/23 financial statements. There was a backlog of 771 overdue audits as of 31 December 2023.
3. Delays are prevalent across local authorities who have issued s114 notices, with all seven English councils who have issued such a notice since 2020 having delays in publishing audited financial statements of at least three years. There is a key risk of financial issues going undetected at other local authorities without appropriate scrutiny, and such issues could be preventable if identified at an early stage in the audit process.
4. Local authority accounts must be a credible public record which enables stakeholders to hold local authorities to account, however this is only possible when audited financial statements are published on a timely basis. The proposals therefore are welcomed as an essential short-term measure in aiming to return timely accountability to local authority financial reporting.
5. Our [vision for local financial reporting and audit](#) sets out steps we believe are necessary to improve the quality and rigour of the financial information provided to councillors to enable them to be effective in holding their local authorities to account. It also sets out steps to strengthen local audit to assure that information.
6. We submitted evidence on 17 April 2023 to the House of Commons Levelling Up, Housing and Communities Committee setting out how we believe [financial reporting and audit in local authorities](#) can be improved.
7. We [submitted evidence](#) on 18 May 2023 to the HM Treasury thematic review of non-investment asset valuation for financial reporting purposes.
8. We [submitted evidence on 15 August 2023](#) to the DLUHC consultation on statutory guidance on the Best Value Duty for local authorities in England.
9. We submitted evidence on 17 October 2023 to CIPFA LASAAC on [how we believe the Local Authority Accounting Code](#) can be improved.

KEY POINTS

ICAEW SUPPORTS THE PROPOSALS

10. We support the changes to the Accounts and Audit Regulations 2015 (AAR 2015) proposed in the consultation, as well as other measures aimed at clearing the backlog of overdue audits.
11. We agree with Phase 1 of the plan to require larger (Category 1) local authorities to finalise audited financial statements for financial years 2015/16 up to 2022/23 by 30 September 2024 at the latest, 18 months after the balance sheet date for the audited financial statements for the year ended 31 March 2023.
12. We hope that as many local authorities as possible will be able to resolve accounting issues in time and publish audited financial statements with clean audit opinions. Some local authorities may receive a modified audit opinion, but on balance this is preferable to allowing the local financial reporting and audit crisis to continue to go unresolved.
13. We agree with Phase 2 of the plan to gradually bring down the backstop date for publishing audited financial statements until it aligns with what was previously a non-mandatory target date of eight months after the balance sheet date.

14. We would not support any changes to these backstop dates, as we believe these provide essential momentum for the plan to eliminate the audit backlog to be successful.

RESOURCE IMPLICATIONS

15. The proposals are likely to require additional resourcing for local authority finance teams over the next two to three years, especially if local authorities are to avoid unwanted audit disclaimers. Some local authorities have yet to produce draft financial statements for some of the years that are outstanding, while others have yet to produce working papers and other supporting information that their external auditors require.
16. Resourcing was cited as a key issue at a recent roundtable on the consultation and we have also heard similar concerns expressed by preparers and auditors about the capacity of local authority finance teams required to meet the backstop dates.
17. One local authority cited as a concern the direct clash between the 31 May 2025 deadline to publish both 2023/24 audited financial statements and 2024/25 unaudited financial statements. Many local authorities have relatively small finance teams, already under pressure for other reasons, and we consider that there is a danger of them being unable to meet one of these deadlines, or a danger of missing both deadlines should teams be split in working to meet both.
18. Furthermore, many audit firms are likely to be completing NHS or other public sector audits in May or June of each year. Accounts produced by the 31 May are less likely to have a significant amount of audit performed on them until early July.
19. We have therefore suggested extending the 31 May deadline date for preparing unaudited financial statements by one month to 30 June each year, initially to mitigate the pressure that local finance teams will be under to also complete their 2023/24 audits by 31 May 2025, but also to allow local authorities more time to create quality working papers going forwards.
20. There are also likely to be resource implications for external audit firms and local authorities alike. DLUHC should consider whether funding is required to cover any additional fees that are required to deliver on the plans.

PREVENTING RECURRENCE

21. Restoring the timely publication of audited financial statements is only the first step. It is also critical that underlying causes are addressed so that audit backlogs do not recur.
22. DLUHC will need to work with local authorities to ensure that their finance teams and governance structures are adequately resourced and capable, and with the shadow system leader, PSAA, and audit firms to ensure that there is sufficient market capacity available.
23. It is paramount that measures to improve the attractiveness of the local audit sector and measures to simplify local authority financial reporting are implemented as soon as possible.
24. For the sector to be sustainable in the long run, more audit firms must be registered to work in the sector and more individuals must be attracted to train and qualify in the sector and be motivated to continue working in it.
25. Currently, there are only 10 audit firms registered as a local auditor on ICAEW's local audit register. Only five of these firms are signed up to the PSAA contract to undertake a 2022/23 financial audit of a local authority which appoints their auditors through the contract, which typically covers larger and more complex local authorities.
26. Arguably more concerningly, there are only 102 key audit partners who are qualified to sign local audit reports within a registered local audit firm. We are aware that a number of these people no longer work in the local audit sector, so the true number still working in local audit is likely to be less than this. We do not consider that this is a sustainable number.
27. We welcome the Reform phase of the proposals, which recognises that work is required to address the systemic challenges which have contributed to the current local audit backlog. All parties working across the system must work together to launch appropriate measures on a timely basis to ensure that such a backlog does not re-occur in the future.

THE NEED FOR LONG-TERM REFORM

28. The local financial reporting and audit crisis has highlighted how audited financial statements are not being used effectively in accountability and governance.
29. In theory, audited financial statements, together with accompanying narrative reports, should provide cabinets and councillors with critical information for making financial decisions, determining strategy, monitoring financial performance, and managing risk. They are also a tool for assessing the quality of management, and a vehicle for disclosures of importance to residents and other stakeholders.
30. Unfortunately, local authority financial statements are considered to be difficult to follow or even impenetrable to many users, hampering their use as a credible public record to hold local authorities to account, in addition to limiting their usefulness in supporting effective decision-making, strategy, performance monitoring, risk management and other governance processes.
31. Our view is the underuse of audited financial statements, which pre-dates the recent accumulation of delayed audit opinions, presents a significant gap in the systems of accountability and governance operating in local authorities in England. We believe that it is therefore important that DLUHC works with other stakeholders to improve the understandability of financial statements, to ensure they are being used effectively in accountability and governance processes, and that they provide a platform for better communication with residents and local and national taxpayers.

ANSWERS TO SPECIFIC QUESTIONS

Question 1

Notwithstanding the possibility of exemptions in exceptional circumstances (covered by questions 3-4 below), do you agree that Category 1 authorities should be required to have published audited accounts for all financial years up to and including financial year 2022/2023 by 30 September 2024? (agree, disagree, unsure)

Do you have any comments on this issue?

32. Yes, we agree that Category 1 authorities should be required to publish audited financial statements for all financial years up to and including financial year 2022/23 by 30 September 2024.
33. We consider that this is an essential short-term measure which is a way to resolve the backlog in local audit opinions.
34. Ensuring publication of audited accounts up to 2022/23 by the deadline will enable local authority finance teams and auditors to begin focusing all their efforts on publishing audited accounts for future financial years.

Question 2

Do you agree that the requirement at Regulation 10 (2) for Category 1 authorities to publish a delay notice should be disapplied in relation to any outstanding audits covering financial years 2015/2016 to 2022/2023? (agree, disagree, unsure)

Do you have any comments on this issue?

35. Yes, we agree that the requirement for Category 1 authorities to publish a delay notice should be disapplied in relation to any outstanding audits covering financial years 2015/16 to 2022/23.
36. Our only reservation is whether such a notice should still be applied if there are outstanding objections to the accounts, which could be material to the audit opinion.

Question 3

Do you think it would be appropriate for Category 1 authorities to be exempt from the statutory backstop date of 30 September in circumstances where the auditor is unable to issue their opinion due to outstanding objections to the accounts that could be material to that opinion? (agree, disagree, unsure)

Please explain your response.

37. Yes, we agree that it would be appropriate for Category 1 authorities to be exempt from the statutory backstop date of 30 September in circumstances where the auditor is unable to issue their opinion, due to outstanding objections to the accounts that could be material to that opinion.
38. The objection process, as per the National Audit Office's guide to your rights on Local Authority Accounts, allows electors to object in instances where they deem an item in the accounts to be unlawful, where they deem there are issues relevant to the authority's arrangements for securing value for money or that are referred to in an authority's annual governance statement; or there are serious matters of wider concern, for instance around corporate governance, arising from the authority's finances.
39. It would be more damaging reputationally to issue an inappropriate audit opinion because of an item which is unlawful in the accounts, for example, rather than publishing audited financial statements late but allowing the important objection process to occur and issuing an appropriate audit opinion.

Question 4

Do you think there would be any other exceptional circumstances which might create conditions in which it would be appropriate for Category 1 authorities to be exempt from the 30 September backstop date? (agree, disagree, unsure)

Please explain your response, including, where relevant, details of exceptional circumstances you consider would justify an exemption.

40. No, we do not consider that there are any other exceptional circumstances which might create conditions in which it would be appropriate for Category 1 authorities to be exempt from the 30 September backstop date.
41. While we agree on exempting Category 1 authorities where there is an objection to the accounts, having further circumstances where an authority would be exempt from the backstop date would detract from the aim of returning timely accountability to local authority financial reporting.
42. Audited financial statements must therefore be published except in exceptional circumstances where there is a material risk of an inappropriate audit opinion being issued, such as when an objection to the accounts is raised.

Question 5

We intend to publish a list of local bodies and audit firms which meet statutory deadlines for the publication of audited accounts and those which do not. Do you think there should be additional consequences for Category 1 authorities or audit firms (excluding an authority or firm covered by an exemption) if they do not comply with the statutory deadline of 30 September 2024? (agree, disagree, unsure)

Please explain your response and, where relevant, include any suggested consequences

43. No, we do not believe that it would be appropriate for there to be additional consequences for Category 1 authorities or audit firms, if they do not comply with the statutory deadline of publishing audited financial statements by 30 September 2024.
44. We consider that the best approach is to provide local authority finance teams and audit firms with guidance and encouragement to ensure that they do publish audited financial statements by the statutory deadline.

45. Implementing further additional consequences may have a detrimental impact on the sector, potentially by deterring new audit firms from entering the market or by deterring existing audit firms currently operating in the market from continuing.
46. Similarly, any consequences placed on local authorities are likely to impact morale within local authority finance teams when morale is already low due to the current situation.

Question 6

Notwithstanding the possibility of exemptions in exceptional circumstances (covered by questions 7-8 below), do you agree that Category 1 local authorities should be required to publish audited accounts for financial years 2023/2024 – 2027/2028 by the following dates (agree, disagree, unsure)?

- **2023/24: 31 May 2025**
- **2024/25: 31 March 2026**
- **2025/26: 31 January 2027**
- **2026/27: 30 November 2027**
- **2027/28: 30 November 2028**

Do you have any comments on these dates?

47. Yes, we agree in principal that statutory deadlines should be put in place for Category 1 local authorities to publish audited accounts for financial years 2023/24 – 2027/28.
48. The need for returning local authority financial reporting back to a sustainable footing is paramount and implementing five years of backstop dates should assist in preventing a new backlog occurring in the future.
49. We have a reservation regarding the date set for publishing audited financial statements for 2023/24, as the 31 May 2025 deadline clashes with the deadline for local authorities to publish unaudited financial statements for 2024/25.
50. We consider that the clash may lead to intense pressure on local authority finance teams, who will need to publish two years' worth of financial statements by the same date. This could lead to one deadline being missed or alternatively, both deadlines being missed if teams are stretched working across both financial years.
51. As noted in more detail in our response to Q11 below, we therefore suggest moving the deadline to publish unaudited financial statements from 31 May and keeping the 31 May 2025 deadline to publish 2023/24 audited financial statements, to mitigate pressures on local authority finance teams.

Question 7

Do you think it would be appropriate for Category 1 authorities to be exempt from the statutory backstop dates for Phase 2 in circumstances where the auditor is unable to issue their opinion due to outstanding objections to the accounts that could be material to that opinion? (agree, disagree, unsure)

Please explain your response.

52. In the same way as Phase 1, we consider that it would be appropriate for Category 1 authorities to be exempt from the statutory backstop dates for Phase 2 in circumstances where the auditor is unable to issue their opinion due to outstanding objections to the accounts which could be material to the audit opinion.
53. As noted in our response to Q3, our view is that the reputational damage of issuing an inappropriate audit opinion would be greater than issuing a materially accurate audit opinion late.

Question 8

Do you think there would be any other exceptional circumstances which might create conditions in which it would be appropriate for Category 1 authorities to be exempt from the backstop dates for Phase 2? (agree, disagree, unsure)

Please explain your response, including, where relevant, details of exceptional circumstances you consider would justify an exemption.

54. No, we do not believe there are any other exceptional circumstances which might create conditions in which it would be appropriate for Category 1 authorities to be exempt from the backstop dates for Phase 2. This mirrors our opinion in our response to Q4.
55. As noted in our response to Q4, adding additional circumstances which could prevent an audit opinion being issued would detract from the aim of returning timely accountability to local authority financial reporting.

Question 9

We intend to publish a list of local bodies and audit firms which meet statutory deadlines for the publication of audited accounts and those which do not. Do you think there should be additional consequences for Category 1 authorities or audit firms (excluding an authority or firm covered by an exemption) if they do not comply with the statutory deadlines for Phase 2? (agree, disagree, unsure)

Please explain your response and, where relevant, include any suggested consequences.

56. As noted in our response to Q5, we do not believe that it would be appropriate to issue additional consequences to Category 1 authorities or audit firms for Phase 1. Our viewpoint remains the same for Phase 2, with the best approach being to provide guidance and encouragement to local authority finance teams to ensure they do publish audited financial statements by the statutory deadline.
57. Where authorities are not able to or are struggling to meet the statutory deadline, all parties across the local audit system should work with these authorities to understand the issues in meeting the deadline and work with them to mitigate and resolve these issues.
58. Further consequences, as previously noted, may have a detrimental impact on the sector by deterring new audit firms from entering the market or deterring existing audit firms currently operating from continuing.

Question 10

The Accounts and Audit Regulations 2015 (regulation 15 (1)(a)) currently requires Category 1 local authorities to publish unaudited accounts by the 31 May following the end of the financial year. In light of the proposed deadlines for the publication of audited accounts, do you think the 31 May deadline remains appropriate for financial years 2024/2025 to 2027/2028? (agree, disagree, unsure)

Please explain your response

59. As previously noted in our response to Q6, we do not agree that the 31 May deadline to publish unaudited accounts following the end of the financial year remains appropriate for the 2024/25 financial year, as this directly clashes with the deadline for local authorities to publish their audited 2023/24 financial statements and may lead to intense resource pressures at both local authority finance teams and audit firms.
60. Furthermore, as audit firms are likely to be undertaking NHS and other public sector audits around May and June, it is unlikely that accounts produced by 31 May would have a significant amount of audit work performed until early July onwards. Extending the deadline would therefore give further time for local authority accounts preparers to concentrate on producing quality underlying working papers which would support the audit.
61. Therefore, we believe that the deadline to publish unaudited financial statements for each financial year should be changed to the 31 June, however those authorities which can produce financial statements by 31 May should still be encouraged to do so.

Question 11

The existing annual deadline for the publication of unaudited accounts is 31 May. As set out above, we are proposing a backstop date for the publication of audited accounts for the financial year 2023/2024 of 31 May 2025. This would mean that 31 May 2025 would be the statutory deadline for both the publication of audited accounts for financial year 2023/2024 and unaudited accounts for financial year 2024/2025. Do you expect this would create any significant issues? (agree, disagree, unsure)

Please explain your response

62. As referenced in our responses to Q6 and Q10, we expect that the 31 May 2025 deadline to publish both unaudited financial statements for 2024/25 and audited financial statements for 2023/24 may cause significant issues for both auditors and local authority finance teams alike.
63. We consider that there is a significant risk of a local authority missing both deadlines in the current scenario, which would impact their ability to meet the statutory deadlines for publishing audited financial statements in future years.
64. We are aware that there are recruitment and retention issues at local authorities currently. A recent report from the Social Market Foundation noted that the median vacancy rate in English local authorities reached 14% in 2021-22, while their 2022 survey highlighted that 55% of councils were suffering either 'large' or 'very large' workforce shortages.
65. As noted previously, only five audit firms are currently registered via the Public Sector Audit Appointments Contract to undertake a 2022/23 financial audit at relevant local authorities that have opted into PSAA's national auditor appointment arrangements.
66. Having to meet both deadlines is likely to prevent a local authority from fully engaging with completion of either set of financial statements, as they are likely to be stretched across both priorities. For example, a local authority finance team may not be able to properly engage with the audit process for the 2023/24 financial year if they are also having to complete unaudited 2024/25 financial statements, increasing the risk of missing the statutory deadline or potentially slowing down the audit process which increases the risk of a modified opinion.
67. A modified opinion subsequently makes it more difficult for auditors to gain assurance over the opening balances of the following year's financial statements, increasing the likelihood of modified opinions going forwards as a result. We do appreciate that the Phase 2 proposals are designed to enable auditors to build assurance over opening balances over several financial years rather than having to build all their assurance in one year, however it will be beneficial for auditors to obtain as much assurance as possible early in the Phase 2 period to prevent this being an issue beyond 2027/28.
68. In our view, it is imperative that a local authority finance team focuses on meeting one deadline at a time, with the higher priority deadline likely being the statutory deadline to publish the 2023/24 audited financial statements, in line with the aim of returning timely accountability to local authority financial reporting on an immediate basis.
69. Therefore, as suggested previously, the deadline to publish unaudited financial statements for 2024/25 should be extended to 30 June 2025.

Question 12

The Government anticipates that the Phase 1 backstop proposals will result in modified or disclaimed opinions. A modified or disclaimed opinion at the end of Phase 1 would require auditors to subsequently rebuild assurance. The Phase 2 backstop dates are intended to enable this work to be spread across multiple years. Given this additional work, and noting the further explanation at paragraphs 15-46 of the Joint Statement [Local audit delays: Joint statement on update to proposals to clear the backlog and embed timely audit - GOV.UK \(www.gov.uk\)](#), do you have any views on the feasibility of audited accounts being published by the proposed statutory backstop dates for Phase 2?

70. We believe that it is feasible for audited accounts to be published by the proposed statutory backstop dates for Phase 2, provided that the deadline for publishing unaudited accounts of 2024/25 is extended so there is no longer a direct clash with the deadline for publishing audited accounts for 2023/24.
71. As the Joint Statement notes, the backstop dates enable auditors to rebuild assurance over local bodies financial information over a period of years, rather than requiring all assurance to be rebuilt in the first instance. We agree that this is an essential measure to ensure that there is not a re-occurrence of the backlog and are pleased that the FRC have confirmed this approach is compliant with ISAs.
72. However, as previously noted in this response, auditors will need to be able to perform as much of this work as possible at an early stage in the Phase 2 process, to ensure that issues surrounding opening balances do not remain after completion of Phase 2 in 2027/28.

Question 13

Do you agree that it would be beneficial for the 2015 Regulations be amended so that Category 1 bodies would be under a duty to consider and publish audit letters received from the local auditor whenever they are issued, rather than, as is currently the case, only following the completion of the audit? (agree, disagree, unsure)

Do you have any comments on this issue?

73. We agree that it would be beneficial for the 2015 regulations to be amended so that Category 1 bodies would be under a duty to consider and publish audit letters received from the local auditor whenever they are issued.
74. The proposed arrangements would enable more timely public reporting and ensure that the public can hold local authorities accountable in terms of financial sustainability and governance, rather than having to wait for the completion of the audit.

Question 14

Do you have any comments on whether any of the proposals outlined above could have disproportionate impact, either positively or negatively, on people with protected characteristics or wish to highlight any other potential equality impacts?

75. We have no comments in this regard.

Question 15

Finally, we would also welcome further comments on the proposed changes to the 2015 Regulations not covered by the questions above, including relating to any unintended consequences.

(Where possible, please limit your response to 500 words)

76. We believe that guidance is needed of what is best practice for audit firms to follow when the backstop proposals are implemented. This is due to this being an unprecedented situation which causes uncertainty and risk for auditors' compliance and technical teams in ensuring that they are able to deliver an ISA compliant audit.

77. There are concerns that audit firms may be left to figure this out for themselves. This may lead to inconsistencies between firms in how they approach auditing local authorities, which may detrimentally impact different local authorities, who, for example, may have their accounts disclaimed when a different firm may have taken an alternative approach to the audit. An overarching framework in this area would therefore provide clarity to audit firms and hopefully lead to a more consistent approach across the sector.