EXPLANATORY MEMORANDUM TO

THE ACCOUNTS AND AUDIT (AMENDMENT) REGULATIONS 2024

2024 No. 907

1. Introduction

1.1 This explanatory memorandum has been prepared by the Ministry of Housing, Communities and Local Government and is laid before Parliament by Command of His Majesty.

1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Declaration

2.1 Jim McMahon, Minister of State for Housing, Communities and Local Government at the Ministry of Housing, Communities and Local Government confirms that this Explanatory Memorandum meets the required standard.

2.2 Rosie Seymour, Deputy Director for Local Government Accountability and Audit, at the Ministry of Housing, Communities and Local Government confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Policy officials at the Ministry of Housing, Communities and Local Government localaudit@communities.gov.uk can be contacted with any queries regarding the instrument.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 This instrument amends requirements for 'Category 1' bodies in the Accounts and Audit Regulations 2015 (S.I. 2015/234) (the "2015 Regulations") as part of measures to address the significant backlog of local audits in England. Category 1 bodies defined in regulation 2(1)[1] of the 2015 Regulations) encompass local authorities, police and fire bodies, as well as bodies such as National Parks Authorities, waste authorities and Passenger Transport Authorities.

[1] https://www.legislation.gov.uk/uksi/2015/234/regulation/2. In accordance with Regulation 2, local bodies listed in Schedule 2 to the Local Audit and Accountability Act 2014 are considered Category 1 bodies unless they are smaller authorities (or NHS bodies, to which the Regulations do not apply). Schedule 2 bodies are in England with the caveat that under paragraph 29 relevant authorities include: *Any person or body exercising functions in relation to an area wholly in England or partly in England and partly in Wales—*
(a)which was originally subject to audit provisions contained in an enactment passed before the Audit Commission Act 1998, and
(b)to which the audit provisions of that Act applied by virtue of paragraph 4(1) or 7 of Schedule 4 to that Act immediately before the repeal of section 2(1) of that Act by this Act.

4.2 This instrument will require Category 1 bodies – unless limited exemptions apply – to publish outstanding audited accounts for financial years up-to-and-including 2022/23 by a statutory backstop date of 13 December 2024 and sets a series of further backstop dates for financial years 2023/24 to 2027/28. Other changes include, from financial year 2024/25, providing Category 1 bodies with an additional month to prepare and publish unaudited (draft) accounts (which enables the period for exercise of public rights under sections 26 and 27 of the Local Audit and Accountability Act 2014 to commence[2]).

4.3 This instrument also makes consequential changes to the Non-Domestic Rating (Rates Retention) Regulations 2013 (S.I. 2013/452 - 'RR Regulations') and the Non-Domestic Rating (Transitional Protection Payments) Regulations 2013 (S.I. 2013/106 - 'TPP Regulations'), which relate to the Business Rates Retention System. These changes will align the RR Regulations and TPP Regulations with the 2015 Regulations, by replacing the existing dates for the provision for the end of year calculations, with the statutory backstop dates in the years that these backstop dates apply.

Where does the legislation extend to, and apply?

4.4 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is England and Wales.

4.5 The territorial application of this instrument (that is, where the instrument produces a practical effect) is England and Wales.

5. Policy Context

What is being done and why?

5.1 Category 1 bodies provide vital public services to local communities. Effective local audit ensures transparency and accountability for public money spent on these services, and builds public confidence.

5.2 The timeliness of local audit completion and subsequent publication by local bodies has, however, been deteriorating in recent years. There is now a significant backlog of unaudited accounts in England. For the 2022/23 financial year, just one percent of Category 1 local bodies in England published audited accounts on time. Without action, the backlog will continue to grow. This would also hamper necessary fundamental reforms to repair the system.

5.3 On 30 July 2024, Jim McMahon, Minister of State in the Ministry of Housing Communities and Local Government, published a Written Ministerial Statement outlining actions the Government – together with the Financial Reporting Council (FRC), the National Audit Office (NAO), and organisations in the wider system – is taking to address this backlog and put local audit on a sustainable footing. The approach was also tested via a public consultation, which ran between 8 February and 7 March 2024 (see also consultation section below).

5.4 New regulation 9A (to be inserted into the 2015 Regulations by regulation 2(3) of this instrument) will require local bodies, where they have not done so already, to publish audited accounts for financial years 2015/16 up-to-and-including 2022/23 by a backstop date of 13 December 2024. More specifically, bodies will be required to

[2] See regulation 2(1) of the 2015 Regulations for the definition of "period for the exercise of public rights" and regulation 15 for provision about when this period is to take place.

publish their accountability statements (defined in regulation 9A(9)), which includes the audit opinion.

5.5 The 13 December backstop will help clear the backlog and enable a focus on recent accounts, where assurance is most valuable. Given the size of the backlog, however, it is unlikely that all outstanding audits will be completed in full by that date. This is likely to have unfortunate consequences for the system in the short term. Where auditors have been unable to complete audits, they will issue a 'disclaimed' or 'modified' audit opinion. Auditors are likely to issue hundreds of disclaimed audit opinions, and disclaimed opinions will likely continue for some bodies for several years.

5.6 Regulation 9A(3) sets five further backstop dates for financial years 2023/24 to 2027/28. These are:

- Financial year 2023/24: 28 February 2025
- Financial year 2024/25: 27 February 2026
- Financial year 2025/26: 31 January 2027
- Financial year 2026/27: 30 November 2027
- Financial year 2027/28: 30 November 2028

5.7 These backstops will enable auditors to rebuild assurance following disclaimed or modified opinions over several audit cycles rather than in a single year, reducing the risk of the backlog re-emerging. It is the aspiration of the Government and key local audit system partners that, in the public interest, local audit recovers as early in this five-year period as possible. This means disclaimed opinions driven by backstop dates during this period should, in most cases, be limited to financial years 2023/24 and 2024/25.

5.8 While there will be modified and disclaimed opinions, auditors' other statutory duties – including to report on Value for Money arrangements, to make statutory recommendations and issue Public Interest Reports – remain a high priority.

5.9 Alongside these Regulations, the Government has laid the draft Code of Audit Practice 2024 on behalf of the Comptroller & Auditor General. The changes being delivered via this replacement draft Code are part of the same package of measures to deal with the audit backlog. Changes in the draft Code will, for example, introduce a requirement on auditors to issue their opinion in time for local bodies to publish their accounts by the relevant backstop date.

5.10 Regulation 9A(5) will exempt local bodies from publishing audited accounts by a backstop date in exceptional circumstances. A body may be exempt where the auditor has not entered their opinion by the relevant backstop date and one of the following circumstances apply: the auditor is considering a material objection[3]; an objector has appealed or could still appeal the auditor's decision in relation to the objection; the auditor thinks that an item of account may be contrary to law and has made, or is considering making, an application to the Court on that basis; or from 2023/24, if the auditor is not yet satisfied with the body's Value for Money arrangements. These

[3] Chapter 2 of the draft Code of Audit Practice 2024 sets out certain circumstances in which auditors are exempt from the requirement to provide their opinion in time for the body to comply with the backstop dates. One such circumstances is where the auditor is considering an objection that may have a material impact on their opinion on the financial statements (see paragraph 2.13).

exemptions also align with those for auditors set out in the Comptroller & Auditor General's replacement draft Code of Audit Practice 2024.

5.11 Regulation 9A(4) includes a requirement on exempt bodies to publish an explanation of their exemption on (or, if necessary, as soon as reasonably practicable after) a backstop date and to publish its accountability statements (including the audit opinion) as soon as practicable. These requirements will ensure transparency and ensure that audited accounts are published promptly once the underlying conditions of the exemption no longer apply.

5.12 Regulation 9A(9), which defines the accountability statements to be issued by the backstop dates, makes publication of the audit opinion a requirement but would, if necessary, enable a body to meet the backstop without publishing the audit certificate (confirmation from an auditor that they have finished an audit). This is because there are some circumstances in which an auditor will be able to issue their opinion, but not yet have discharged all their statutory functions or duties – this could include, for example, consideration of a non-material[4] objection. (For the same reasons, this instrument also amends the reference to the opinion and certificate in existing regulation 10(1)(a), which applies from financial year 2028/29 onwards.)

5.13 Regulation 9A(6) will require a body that fails to comply with a backstop date to publish an explanation, to send a copy of this to the Secretary of State (to facilitate further scrutiny) and publish audited accounts as soon as practicable. To complement this regulation change, the Government will publish a list of bodies and auditors that do not meet the proposed backstop dates, which will also make clear where unaudited (draft) accounts have not been published. These steps are important for ensuring transparency and accountability. The Government will also keep the issue of consequences under close review and may explore further mechanisms to take appropriate action.

5.14 For financial years 2024/25 to 2027/28, regulation 5 will amend existing regulation 15 to change the date by which bodies must publish draft (unaudited) accounts from 31 May to 30 June following the financial year to which they relate. This will give those preparing accounts more time to ensure they are high-quality accounts. This should, in turn, benefit auditors while still ensuring publication and commencement of the period for exercise of public rights shortly after financial year end.

5.15 Regulation 20 in the 2015 Regulations currently specifies that when, following completion of an audit, a relevant authority receives an audit letter, they are required to consider and publish it. This instrument will ensure that Category 1 authorities are required to consider and publish annual audit letters or auditor's annual reports that are issued under the relevant Code of Audit Practice whenever they are received, as opposed to only upon completion of an audit. This supports changes being made via the draft Code of Audit Practice 2024 to help restore timely reporting of auditors' work on arrangements to secure value for money.

5.16 All key local audit organisations support the package of measures to tackle the audit backlog, recognise their exceptional nature, and continue to share the conviction that this urgent and decisive action is needed. Taken together, these proposals aim to facilitate a return to timely, purposeful audits.

[4] Schedule 4 and Chapter 4 to the 2024 Code states that auditors may be able to issue the audit report on the financial statements, but cannot certify completion of the audit because they are considering an objection made under Section 26 of the 2014 Act.

5.17 The Government will also update Parliament in the Autumn on longer-term plans to fix local audit.

What was the previous policy, how is this different?

5.18 The key changes are set out above.

6. Legislative and Legal Context

How has the law changed?

6.1 The 2015 Regulations set out the detailed requirements on relevant authorities (other than health bodies) in relation to duties to keep adequate accounting records and to prepare a statement of accounts (under section 3 of the Act) and rights of local electors to inspect documents and make objections in relation to the audit of those accounts (under sections 26 and 27).

6.2 Under regulation 10 of the 2015 Regulations, relevant authorities are required to publish by a specified date their statements of accounts together with any certificate or opinion entered by the local auditor (and associated other documents). The dates in regulation 10 have been amended several times in relation to specified financial years, due to the chronic difficulties in the local audit system in England which has led to a large backlog of unaudited accounts.

6.3 This instrument amends the 2015 Regulations to apply regulation 10 to financial years beginning in 2028 onwards and inserts a new regulation 9A which provides for amended deadlines for publishing audited accounts, and the associated documents, for the financial years from 2015/16 up to and including 2027/28.

6.4 It also amends regulation 15 of the 2015 Regulations, which relates to the period during which local electors may exercise public rights of objection, inspection and questioning of the local auditor under sections 26 and 27 of the Act, for the financial years from 2024/25 up to and including 2027/28.

6.5 Regulation 20 is amended so that relevant authorities are now required to consider any audit letter or auditor's annual report whenever received and not only after the audit has been concluded. In connection with the amendments to regulation 20, regulation 2(1) is amended to include a reference to the "auditor's annual report" under the Codes of Audit Practice published in 2020 and 2024.

6.6 The RR Regulations and TPP Regulations make provision about the end of year calculations which must be performed by certain local authorities pursuant to the business rates retention system. The deadlines for performing these calculations are linked to the deadlines for publishing audited accounts and are therefore amended in consequence of the new dates.

Why was this approach taken to change the law?

6.7 This is the only possible approach to make the necessary changes.

7. Consultation

Summary of consultation outcome and methodology

7.1 Section 32(3) of the Local Audit and Accountability Act 2014 requires that, before making any regulations under that section, the Secretary of State must consult named stakeholders. These are: the Comptroller and Auditor General of the National Audit

Office, such representatives of relevant authorities as the Secretary thinks appropriate, and the recognised supervisory bodies.

7.2 Between 8 February and 7 March 2024, the Department for Levelling-Up Housing and Communities consulted on amending the Accounts and Audit Regulations 2015 as part of measures to tackle the local audit backlog. All the named stakeholders were consulted, and responses were welcomed from any individual or entity interested in the proposals, including all relevant local bodies, audit firms, and other organisations which form part of the local audit framework. There were 191 responses to the consultation. The Government has published a response to feedback on the consultation[5] in parallel to laying this instrument.

7.3 Consultation feedback demonstrated strong support for setting a statutory backstop to clear outstanding audits up-to-and-including financial years 2022/23. Many respondents expressed the view that this is a necessary and pragmatic step to clear the current backlog. Many also highlighted the lack of viable alternatives. The consultation proposed a backstop date of 30 September 2024, but given the General Election and the dissolution of Parliament this date was no longer feasible. The 13 December 2024 backstop set out in this instrument represents the earliest viable alternative and has been tested with audit firms, representatives of local government and key system partner organisations.

7.4 The consultation also tested views on the following backstop dates for financial years 2023/24 to 2027/28:

- 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

7.5 A majority of those who responded to this consultation question supported the dates. A notable number of respondents expressed concern that a 31 May 2025 deadline (for financial year 2023/24) would clash with the unaudited (draft) accounts deadline for financial year 2024/25 (also currently 31 May 2025), as well as concerns regarding the interaction with auditors' NHS audit work[6]. Of those who suggested alternatives, a clear majority supported an earlier backstop for financial year 2023/24.

7.6 This instrument sets a backstop date of 28 February 2025 for financial year 2023/24 and this will negate the issues highlighted with the proposed 31 May 2025 date. It will also ensure that the backstop will not fall within pre-election periods for local authorities, an issue that the Local Government Association (LGA) have emphasised as important. This instrument also differs from the consultation approach by setting a deadline of 27 February 2026 for financial year 2024/25, which will ensure that this backstop does not fall within pre-election periods for local authorities. In addition to being shaped by consultation feedback, the updated backstop dates have been considered further with audit firms, representatives of local government and key system partner organisations.

[5] https://www.gov.uk/government/consultations/addressing-the-local-audit-backlog-in-england-consultation
[6] Under regulation 15(1)(a) the public inspection period must include the first 10 working days of June. By extension, this requires the publication of unaudited (draft) accounts by 31 May at the latest.

7.7 More broadly, some consultees expressed concern or uncertainty regarding the scale of modified or disclaimed audit opinions that would be issued due to the statutory deadline; the impact of these opinions on the subsequent processes by which auditors would rebuild assurance; and the risk of reputational impacts on local bodies of disclaimed or modified opinions.

7.8 The Government recognises that clearing the backlog is also likely to have unfortunate consequences in the short term. However, this approach will enable a focus on recent accounts, where assurance is most valuable, and all key local audit organisations support these bold measures, while recognising their exceptional nature. It is the aspiration of the Government and key local audit system partners that, in the public interest, local audit recovers as early in this five-year period as possible. This means disclaimed opinions driven by backstop dates during this period should, in most cases, be limited to financial years 2023/24 and 2024/25.

7.9 In relation to potential reputational impacts for relevant authorities, there will be extensive communications and engagement, to make clear the necessity of these steps and emphasise the context for modified or disclaimed opinions. Local bodies should not be unfairly judged based on disclaimed or modified opinions, caused by the introduction of backstop dates that are largely beyond their control. Auditors will be expected to provide clear reasons for the issuing of such opinions to mitigate the potential reputational risk that local bodies may face. The Government will work with partners to provide communications support to the system.

7.10 In response to other aspects of the proposals, consultees indicated clear support for extending the deadline for the publication of unaudited (draft) accounts (many expressed specific support for a 30 June deadline), as well as for changes to ensure that local bodies consider and publish auditors' annual letters or auditors' annual reports whenever they are issued.

7.11 Consultees also highlighted systemic issues in the audit system. The Government was elected with a manifesto commitment to overhaul the local audit system. As set out in the WMS of 30 July 2024, it will continue to review the evidence, including considering the recommendations of external reviews to date, and will update Parliament in the Autumn on longer-term plans to fix local audit.

8. Applicable Guidance

8.1 The NAO will publish supplementary guidance for auditors on the impact of backstop arrangements on audits of English local bodies. We will continue to work with system partners on the need for further guidance and information.

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A full Impact Assessment has not been prepared for this instrument because the overall impact on business, charities or voluntary bodies is unlikely to be significant. This instrument has no impact in isolation, but is intended to work alongside the new draft Code of Audit Practice (which is being laid before Parliament at the same time as this instrument) and this section describes the combined impact of this instrument and the draft Code. A proportionate level of analysis has been produced for this combined impact and is summarised below in 9.2.

Impact on businesses, charities and voluntary bodies

9.2 Local public audit in England is provided by privately operated audit firms. There is no significant impact on business because auditors will be paid for the cost of work they undertake that arises from the changes, which will be a positive impact overall for the audit providers. The proposals have been consulted upon and extensively discussed with audit firms. Issuing a disclaimed or modified audit opinion and a subsequent return to being able to fully complete audits will require differing levels of work by auditors.

9.3 There is no impact on charities or voluntary bodies because they are not within the scope of the SI (they are not Category 1 authorities).

9.4 The legislation does not impact small or micro businesses.

9.5 The impact on the public sector is that local public bodies in England will pay audit fees to restore full assurance on their accounts where auditors have disclaimed or qualified their opinions on previous accounts as a result of the backstop provisions. Work is ongoing to understand the financial impact further and consequent action.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 The impact of this legislation will be kept under review by the Department and in discussion with partner organisations in the local audit system.

10.2 The regulations do not include a statutory review clause as the SI does not regulate business or voluntary bodies.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 As set out above, the changes are part of a wider package of urgent measures to tackle the local audit backlog in England. The replacement draft Code of Audit Practice 2024, which has been laid in parallel, is a complementary part of this package. For example, while this instrument will require Category 1 bodies to published audited accounts by backstop dates, the draft Code will introduce a requirement on auditors to issue their opinion in time for local bodies to publish their accounts by the backstops.

11.2 This instrument is being laid in proximity to the beginning of Conference Recess. Laying the regulations at this juncture will provide further and vital direction to the sector ahead of the 13 December 2024 backstop date. It will also ensure a coming into force date of 30 September 2024, which is the current deadline for the publication of audited accounts for financial year 2023/24.

12. European Convention on Human Rights

12.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 (“relevant European Union Acts”).