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Consultation Document on the Revision of Practice Note 10: Audit of Financial Statements and regularity of Public Sector Bodies in the United Kingdom (revised 2022)

Thank you for giving us the opportunity to comment on the Public Audit Forum's exposure draft for the 2022 revision of *Practice Note 10: Audit of Financial Statements and Regularity of Public Sector Bodies in the United Kingdom (PN 10)*

Overall, we are very supportive of the proposals within the exposure draft and have included some suggestions where areas could be further clarified. Our detailed responses to the consultation questions listed on the invitation to comment are set out below

Question 1: *This version of Practice Note 10 includes changes to the section on ISA (UK) 320 (Revised June 2016) Materiality in planning and performing an audit concerning the determination of materiality for the financial statements as a whole and the materiality level(s) to be applied to specific 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. Further guidance is also provided in Part 2 on the determination of a separate materiality threshold for the regularity opinion. Do you consider the revised draft provides appropriate and useful guidance on applying materiality to the audit of public sector financial statements and regularity? What changes should be made, if any?*

We very much welcome the proposed guidance on the application of materiality in the public sector. We consider the draft revisions to Practice Note 10 provide appropriate and useful guidance on applying materiality in line with ISA (UK) 320 (Revised June 2016) in a public sector context. In particular, for the financial statements audit, applying a lower materiality to specific classes of transactions, account balances or disclosure where a misstatement could influence the decisions of users of the financial statements should help auditors to direct resources more effectively on things which matter most to stakeholders.

If Practice Note 10 could more explicitly set out the affect this could have on Local Government audits by

setting out that auditors could set a lower materiality to specific classes of transactions and account balances where a misstatement would affect the General Fund, at a level similar to current overall materiality, compared to misstatements which do not, such as PPE balances and PFI liabilities, where a higher headline materiality would be appropriate, this would be beneficial. For example, specifying that a materiality circa 5-10 times larger than currently used, based on total assets would be applied with a lower specific materiality applied to certain account balances.

The illustrative examples in this version of Practice Note 10 are useful in demonstrating the application of ISA (UK) 320 (Revised June 2016). Equally, the draft revised Practice Note 10 clearly sets out the different approaches to materiality with respect to the Regularity opinion for public sector accounts. However, these could go further by setting out expected percentages (e.g. 10% of total assets versus 2% expenses currently). Moreover, in addition to the clarification in the materiality guidance we believe PAF should consider further changes which results in an audit approach for property valuations which reflects the low importance of these assets to the users of the financial statements. This could include reflecting the low risk of management manipulation and the low risk to the local authority.

Question 2: *The previous section on ISQC (UK) 1 has been replaced by guidance on applying ISQM (UK) 1 in the public sector, including for contracted-out audits. Does this section provide appropriate and useful guidance on quality management arrangements for statutory and contractor auditors of public sector entities? What changes should be made, if any?*

Our view is that this sector provides sufficient and appropriate guidance on quality management arrangements in the public sector when applying ISQM (UK) 1. We do not propose any further changes to this section of the Practice Note.

Question 3: *The section on ISA (UK) 315 includes additional examples of inherent risk factors that may be particularly relevant to public sector entities. Are these example inherent risk factors relevant to public sector audits and do they encompass the common areas of inherent risk that are particular to public sector entities?*

The section on ISA (UK) 315 contains some useful example risk factors such as differing incentives and pressure from the private sector, which “may be more focused on information about the profitability and solvency of the entity, those present in public sector entities may be to influence information on stewardship of public funds, service delivery, compliance with government requirements and policies and matters that may be politically contentious.”

The identification of risk factors is the responsibility of the engagement team and cannot be prescribed and this section clearly sets out these are example risk factors only and should not be used like a checklist for teams, who should continue to apply professional judgement. They do encompass the common areas of inherent risk factors specific to public sector entities.

Question 4: *The section on the audit of regularity reflects existing practice in the public sector. Do you consider that the guidance in Part 2: The audit of regularity is appropriate, sufficient and applicable to all parts of the public sector? If not, what changes would you like to see made and why?*

We consider that “Part 2: The audit of regularity” is appropriate, sufficient and applicable for CCGs where we have given this opinion. The fact this opinion only applies to certain areas within the public sector could be clarified further. Examples of when a modification may be incurred in certain sectors would be helpful. For example, in the NHS, prior to their dissolution Clinical Commissioning Groups (CCGs) had a number of statutory duties, including a duty that gross expenditure should not exceed income. A breach of these duties could result in a qualification of a regularity opinion and is relatively common in the sector. Once the framework for the new Integrated Care Boards is established it would be useful to provide an example for this new type of body.

Question 5: *The consultation draft includes other changes, as outlined in the Annex below. Do the other changes that have been proposed contribute to the objective of providing useful and appropriate guidance for public sector auditors? If not, how could these be improved?*

We welcome the proposed update in respect of ISA (UK) 570 are useful in clarifying that going concern is based on the continued provision of services, and that uncertainty around future funding or existence does not create a material uncertainty in relation to going concern.

We would add that, a public body could deliver a wide range of services, some of which are discretionary. It is possible that such a body could decide to discontinue providing some of these services (for either strategic or financial reasons) while continuing to provide others. It would be helpful if para 1-154 (or another suitable para) could clarify that a body's decision to discontinue the provision of some services is not a reason in and of itself for the 'continued provision of services' approach not to be applicable. Rather, an auditor's judgement on 'continued provision of services' should be made for the body as a whole, taking into account whether the services that a body is discontinuing are discretionary. It would also be helpful if guidance could be provided to cover the scenario where a public body has a subsidiary, joint venture or associate for which the auditor of the subsidiary, joint venture or associate has reported a 'material uncertainty related to going concern' in respect of the subsidiary, joint venture or associate's financial statements.

We have no comments on other proposed changes.

Question 6: Are there any other changes you believe would be appropriate? If so, what changes would you like to see made and why?

There are no further changes which we propose in respect of the Practice Note.

Question 7: The Auditor General for Wales and the Wales Audit Office are required to comply with Welsh Language Standards that provide for the Welsh language not to be treated less favourably to the English language in Wales and for individuals to be able to access public services in Wales through the Welsh or English languages. Do you consider there to be anything in this consultation draft that undermines these requirements? Do you consider there is any revision that could be made to support the use of the Welsh language?

We have no comments on this area.

I hope these responses are constructive and helpful. If you would like to discuss any of them further, please do not hesitate to contact me.

Yours sincerely



Jon Roberts
Partner