2019 Local Audit Transparency Report - Deloitte LLP

Reporting on our audits of English NHS Trusts, Local Authorities and Clinical Commissioning Groups

For the year ended 31 May 2019
Regulatory context

Public sector bodies in the United Kingdom have differing audit requirements and arrangements, depending upon the country and the type of body. ‘Local audits’ (or ‘local public audits’) are audits of English bodies conducted in accordance with the Local Audit and Accountability Act 2014. These local audits cover Local Authorities, Clinical Commissioning Groups, and NHS Trusts (but not NHS Foundation Trusts).

This Local Audit Transparency Report (Report) is in respect of local audits, and has been prepared in accordance with The Local Auditors (Transparency) Instrument 2015. It is required because one of the three local audit reports (each of which was an NHS Trust) which we issued during the year ended 31 May 2019 was in respect of a major local audit as defined in The Local Audit (Professional Qualifications and Major Local Audit) Regulations 2014. The appendix (on page 40) includes a summary of the requirements of The Local Auditors (Transparency) Instrument 2015 and where these requirement are addressed within this report.

We have been appointed as auditors for 36 local government bodies (including pension schemes), commencing with the audit of the annual accounts for the year ended 31 March 2019. This Report includes details of our arrangements relevant to these audits, which had commenced during the year ended 31 May 2019. However, due to the timing of local government audits, we had not issued any audit reports in respect of these bodies during the year ended 31 May 2019.

Our local government audit appointments were made by Public Sector Audit Appointments Limited (PSAA) as an appointing person under the provisions of the Local Audit and Accountability Act 2014 and regulation 3 of the Local Audit (Appointing Person) Regulations 2015. PSAA’s role includes contract management with Deloitte and other audit firms for the delivery of consistent, quality and effective audit services to relevant authorities. Further details in respect of these audits, and of our audit reports made in respect of annual accounts for the year ended 31 March 2019, will be included in our Local Audit Transparency Report for the year ended 31 May 2020.

Our arrangements in respect of NHS Foundation Trusts (which are not required to be included in this Report under The Local Auditors (Transparency) Instrument 2015) are consistent with those for local audits.

An Audit Transparency Report prepared in accordance with Article 13 of the Regulation No 537/2014 of the European Parliament and of the Council of 16 April 2014 (the EU Audit Regulation) will be issued by 30 September 2019. For further detail on several of the areas covered by this Local Audit Transparency Report, we recommend you read that wider Audit Transparency Report.

There is a list of Local Audits in Appendix 1 on page 38.
Contents

Deloitte UK: legal structure and ownership  | 4
Deloitte UK: governance and management  | 5
Independent Non-Executives  | 7
Deloitte network  | 8
Delivering quality audits  | 9
External and internal audit quality monitoring  | 22
Independence  | 32
Appendices  | 37
Deloitte LLP is a limited liability partnership, incorporated under the Limited Liability Partnerships Act 2000 and is wholly owned by its members (which comprise the UK and Swiss equity partners and Deloitte NSE LLP). The firm provides audit, risk advisory, tax, consulting and financial advisory services in the UK, Channel Islands and Isle of Man and through its subsidiaries in Switzerland and Gibraltar.

With effect from 1 June 2017, Deloitte LLP became the UK affiliate of Deloitte North West Europe (NWE) LLP, a member firm of the Deloitte network and, with effect from 1 June 2019, Deloitte NWE LLP was renamed Deloitte North and South Europe (NSE) LLP. The governance arrangements are set out below.

Deloitte LLP operates an integrated business model: each of our service lines applies a common set of procedures and policies, where appropriate, and each has developed additional and bespoke policies and guidance to reflect the specific requirements of its business offerings. For the purposes of transparency reporting, this report contains information about Deloitte UK which is relevant to all of the service lines, as well as specific matters relevant to the audit and local audit business.

During the year ended 31 May 2019 the public sector audit practice was operationally part of Risk Advisory, as part of our Audit & Risk Advisory service line. From 1 June 2019, the Audit & Risk Advisory service line was divided into two separate service lines: Audit & Assurance and Risk Advisory. As part of the change in structure, and driven by audit quality considerations, the public sector audit practice was moved from Risk Advisory to sit within the Audit & Assurance service line to ensure continued access to the necessary skills and experience.

For the purposes of this report all references are to Audit & Assurance but under both organisational structures all accredited audit staff were, and are, subject to the same internal controls and training processes as each other, as described within this report.
Deloitte UK: governance and management

The roles, responsibilities and membership of the key elements of our UK governance and management structures are set out below. Further details regarding our legal structure and governance will be included in the main transparency report to be published in September 2019.
The role of the Senior Partner and Chief Executive

The UK Senior Partner and Chief Executive is appointed by the NSE Senior Partner and Chief Executive, subject to confirmation by a resolution of the UK equity partners, for a term not exceeding four years.

David Sproul served as Senior Partner and Chief Executive of the UK Practice during FY19 and until 31 May 2019. Richard Houston is the current Senior Partner and Chief Executive of the UK Practice and has full executive authority for its management. In keeping with our client service focus, he continues to spend a significant proportion of his time actively engaging with a broad cross-section of clients.

Richard began his first term as UK Senior Partner on 1 June 2019. He is also Senior Partner and Chief Executive of Deloitte NSE.

The responsibilities of the Senior Partner and Chief Executive fall under five principal headings:

- The business of Deloitte, including the development and management of professional services at the highest level of quality, and compliance with all regulations
- The development of policies and strategic direction
- Financial performance
- Partners, including the development and management of our talent goals
- International, representing Deloitte UK within Deloitte Global

Richard communicates regularly with the partner group, and with all of our people, in person and through a series of webcasts, voicemails and email alerts.

Biographical details of members of the firm’s governance structure and management team, along with details of their meeting attendance, will be provided within an appendix to the main transparency report to be published during September 2019.
Independent Non-Executives

**INEs’ Duties**
The INEs serve on the UKOB and meet as a separate group to discuss matters relating to their remit. They participate in the UKOB’s activities in relation to promoting the success of the firm by directing and supervising its affairs.

Additionally the INEs participate in other activities of the firm consistent with their role and experience such as promoting audit quality; helping the firm secure its reputation more broadly, including in its non-audit businesses; and reducing the risk of firm failure.

**Supporting the INEs**
To assist the INEs in discharging their role, the firm provides them with:

- A chief of staff to assist the INEs in navigating the business and discharging their responsibilities under the Audit Firm Governance Code
- Any information they require about any aspect of the firm’s business (subject to individual client confidentiality and audit independence rules)
- Secretarial support
- Access to independent professional advice at the firm’s expense where judged necessary to discharge their duties (having first discussed such request with the UKOB Chair); and
- Any other support agreed upon from time to time.

**INEs’ other directorships and business interests**
The INEs have various business interests, other than those of the firm, which help them bring appropriate challenge and different perspectives to the firm by drawing on their diverse external roles and experiences.

They have been (and continue to be) members of a number of audit committees, including an INE with experience of auditing and accounting through their qualification as a Chartered Accountant and various accounting roles throughout their career.

The INEs declared any pre-existing assignments (including any appointments, directorships or posts) and potential conflicts of interest apparent at the time of appointment. They cannot be a director or officer of a restricted entity of the firm (i.e. any entity audited by a Deloitte network firm, affiliates of entities audited by a Deloitte network firm and other assurance clients for which the firm has to maintain its independence).

The INEs are required to consult with the Chairman of the UKOB and obtain his written consent prior to accepting any further assignments with a third party. In the event that an INE becomes aware of any actual or potential conflict of interest or any threat to the firm’s independence, the INE is required to disclose it to the Chairman as soon as it becomes apparent.

**Independence of INEs**
In assessing the independence of the firm’s INEs, we:

- Considered the INEs’ financial interests and business, family and employment relationships entered into and notified to the firm
- Applied the Audit Firm Governance Codes (‘the Code’s’) principles and complied with its provisions on INEs without placing them in the chain of command; and
- Considered the independence requirements of the UK and US regulators, as well as those of the International Federation of Accountants

**Appointment of INEs**
The firm’s INEs are, subject to earlier termination, appointed for an initial period of three years. Unless the appointment is renewed on or prior to the termination date, the INE will cease to be an INE on termination of the appointment.

We are mindful of the Code requirement for Independent Non-Executives to be “appointed for specific terms and any term beyond nine years should be subject to particularly rigorous review and explanation” and will take any necessary action as and when appropriate.

**Termination of appointment of INEs**
The appointment may be terminated at any time, by either the INE or by the firm, with three months’ written notice. The appointment may also be terminated by the firm with immediate effect should any situation arise which amounts to a professional conflict of interest or breach of independence rules.

**Other matters**
Appropriate indemnity provisions are in place in respect of any legal action against any INE and sufficient resources are provided by the firm to enable the INEs to perform their duties.

A process has also been established to resolve any disputes between the INEs and the governance structures and management of the firm.
Deloitte network

The Deloitte network is a globally connected network of member firms and their affiliates operating in more than 150 countries and territories across the world. These separate and independent member firms operate under a common brand.

**Deloitte Touche Tohmatsu Limited** (DTTL or Deloitte Global).

Deloitte Touche Tohmatsu Limited is a UK private company limited by guarantee. DTTL serves a coordinating role for its member firms and their affiliates by requiring adherence to policies and protocols with the objective of promoting a consistently high level of quality, professional conduct and service across the Deloitte network. DTTL does not provide professional services to clients, or direct, manage, control or own any interest in any member firm or any member firm's affiliated entities.

For more information about the Deloitte network, please see: About Deloitte.
Delivering quality audits

We set out below the steps we take to deliver quality audits, building on our culture of ethics and integrity and on the recognition that quality is our foundation.

Quality is driven by:

1. Culture
2. People
3. Systems and processes
4. Consistency
1. Culture

Culture is an essential part of our business in engendering and preserving trust and we continue to define our culture and to build confidence and trust in our profession.

Tone at the top

The tone at the top is consistently honest and clear. This is cascaded throughout our business by maximising firmwide and audit engagement and communication activities. Topics such as pride in our profession, innovation supporting audit quality, the benefits of our Multi-Disciplinary Model to our audit delivery and maintaining professional scepticism regularly feature on our intranet; also leadership questions and answers online, at our annual TechEx training, and at audit business town halls.

Our previous Senior Partner and Chief Executive aired his views on unacceptable workplace behaviours and the shift towards a culture of greater respect and inclusion in the press and on social media. New and mandated respect & inclusion eLearning, for all partners and staff, clearly sets expectations around what a positive and thriving workplace environment and culture looks like for our people.

Our leadership is driving an enthusiastic and engaging approach on ‘what is an audit and why it matters’ in a spotlight series of articles. There they share opinion and their personal experiences to highlight and champion our core values of integrity, objectivity and independence.

An edition of our ‘Essential Professional Update’ video, produced for all qualified audit professionals to watch in advance of audit ‘busy season’, reinforces the audit imperatives (see page 21), core principles and ethics to embed quality into everyday activities.
Promoting the purpose of an audit and the societal value that it brings

We established an Audit Culture Working Group in FY19, with representation from across our audit business. It is committed to actively promoting the purpose of audit, reinforcing our core values and acknowledging the behaviours we wish to encourage and reward throughout the firm.

The Audit Culture Working Group, sponsored by our Audit Talent Partner, has made tangible progress by embedding the purpose of audit into induction course content for new and experienced hires. Partner led discussion and storytelling on the purpose of audit now form part of the Engagement Team Based Learning (ETBL) support materials. This places greater emphasis on sharing knowledge and bringing to life practical examples of where audit has made an impact to our stakeholders.

Recognising that it is equally important our people not only understand the purpose of audit, but also feel proud of the work they do, we launched a ‘stories of pride’ campaign. We invited over 100 colleagues to gauge opinions and share stories on what makes them feel most proud to be a Deloitte auditor. The output of this targeted engagement activity were videos on the role of the auditor and how we work together, designed to initiate conversations within audit engagement teams.

In October 2018, we asked over 4,000 staff across the firm what we could do to make Deloitte a better place to work through the first of our ‘Your Voice’ surveys. These surveys are now running every quarter, sharing anonymised responses with leaders to improve our future planning and to focus action in our audit business. They will inform and shape our work around culture by actively listening to what our people are saying and obtaining continuous feedback on topics such as thriving at work, trust, open relationships with others and how we work together, designed to initiate conversations within audit engagement teams.

Recognising positive contributions to high quality audit

We are committed to recognising and celebrating our people who reinforce a culture of wellbeing, personal growth and development and to rewarding exceptional contributions to quality. In 2018, a Deloitte Global working party was set up to consider global reward and recognition in respect of audit quality. Deloitte UK contributed one of the six partners on that working party.

The global working party issued guides designed to help Deloitte member firms recognise the ‘moments that matter’ to encourage our people to step up and be the best that they can be.

In the UK, we used these global guides for partners and staff to develop specific categories around culture and positive behaviours we want to recognise and to provide practical examples of how to acknowledge exceptional contributions to quality based on everyday scenarios.

Individuals from all grades across our business are actively encouraged to nominate their colleagues where they consider exceptional contributions to quality have been made in the following four categories:

» 1. Courageous actions to protect the public interest by upholding our professional standards

» 2. Voluntarily assisting in difficult and challenging matters that arise locally, nationally or globally in order to protect the Deloitte brand

» 3. Agility and capacity to lead change by applying an adaptive mindset and anticipating stakeholder needs to innovate

» 4. A drive to learn and share knowledge and thought leadership through teaching and instilling the knowledge in others

Our recognition and reward scheme for exceptional contributions to quality is open to all Audit & Assurance staff. Over 70 awards were announced in relation to the first six months of the new reward scheme year (December 2018 - May 2019), and we continue to listen, acknowledge and reward our people every quarter, throughout the year.

Management Information

The firm has developed a ‘Do the Right Thing’ dashboard, for use by the UK Executive and reporting to the UKOB. This dashboard provides enhanced oversight on culture, providing the information to assess and challenge how we are performing against our core values of integrity, quality and respect at the heart of everything we do.

The dashboard covers firmwide metrics on Ethics, Quality and Risk, Talent, Stakeholders and Societal Impact. It includes commentary on key trends and areas of strength, areas for improvement and specific areas of focus. Key actions and trends will reside with Audit & Assurance Executive members to prioritise and ensure the right interventions are embedding culture and improvements in desired outcomes. For example, action planning in respect of the ‘Your Voice’ survey results, included in the dashboard, occurs every six months. Dependent on the results, planning will usually direct management focus on areas that are already being targeted, but which require more emphasis. The ‘My Feedback’ tool has also been introduced to address staff sentiment from the survey and make it easier for staff to provide upward feedback. The tool allows our people to give, receive and capture feedback in real time.

The ‘Do the Right Thing’ dashboard was developed as a pilot in the UK as part of a proposed NSE level Partnership Culture framework. A plan is in place to evolve this dashboard and roll it out across NSE.
The role of governance in reviewing and promoting an appropriate culture

It is paramount that the firm’s leadership takes an active responsibility for promoting and establishing our culture, underpinned by the fundamental audit principles of integrity, objectivity and independence.

At its April 2019 meeting, a deep-dive presentation was made to the UKOB into the culture of the firm, encompassing the steps being taken to establish and promote an appropriate culture throughout the firm, and how progress is being measured. Access to the new management information dashboards will enable the INEs to form an independent view of the culture of the firm and, where necessary, to challenge the firms’ leadership and direction.

The UKOB met with the Ethics Partner on two occasions in the last year, to review the Ethics Code of Conduct and the ethical behaviours we want to champion across the firm, as well as to receive updates on the internal investigations process for partners and staff.

In addition, the UKOB has reviewed the adequacy of the whistleblowing procedures in place and has assessed the work undertaken to improve independence compliance through the implementation of Independence Breach Policies.

Conclusion

In summary, our initiatives and targeted actions are moving forwards within the Audit & Assurance Practice and across the firm.

We will continue to define, enhance and embed a culture that builds trust in our profession and to transparently report on this.
2. People

The processes outlined below seek to ensure that the professionals working on our audit engagements have the necessary knowledge, capabilities, experience and competence to deliver work of the highest quality and that they are appropriately supervised by skilled partners and managers.

i) Recruitment

During the year ended 31 May 2019 we recruited 589 people into our Audit & Assurance graduate and school leaver programmes and 21 specifically into public sector audit. We have also recruited experienced hires including audit practitioners from within other Deloitte network firms, and we maintain the high calibre of the people within our Audit & Assurance Practice through a rigorous recruitment process, including skills assessments and competency-based interviews.

ii) Measuring and rewarding audit quality performance

We create an environment where achieving high quality is valued, invested in, measured and rewarded.

Each audit partner, director and manager receives a quarterly quality dashboard recording a variety of audit quality metrics covering their positive contributions to audit quality, including:

- Additional partner review role(s) they may fulfil
- Findings from internal and external audit reviews, and corporate reporting reviews
- Timely completion of appraisal documentation and audit compliance (updates of personal independence and continuing professional development, timely archiving of audit engagement files, and timely completion of essential professional updates and other mandatory audit learning)
- For Responsible Individuals (audit partners and signing directors), any independence breaches and other procedural breaches
- Individuals’ own commentary (if relevant) on positive contributions to audit quality on a quarterly basis

Certain key metrics, such as the results of quality inspections of their audit engagements, are given an increased weighting in formulating an overall audit quality performance score and a Harvey Ball graphic, together with an indication of movement from the previous year, is included. Any failings in certain key quality metrics will apply a restriction to a Harvey Ball result whatever the overall score.
In addition, each Responsible Individual receives an Audit Responsibility Rating, reflecting their roles on audit engagements. This is a key driver in their reward and promotion and recognises the level of risk, complexity and public scrutiny they shoulder in their roles, including any Engagement Quality Control Reviewer roles on audit engagements.

Both the audit quality dashboard and, where relevant, the audit responsibility rating are key inputs into the appraisal and remuneration process for Responsible Individuals (Audit Partners and signing directors) and other staff at manager level and above.

Managers and above are required to set Audit Quality objectives at the beginning of the appraisal year and carry out a self-assessment exercise at year-end to review progress, which are considered as part of annual performance review discussions.

Regular check-in meetings encourage discussions around quality. Feedback is received via ‘snapshots’ for work on engagements and projects and from team leaders throughout the year, and the process is designed to ensure that audit quality is at the core of the appraisal discussion. Individuals are also able to request written feedback to support the discussions. Reward decision-makers review a graph of results for snapshot feedback, quality dashboard results and an individual’s self-assessment review of their quality objectives that have been addressed in their year-end performance discussions as part of the annual reward review process, to gauge a rounded view of individuals’ performance and development needs.

We are committed to furthering our culture of quality and excellence, which expects all our professionals to strive to demonstrate an exceptional contribution to quality.

For staff, we use the annual bonus scheme to recognise the demonstration of exceptional audit quality. The Audit Quality Award scheme further rewards significant contributions to the above positive audit quality behaviours on a quarterly basis. ‘Exceptional’ and ‘Role Model’ individuals are differentiated in the value of vouchers presented, to provide additional recognition for our people who make a significant contribution to positive audit quality.

Partners have an annual goal setting process. A balanced scorecard is used to set objectives across the whole of a partner’s contribution and at the year-end process they are assessed on actual contribution against those objectives. Quality is one of the areas included in the balanced scorecard and partners ensure they pick up any remediation from quality dashboard scores in their quality objectives.

The Peering Regime provides a robust series of peering conversations applied to all recommendations to ensure partners are treated equitably, which includes responses to quality events.

Leadership 360 feedback is sought from a variety of individuals (senior, peers, upward) to assess an individual’s performance against an agreed set of people leadership behaviours, which we believe contribute to tone at the top and influence behaviour around areas such as quality. The output is fed into all areas of partner assessment.

During FY19 the policy on responses to audit quality issues expanded a range of potential remedies in respect of quality matters. The overriding aim of the responses is to improve audit quality and support partners and professionals in achieving this aim and may include:

- 1. Inclusion in the Audit Quality Measurement and Monitoring programme (AQMM)
- 2. Additional coaching and learning for the partner(s) or Director Responsible Individual (RI)
- 3. Financial penalties in the form of bonus or unit reduction

These responses may extend to other partners on the engagement, for example the Engagement Quality Control Review (EQCR) partner, the National Risk Partner (an independent partner assigned to our highest risk audits) or other key audit partners. Involvement of other partners is defined by the causal factor analysis.

To further enhance audit quality and to respond to the restructuring in the Audit & Assurance service line, local audit partners will be included in the FY20 audit appraisal process. The key part in partners’ audit quality evaluation is the Audit Quality Remuneration Committee. The AQRC comprises a small group of partners, independent of the Audit & Assurance Executive, who are respected for their own quality contribution. The AQRC uses the audit quality dashboards and audit responsibility ratings as key tools in their evaluation of partners. While a two-year track record is provided to individuals and appraisers, the AQRC receives four years’ to ensure patterns of behaviour and changes in behaviour are considered. The Committee’s recommendations are used by the Audit & Assurance Executive to make final decisions on audit partner reward and promotion, which are then reviewed by the firm’s overall Executive. In FY19 local audit partners were assessed by the AQRC by exception, if they had any severe negative quality events (for example an adverse inspection result).

For FY19 a new ‘Yellow’ and ‘Red’ card system was introduced for partners, replacing the existing penalty regime. Should there be a negative quality event a partner may receive a yellow card from the AQRC. The individual has one year to reverse the situation by making a positive quality contribution and if, as we hope, that contribution is meaningful the yellow card will be removed. If the situation is not reversed a financial penalty will arise. When a negative quality event is of such significance or represents a recurring quality failure, a financial penalty may be recommended without yellow card suspension.
iii) Learning programmes

Our wider approach to continuing professional development, relevant to all audit staff including those working on local audit engagements, is based around targeted learning programmes, including regular audit, accounting and industry-specific training to keep all our professionals at the forefront of new developments and regulations.

All qualified audit professionals are required to complete annual technical update training – ‘TechEx’ - a residential course covering audit, accounting and other matters such as internal controls, accounting estimates and professional scepticism, audit innovation, audit tools and project management. Experienced partners and technical experts lead the delivery of the course, seeking to ensure consistency, quality and maximum impact.

We have a mandatory global audit learning curriculum for all levels, which promotes consistency with other Deloitte member firms, and incorporates parallel curriculums designed for our practitioners working on PCAOB and ISA engagements. We supplement these courses with UK-specific learning topics and courses, as required, to best meet the needs of our business and markets. Sector-specific courses are provided to particular audit specialisms, for example on financial instruments and loan loss provisions, and for Public Sector auditors there is annual update training on health and higher education.

All of our partners and staff are also supported in their legal, ethical and quality responsibilities by appropriate learning programmes, including regulatory/policy compliance, ethics, personal independence, data privacy and protection, GDPR, insider dealing, anti-money laundering and anti-bribery.

In addition, we run regular Essential Professional Updates for audit professionals, which cover current and emerging audit and accounting matters.

All these programmes are mandatory for our practising auditors and we monitor compliance. Anyone who has not completed the training programmes within the designated timeframe is prevented from participating in audit work until the programmes have been completed.
iv) On-the-job training
We develop our professionals with appropriate mentoring, on-the-job training, regular feedback, appraisal and other support activities, supervised by partners and other senior team members.

In the autumn of each year we run partner-led Engagement Team Based Learning, designed to help our people integrate their learnings from the annual technical update training, and other training courses, into their work on audit engagements.

v) Developing the auditor of the future
As we transform the nature of the audit to a more analytical, data-driven audit, so the nature and skills of the people we have auditing need to evolve and develop.

This starts from the moment they join us from school or university via our Early Career Development Programme (ECDP) which has been launched this year. ECDP will provide them with the building blocks to become both the auditor and leader of the future. Additionally we are enhancing our technical learning curriculum to reflect the nature of work that our people will be doing in the future, focusing on the use of areas such as data analytics and IT to deliver an enhanced higher quality audit.

Additionally we are directly recruiting and developing different types of skills to the traditional accountancy and auditing skills, including deep subject matter expertise in data science and advance project management.

vi) Key partner and staff rotation
We recognise the risk of a threat to independence from prolonged service of partners and key staff on the audit engagement team, and note that audit quality can be enhanced by a fresh look at the engagement. We closely monitor, including with the use of system data, the length of time that partners and key staff spend on each engagement, including across different roles, and implement succession plans where appropriate. Investment has been made to enable monitoring of key partner roles systematically and further work is being taken to enable staff monitoring in the same way.
3. Systems and processes

The steps outlined below demonstrate the investment we have made in our underlying audit methodology, tools and resources to enhance the effectiveness of our audit process as we look to the audit of the future.

i) Audit methodology and software

The Deloitte Audit Approach Methodologies are designed centrally by our global team (to which all Deloitte member firms contribute) and are then tailored to comply with all UK professional standards and legal and regulatory requirements. We also supplement our methodologies for local audits, with specific content for NHS and local government bodies reflecting sector-specific requirements including those of the National Audit Office’s Code of Audit Practice and the supporting Auditor Guidance Notes and Practice Note 10: Audit of Financial Statements of Public Sector Bodies in the United Kingdom.

The core of our methodology is a robust, fact-based risk assessment, with an audit response based on that risk assessment. We continue to enhance our audit methodologies across all the member firms in our network. In 2019 we continued our global, multi-year programme to develop ‘Deloitte Way Workflows’ for each area of the audit, to promote greater global consistency in the execution of our methodology. Each of these workflows includes a Guided Risk Assessment, prescribed tasks and templates, embedded use of analytics and audit delivery centres along with associated guidance and support. These workflows allow us to perform audit work consistently across our global network, and ensure errors are spotted and escalated more readily, to maintain continuous quality improvement.

Our methodologies are built into bespoke software, providing a clear framework of procedures. This also gives our audit partners and staff the tools to help them assess risks and make robust audit judgements, with regular partner and manager involvement from the outset of the engagement, while better managing the progress of engagements and evidencing the appropriate reviews and documents on file. We upgrade the software on a regular basis.

ii) Use of specialists and experts

The use of specialists is vital in our delivery of quality audits. The firm has over 2,000 practitioners (including tax, IT, real estate, actuarial and valuations specialists, as well as our centres of excellence for impairment and pensions) who act as specialists on audits. They share the same culture of delivering audit quality as our audit practitioners, and work as integrated members of our engagement teams.
The use of technical experts in our audits is also key to our ability to deliver audit quality. Our consultation system enables us to record when and in what form – consultation on audit and accounting technical matters with our team of technical experts has taken place. This helps us ensure consistency in response and the ability to identify any trends where further guidance and training may be needed.

iii) Audit engagement acceptance and continuance
For any proposed service, whether it be an audit or any other type of service, we review whether it conflicts with any existing relationship/services (conflict check), and we perform independence checking, client due diligence and anti-money laundering procedures. Each new engagement is assigned an Engagement Risk Rating based on the risk profile of the work, which determines the additional review procedures required to be performed by quality control review partners.

Our risk assessment and due diligence procedures are refreshed at least annually. The full process is repeated when there has been a change to a client ownership structure or to the parties involved in the engagement, or if there is a substantial change in the services provided or in the risk profile.

iv) Audit project management and timing
Our audit milestones programme guides teams to complete key activities by certain deadlines based on the entity’s year end and audit engagement profile. Milestone tracking is supported by bespoke diagnostic software that integrates with our audit software to provide real-time information to partners and staff on the progress of their audits.

v) Audit reporting
We believe that high quality, insightful audit reporting must be carefully tailored to the entity and the requirements of its stakeholders and be clear and unambiguous, including Annual Audit Letters. Effective, clear and timely communication with audit committees, and with others charged with governance, is also key to the quality of our audits. We aim to continually improve the quality of such reporting, including enhancing the clarity of our explanations of the audit process, for example when discussing materiality and the impact this has on the audit work undertaken.

We report on our NHS Foundation Trusts audits in enhanced audit reports¹. All of our enhanced audit reports are reviewed by our Enhanced Auditor Reporting Panel to consider the appropriateness and clarity of the report. This panel also seeks to share best practice in audit reporting and latest developments, such as the changes as a result of EU legislation, to help audit engagement teams give further perspective in audit reports.

We recognise that, in addition to focusing on the quality of our own audit reporting, auditors also have an important role to play in raising the overall quality of the financial statements. In addition to using guidance from our Quality Corporate Reporting Centre of Excellence contributing to improving the production of insightful and accurate financial information by the entities we audit, we provide specific guidance to our local audit teams on sector specific developments and implications of changes in reporting requirements.

vi) Engagement Quality Control Review
For public interest entities, higher risk engagements and certain other specified engagements, an independent EQCR partner has responsibility for the whole of an engagement’s EQCR process, supported by Professional Standards Review (PSR), together with other specialist support as deemed necessary.

PSR supports our high standards of professional scepticism and audit quality by providing independent challenge as appropriate, across our portfolio, focusing on significant accounting, auditing and financial reporting matters, appropriate audit documentation and disclosure areas. We regularly refine this process to reflect evolving audit and professional risks.

The PSR Centre of Excellence provides a dedicated central professional standards review team for many of our engagements, focusing on providing a consistent and knowledgeable approach to their reviews.

The independent EQCR partner role is performed by appropriately skilled and experienced audit partners who would, in other circumstances, be eligible to act as audit engagement partner on the relevant audit engagement. EQCR partners are involved in our public interest entities and higher risk engagements, together with other entities as appropriate. For other engagements, the independent challenge process is undertaken by the PSR team. Neither the EQCR partner nor PSR is part of the entity-facing team; they are therefore well-placed to bring independent challenge to the audit process.

All engagements, where the team is considering issuing a modified audit opinion (including in respect of the audited entity’s arrangements to secure economy, efficiency and effectiveness in the use of resources ("Value for Money"/"VfM"), are subject to an additional level of independent review by the Centre of Excellence for Modified Opinions. This Centre reviews the proposed wording and audit documentation to assess its appropriateness, accuracy and consistency.

¹ Regulatory differences mean that NHS Trusts and local government bodies do not currently require enhanced audit reports, and instead reporting is via the Annual Audit Letter.
vii) Driving continual improvement

We are always looking to improve aspects of our services and use the findings of our internal inspections programme, other internal reviews and external regulatory reviews to enhance our system of quality control. This is led, implemented and monitored at the leadership level by the Audit & Assurance Executive and, in more detail, by the Audit Quality Board (AQB).

We continue to innovate our approach to quality monitoring to lead and align in a world where the economy, political landscape and stakeholders’ expectations evolve over time and live our ambition to be recognised as the standard of excellence. A new, more demanding standard on quality control is being issued to respond to the changes in audit delivery, underlying supporting processes, and public and regulatory expectations. The International Standard on Quality Management 1 (ISQM 1) places an emphasis on the public interest perspective, such that the firm’s strategic decisions and actions, including financial and operational priorities, demonstrate a commitment to quality and to the firm’s role in serving the public interest, by consistently performing quality engagements. We support the aim and structure of the new standard and successful implementation is a key focus for leadership.

viii) Causal Factor Analysis

Where any external or internal inspection indicates that an audit has fallen short of the highest expected quality standards, we perform a robust causal factor analysis to understand the deficiencies and consider what remediation is required. The scope of causal factor analysis includes:

• Engagements receiving adverse ratings in regulatory or internal inspections

• Selected findings arising from inspections of our system of quality control

• Recurring findings across a number of engagements or areas, regardless of inspection outcome

• A selection of our highest quality audits assessed during inspections and other selected examples of good practice

• Others including a selection of first year audits and prior period adjustments

The causal factor process involves a detailed analysis of the audit work in the area of the finding or good practice, review of relevant technical guidance and learning materials, an analysis of relevant audit quality indicators and interviews with key engagement personnel who were responsible for the preparation or review of the relevant area.

Causal factors are reported as part of our inspection summaries to the Audit & Assurance Executive, Audit Quality Board, Emerging Issues Group (EiG) and the UK Oversight Board. Recurring themes, common pitfalls, good practice observations and causal factors are communicated on a regular basis to audit practitioners.

We have made further investment in our causal factor process to increase the dedicated resource in the central team to ensure that, on files where improvement is required, causal factor analysis is performed within 60 days of the findings being identified or the inspection result being notified. We have also formalised the annual plan of work for causal factor analysis in response to a recommendation made in the FRC’s thematic review.

ix) Audit Quality Structures

Audit Quality Board (AQB)

We established our AQB in 2014, comprising partners and directors from across our Audit & Assurance Practice. An INE attended one AQB meeting during the year, by invitation. Its remit is to:

• Develop and govern activities that will achieve sustainable improvements in audit quality

• Implement these improvements across the Audit & Assurance Practice

• Respond to audit quality issues raised by regulators and stakeholders, including the FRC’s Audit Quality Review (AQR) team and the ICAEW’s Quality Assurance Department (QAD)

The AQB meets quarterly and actions driven by the AQB during the year include the matters covered in this section of the report, specifically:

• Outcomes from external and internal inspections and internal monitoring programmes

• Strategic responses to the underlying causes of inspection findings, including recurring underlying causes from year to year

• Further enhancement of the content and delivery of our learning curriculum

• Enhancements of our policies for engagement review, Engagement Quality Control and Practice Review

• Including some large private companies within our PIE policies

• Discussion of future plans for audit reporting

• Updates from the Global AQB to discuss a UK specific response

• Identifying priorities and creating a formal Audit Quality Plan for 2020
Audit Quality Forum (AQF)
The AQB established an Audit Quality Forum in 2015, comprising staff from associate to manager grades, to give a voice to people at different stages of their careers and further improve audit quality. The forum meets three or four times a year. Matters discussed in the current year included the future of the audit product, methodology, the form and content of audit learning, performance management, and working with the wider engagement team such as specialists. A representative from the Forum sits on the AQB to feed back results for further action, as necessary.

Ruth Markland, Independent Non-Executive, attended one meeting of the AQF to give her perspective on audit quality and to hear from the members of the Forum on their current concerns.

Emerging Issues Group (EIG)
Our EIG was established during 2015 and includes partners from across the audit business, including industry specialists and those from our National Accounting & Auditing (NAA) technical team. Leveraging this wide range of experience, along with partnering with industry groups, the EIG’s objective is to identify significant emerging industry, political/economic, technology and regulatory/inspection related issues that could have a significant impact on audit quality in the future.

Some recent areas where the EIG has focused attention include Brexit and climate change. We have issued guidance to the Audit & Assurance Practice on how to incorporate emerging issues into their risk assessment.

The EIG drives the development of actions to address these matters, working with Industry Groups, NAA and the network of Audit Quality Leaders who are embedded in the audit groups. The EIG reports directly to the Audit & Assurance Executive.

ix) Developing the audit of the future
Over the past 12 months, there have been various reviews into the UK audit market and Deloitte has welcomed and engaged in these reviews and consultations, and continues to be committed to proposals that address concerns over quality, choice in the market and – critically – trust in the audit profession.

We have been challenging ourselves as to how we can enhance and evolve our audit product to reflect the changing needs of stakeholders, audited entities and society. This has included improving the clarity and detail of narrative reporting, to give stakeholders more relevant and meaningful information around key judgements and risks, and how these have been challenged as part of the audit process. Annual reports have undergone significant change in recent years. We are actively looking at how we should expand the scope of our work, to match this shift in reporting landscape, moving beyond that required under current auditing standards, where it is in the public interest to do so.

Audit & Assurance Transformation
Being a relevant profession of the future and a sustainable practice that evolves with the pace of change in technology and society is critical. Driving this goal is the Deloitte Audit & Assurance Transformation initiative, which is currently being developed and deployed across the Deloitte network, including Deloitte UK.

Audit & Assurance Transformation in an important shift across the network in the way Deloitte professionals work and includes:

- Deloitte Way: standardisation of audit processes supported by global technology suite
- Real-time audit quality monitoring
- Enhanced talent model which includes learning, rewards and recognition, centres of excellence, and delivery centres
- Agile deployment of tools and technologies to respond to changing environments

20
4. Consistency

i) Global network
We serve many global businesses and focus on providing consistent, quality audits across the whole of our international network. We work closely with our Deloitte Global colleagues and with those in other member firms in the Deloitte network to achieve this.

The Deloitte network has adopted several measures to drive quality improvements across the world. We are guided and assisted by a range of Deloitte Global bodies to which we contribute and from which a number of our audit quality initiatives stem, including committees that oversee audit quality and AQMM globally, and including the Global IFRS Leadership Team described in more detail below:

Global IFRS Leadership Team
The Deloitte network’s Global IFRS Leadership Team (GILT) is supported by nine International Financial Reporting Standards (IFRS) Centres of Excellence (including one in the UK) to provide our audit professionals with swift and consistent responses to IFRS technical queries. In particular:

• Global IFRS technical activities, including communications, are led from the UK.

• The global auditing and accounting teams work closely together to provide all our people with swift and consistent guidance around the world.

During 2019 GILT’s work supported by the UK team has included the successful launch of iGAAP on the Deloitte Accounting Research Tool (DART) (with hot links to IFRS Standards), the first truly global instance of DART, together with the UK’s GAAP 2019 on DART. The DART is an online platform that includes PCAOB standards, other accounting and auditing standards and Deloitte’s interpretations. The UK team continued to assist in issuing accounting FAQs and learning on IFRS 9, 15, 16, and 17 and improved our people’s knowledge and support on auditing accounting estimates and impairment.

ii) Audit imperatives
The Deloitte network’s aim is to drive professional excellence through the consistent global application of our audit imperatives, comprising five core principles and eight priorities (which do not necessarily change year-on-year), which have been adopted by every member firm. All audit professionals are expected to know what these are and to understand that they need to demonstrate each one on every audit. The following audit imperatives have been implemented in the UK and are supported by the initiatives discussed throughout this section. We monitor adherence to these imperatives through our internal inspections, to identify where additional actions may be required. When such actions are required, we also analyse the causal factors for this, to improve our processes for the future.

iii) Working across North and South Europe
Quality remains our focus within the Audit & Assurance Practice, and this is reflected by the leadership structure, with an oversight of consistent quality throughout NSE. Our head of Audit Quality for NSE leads the audit quality programme, working closely with Deloitte Global’s Audit Quality Board, the Global IFRS Leadership Team and all the country quality teams.

As part of NSE, we not only develop and share best practices, but also drive a consistent approach to audit quality, non-negotiable behaviours, and effectiveness across NSE.
External and internal audit quality monitoring

Audit Quality Monitoring & Measurement

A continued focus on audit quality is of key importance to the Deloitte brand. It is critical that a Deloitte audit is consistently executed and of high quality, wherever in the world it is performed.

The objectives of the Global Audit Quality Monitoring & Measurement (AQMM) programme are to:

- Transform the way audit quality is monitored and measured and audit deficiencies are resolved; and
- Enhance the internal system of quality control which all Deloitte network firms follow.

The AQMM program is focused on driving:

- Continuous, consistent, and robust monitoring of completed and in-flight engagements
- Fundamental understanding of deficiencies and timely execution of corrective actions by all member firms consistently
- Greater transparency and consistency in reporting key measures of audit quality
In this section we describe how audit quality is monitored at Deloitte via:

1. Internal inspection
2. External reviews
1. Internal inspection

At its core, the practice review programme determines whether we have complied, in all material respects, with the professional standards and the policies contained in the Deloitte Policies Manual (DPM) and Audit Approach Manual (AAM), as well as applicable professional standards and regulatory and legal requirements. Wider than this however, it provides assurance over the level of quality delivered by a Deloitte audit and drives the culture of continuous improvement. In recognition of the importance of practice review, the firm has made a significant investment during recent years to implement and deliver a transformation programme.

Within the practice review programme there are two elements that work together to meet the overall aims: individual Engagement Review (ER) that primarily assesses compliance with the AAM, and the System of Quality Control (SQC) review that primarily focuses on the firm’s internal processes to comply with the DPM. Additional rigour and independence is brought through the oversight of an independent partner from another member firm within the Deloitte network together with independent engagement reviews from a central global team. Our overall aim is that our internal inspection will have at least the same scrutiny and rigour as that applied by our external regulators.

The ER has continued to improve during the year by additional performance of in-flight reviews which were implemented in the prior year: reviews of live engagements which focus upon significant risk areas which are subject to high numbers of findings from internal and external inspections, with the aim of improving audit quality before the audit opinion is signed.

In addition to the points noted below, we have continued to expand the breadth and depth of the SQC review by both widening existing, and adding additional, procedures to increase the robustness and level of challenge in our work. The additional procedures incorporate and expand on European Audit Inspection Group (EAIG’s) Common Audit Inspection Methodology programme for reviewing a firm’s SQC and requires the firm to provide evidence of operational effectiveness of the control alongside appropriate design and implementation. We no longer take a compliance approach to the review, but a best practice approach to encourage stringent and robust reviews to implement appropriate controls.

Our transformed practice review process includes the following key parts that ensure it is delivered with the right level of scrutiny and rigour:
Statement on the monitoring of local audit functions

All local audits are included within the scope of our audit quality control system, including practice review. No local audits conducted under the Local Audit and Accountability Act 2014 have been subject to internal practice reviews during the year. The nature of our portfolio of local audits for the year to 31 May 2019 meant that a high proportion of engagements for which we issued audit reports in the year ended 31 May 2018 would be subject to external inspection by the AQR (for major local audits) and QAD (for other local audits). Consequently we actively de-selected these from our internal practice review for this cycle. For the practice review year to 31 May 2020 we will include local audit selections as the portfolio of engagements has changed.

Statement on the effectiveness of the functioning of the audit quality control system in regards to local audits

In accordance with the schedule of The Local Auditors (Transparency) Instrument, and based on the practice review carried out in 2018 and the status of the 2019 practice review that will be finalised in September 2019, the Audit & Assurance Executive is satisfied that our internal quality controls and systems are, in general, robust and operating effectively in regard to the local audits and allow us to readily identify any areas of potential improvement or refinement. We continually seek to improve all aspects of our business, including in relation to local audits, and we use the findings of the practice review, other internal reviews and external regulatory reviews to enhance our SQC.

The firm also conducts an annual review of the ongoing effectiveness of the firm's systems of internal control, including financial, operational and compliance controls and risk management systems, as well as the promotion of an appropriate culture underpinned by sound values and behaviour within the firm. The review in respect of FY19 was in progress at the time of publication of this report. A statement regarding the effectiveness of the firm's system of internal control will be included in the main transparency report to be published during September 2019.

i) Selection process

A detailed selection process is undertaken each year for both the engagements to be reviewed and the scope of work for the SQC.

ER: Engagements are selected across our audit business portfolio using a risk based approach, focusing on high risk and/or high profile engagements, and ensure that, as a minimum, each of our partner and director Responsible Individuals are subject to a review every three years. All sectors are covered by this selection process, including Public Sector engagements. Selected files are then subject to independent inspection by professionals from the central inspection team, along with reviewers comprising partners and senior auditors from other UK offices, groups and overseas member firms (together the 'Reviewers').

SQC: A detailed risk assessment is performed across all areas that support audit quality to set the areas and the level of testing to be performed. During this process meetings are held with stakeholders to inform the process and a number of critical factors are assessed including Global, UK, and regulatory focus areas to reach a conclusion on the level of risk associated with the process and the scope of work to be performed.

ii) Experienced reviewers

A critical success factor in achieving our desired level of rigour and scrutiny is the competency of the Reviewers. Across both the ER and SQC, we undertake a comprehensive selection process, ensuring the Reviewers as a team have the relevant industry and technical experience, quality record, seniority, and sufficient time to be able to bring robust independent challenge. Once selected, all Reviewers are given thorough training by the leaders in our central team.

iii) Consistency of findings

At the end of each review, the findings are moderated centrally by a moderation panel. This moderation panel applies a regulatory lens from our library of inspection findings to ensure that findings are classified consistently. The moderation panel determines the rating for each review. For ER we classify engagements as either Compliant, Improvement Required or Non-Compliant and with processes subject to independent inspection by professionals from the central inspection team, along with reviewers comprising partners and senior auditors from other UK offices, groups and overseas member firms. For SQC, we undertakes a comprehensive selection process, ensuring the Reviewers as a team have the relevant industry and technical experience, quality record, seniority, and sufficient time to be able to bring robust independent challenge. Once selected, all Reviewers are given thorough training by the leaders in our central team.

iv) Action and ongoing education

The results of the practice review are communicated to the UK Audit & Assurance Executive, the Managing Partner Quality & Risk, the UK Oversight Board and the INEs via their attendance at the UK Oversight Board. In addition, a member of the Deloitte Global Audit Executive attends the UK closing meeting and the results are reported to the Deloitte Global Audit Executive and to the Global Risk Advisory Executive Committee. Casual Factor Analysis (CFA) is performed on the findings as set out in the CFA section below.
2. External reviews

In addition to our own internal reviews of audit quality, we are subject to external reviews by the FRC’s AQR team and the ICAEW’s QAD (as well as the PCAOB).

**External inspections of public sector audits**

The AQR’s scope for 2018/19 included major local health audits and firm wide policies and procedures associated with local audits, and the QAD’s scope includes other local audits.

In relation to firm wide policies and procedures associated with local audits the AQR considered we should enhance the level of information included in our reporting required by The Local Auditors (Transparency) Instrument 2015. We have addressed these findings by publishing a separate report for 2019 and include in the appendix on page 40 a listing of the requirements of the schedule for disclosures and refer to where each can be found within this report.

Both the AQR (major local health audits) and QAD (other local audits) reviewed certain local audits at Deloitte during the year ended 31 May 2019. Their findings have not yet been publically reported, and therefore are not included in the summary of inspection findings below. The results of those external inspections, for financial statements and value for money conclusions, required no more than limited improvements. We were very pleased with the results.

**External inspections**

We have included below, consistent with our main Transparency Report, the findings of the AQR as reported in their 2018/19 Audit Quality Inspection Report, the FRC thematic reviews and a summary of the QAD inspection results for 2018. Whilst these external inspections were not directly of local audit work we consider the findings of all external reviews as findings may also be relevant to local audit work.

We address the findings of external reviews in a number of ways, including changes to our methodology, audit software and training. We apply these responses across our audit business - while differences between sectors mean some responses have less impact on public sector audits, adopting a consistent approach supports the quality of all our audits.
The AQR undertakes independent inspections of the overall quality of the auditing function in the UK in relation to listed and other major public interest entities. The AQR published a report on the findings of its 2018/19 inspection of the firm on 10 July 2019. The full report is available on the FRC’s website at the following link.

The firm’s policies and processes supporting audit quality were reviewed, as were 25 individual audits. The AQR’s review identified that we had taken the actions we committed to following their 2017/18 review, and that they had limited or no repeat findings in most of those areas. In addition, they highlighted that we had made the following enhancements to our policies and procedures:

- As discussed earlier (see Global Consistency sub-section), through the firm’s global audit quality programmes, there has been an increased focus on consistency of audit work across the Audit & Assurance Practice. For certain account balances, standardised approaches have been adopted, further use has been made of centres of excellence and delivery centres and new technologies embedded into the audit process to support and enable risk assessments, analytical procedures and project management activities.

- Further methodology updates and additional guidance and training for the Audit & Assurance Practice covering group audits, accounting estimates, financial services (including the adoption of IFRS 9), provisions and contingencies and the evidencing of quality control procedures (including EQCR) on individual audits.

- Increased support for audit teams throughout the audit cycle. This includes global AQMM approach measures, mirrored in the UK, such as in-flight reviews of audit files as audits progress, coaching programmes for teams, the monitoring of audit milestones and greater use of diagnostics to monitor progress.

- Continued focus on the approach to the testing of internal controls. The firm provided additional training and support to audit teams adopting a controls-based audit approach, increased focus on reporting to Audit Committees on internal controls and on the wording of auditor’s reports.

Quality underpins everything we do. It is our absolute priority and is at the heart of the transformation activities we have undertaken over recent years and in which we continue to significantly invest. We are steadfastly committed to delivering high quality audits that support our wide ranging stakeholders and our public interest role. The UK audit regulatory market is facing a time of significant change and challenge. We are active participants in this debate and support many of the proposals being considered.

We greatly value the FRC reviews of our audit engagements and firm wide quality control systems, a key aspect of evaluating our audit quality. We have further transformed our internal review processes including a new focus for reviewing in progress audits, developing our Audit Quality Indicators (AQI) which are monitored and reported to the Audit & Assurance Executive and UK Oversight Board, and on enhanced remediation procedures.

Whilst we are pleased that overall our quality record, as measured by external inspections, has improved from 76% to 84%, we remain committed to continuous improvement and achieving a high standard across all engagements. We are, however, extremely disappointed one engagement received a rating of significant improvements required during the period. This is viewed very seriously within Deloitte and we have worked with the AQR to agree a set of significant firm wide actions on the critical area of findings relating to the assessment of potential prior period adjustments and conduct matters.
We are also pleased to see the impact of our previous actions on impairment, group audits and contingent liability disclosures reflected in the audits under review and there being limited or no findings in those areas. These continue to be a focus in our training and internal coaching and of our internal review programmes to maintain or increase the level of challenge our audit provides in those areas.

We invest continually in our firm wide processes and controls, which we seek to develop globally, to underpin consistency in delivering high quality audits whilst ensuring engagement teams exercise professional scepticism through robust challenge. This investment includes continued recruitment and enhancement of the skill-sets of our audit staff, including those involved in quality control. This also supports the transformation programmes and standardisation of audit procedures. We are pleased there were no significant findings from the reviews undertaken in these areas in 2018/19, which included our internal quality monitoring and engagement quality control review procedures. In particular we have also taken actions around our systems in response to prior year matters to enable more timely monitoring activities.

In the event an internal or external review results in an improvements required or significant improvements required we have a formal policy to assess what retrospective remediation is appropriate taking account of the public interest. Our causal factor analysis shows that whilst our recent actions have had a measurable impact, because we see reduced findings in previous challenge areas, more can always be done.

We identified the following three areas of root cause underpinning a number of the AQR findings:

- Assumed knowledge, whereby engagement teams do not sufficiently evidence work, or omit information from the audit file due to familiarity or inherent knowledge of the engagement has been identified as an underlying cause in many of the findings. We addressed this during our summer technical excellence training, called TechEx 2019, as we strive to continually improve.

- The sufficiency of evidencing professional scepticism, in particular ensuring engagement teams challenge management’s judgements and estimates rather than adopting a confirmatory approach. This is often influenced by assumed knowledge. This was a focus of our TechEx 2019 particularly in relation to auditing management estimates. We have recently published a new Fraud Response Guide aimed at sharing practice tips for all audit practitioners for how to respond when a fraud is suspected or discovered including consultations, assessing the impact on the audit plan and involving specialists.

- Client readiness for audit. We recognise our role in challenging management to ensure they have given sufficient time and resource to complete their own assessments of key areas of judgement and to evidence those within their own accounting papers. This supports our focus on project management enabling us to have appropriate time to plan and then challenge management on those judgements. We have an imperative this year to focus on audit milestones to ensure key areas of planning work are completed in a timely manner with the right level of senior input and challenge. Our audit transformation also supports strong project management, for example, with increased standardisation of audit procedures and with additional tools to manage the process from start to finish, such as automated information request lists and trackers and a new resource management system which will enable more sophisticated analysis of our people’s workloads supporting our strategic objectives around wellness.

Employee wellbeing is at the heart of our talent strategy. Respect and inclusion have many strands, and we are focused on offering an environment supporting the mental and physical wellbeing of our people. We firmly believe that audit quality is enhanced by positive mental health and wellbeing. We consider a greater awareness of mental health and wellness of our people is crucial and we have many programmes to support this across all partners and practitioners in our firm. We want to ensure everyone is working in a healthy way despite the challenges and time pressures. We have continued to engage a behavioural psychologist to support our causal factor analysis work to better understand the less tangible factors that can impact audit quality.

The FRC’s key individual review findings related principally to the following:

Exercise greater professional scepticism in the audit of potential prior year adjustments and related disclosures in the annual report and accounts.

We recognise that we need to better evidence consultations. We believe project management and client readiness were both root causes of these issues. In addition, whether or not a company makes a prior year adjustment (PPA) is an area requiring significant judgement and assessment of quantitative and qualitative factors. The accounting standards are not prescriptive, and are deliberately drafted so that prior year adjustments can only be made if certain criteria are met. We have considered this in developing our actions.
We have created a new consultation document specifically for the evaluation of potential PPAs to focus on capturing the following in more detail:

- Timing of the consultation(s), which may include multiple discussions over an extended period of time
- More detail of who is being consulted and their qualification/appropriate expertise and experience
- Considering and challenging the completeness of the adjustments identified
- Assessment of the appropriate reporting, to management, the Audit Committee and within our enhanced audit reports, and the level of disclosure provided by management

TechEx 2019 featured a session on regulatory findings, where we covered the new practice aid and the revised consultation templates and key matters for engagement teams to consider.

We also communicated this finding within our January 2019 briefing of EQCR reviewers and April EPU for all audit practitioners. This will encourage increased challenge from EQCR reviewers and a greater awareness of engagement team members of the importance of evidencing more fully work in this area.

**Strengthen the extent of challenge of key estimates and assumptions in key areas of judgement, including asset valuations and impairment testing**

In January 2019 we issued a practice aid on accounting estimates, developed to focus on evaluating management’s own processes and controls and how to challenge and test management’s accounting estimates, further informed by the findings identified here. An additional guide was published on the audit of trade debtors’ credit loss estimates highlighting common pitfalls and best practices.

A number of the issues identified by the AQR were partly caused by the assumed knowledge and inherent conclusions made during the audit as a result of that knowledge. As previously noted earlier, we have taken a number of actions to highlight this pitfall and further develop our evidence of professional scepticism in audit documentation. Management estimates has a specific section at TechEx 2019.

We used our internal newsletter to focus on real estate and valuations in January 2019. We also issued an update on managements papers (linked to the causal factors on both evidencing professional scepticism and project management and client readiness) and on goodwill impairment.

We issued additional guidance to engagement teams on the use of reasonable ranges in the audit of management estimates, highlighting that auditors’ should understand management’s own approach, and then whether they are assessing specific assumptions or developing their own point estimate or range in order to audit management’s estimate. It will also reiterate the importance of assessment of specialist reporting and any ranges identified within that.

We have pro-actively made enhancements to our approach to pension asset and liability testing during 2018 and agreed those changes in advance with the AQR. These changes were highlighted as good practice by the AQR last year and included changes to our methodology, issuing further guidance on approach and on working with specialists and we have developed a central pensions analytics tool to further support audit procedure consistency. We will embed further methodology changes to address new concerns.

Using specialists remains critical in providing sufficient challenge to management in our auditing of key estimates and assumptions in judgement areas. We regularly brief our specialists within the firm on regulatory inspection findings and internal practice reviews, and will also update on findings from this review cycle.

We held a detailed EQCR review team training in January 2019 to continue to keep areas of regulatory focus at the forefront of challenge of EQCRs. This captured this report and other external and internal practice review findings.

Impairment has been a critical area for us over the last two cycles. We established an impairment centre of excellence in 2016 and require engagement teams to consult with those specialists, with a continued focus on training in this area, and, as noted by the AQR we have seen significant improvement. It is disappointing a limited number of findings still arise and we believe addressing this through additional challenge from consultation with our specialists is appropriate. We have also briefed EQCR partners and PSR reviewers on key regulatory findings which has included these matters on impairment. We have highlighted within our April EPU (essential professional update - our online training video) the same matters and reminded engagement teams of the need to consult.
Improve the consistency of the firm’s audit of revenue

Findings related to third parties maintaining revenue systems were both in connection with areas assessed by the auditor as having a low risk of material misstatement. AQR did not disagree with our risk assessment, nevertheless, it felt, and we agree, we could have better evidenced our use of the service auditor reports for these systems. A service auditor report is provided by an auditor, independent of the relevant entity or process, and which is designed to give an opinion on the status of controls over that process. We recognise the importance of service auditor reports in a variety of areas and plan the following actions:

• We will hold a focused EPU session on the use of service auditor reports, common pitfalls and key areas to consider

• TechEx2019 will include specific examples in highlighting these areas

We have not identified any further thematic causes, and noting a number of these findings related to low risk areas, we have addressed the findings in the following ways:

• In each individual engagement referenced we will take action in the following year’s audit to specifically address the findings and better evidence the audit procedures performed.

• We have communicated via an EQCR training session the regulatory findings and the importance of challenging engagement teams with similar circumstances. We have factored all these findings into our practice review training, and recorded an online video tool for the Audit & Assurance Practice focusing on all recent regulatory findings. TechEx 2019 will feature a session on these findings.

• We have communicated the findings to each industry group within the audit business units, allowing them to consider further focused sessions on both the findings and best practice.

• The next wave of our Deloitte Way Workflows (which are standardised audit work packages to drive consistency in quality audit work), includes revenue. We will review those workflows to consider the relevance of including specific reminders within the template documents relating to areas of regulatory and internal review findings.

Achieve greater consistency in the audit of provisions and liabilities

We are pleased to not have any findings relating to contingent liability disclosures, which had featured previously, and our actions in this area were effective.

The assessment of provisions and liabilities is often an inherent area of judgement. We believe there are two broad causal factors which underlie these findings around both assumed knowledge and evidencing professional scepticism. In addressing the completeness findings, we are focused on ensuring teams actively seek contradictory and independence evidence to challenge management. These causal factors are an underlying theme throughout our TechEx2019 to strive for behavioural change in our audit teams. This is also supported by the overall wellness initiatives within the firm supporting our people, enabling them to perform to their best, including a focus on project management and client readiness.

In relation to matters of non-compliances with laws and regulation (‘NOCLAR’) we dedicated a large part of our January 2019 EPU to covering this important area which can often result in matters requiring assessment as provisions or liabilities.

In addition, we have taken action in the following year’s audit to address each of the findings identified where relevant.

ii) FRC Audit Quality Thematic Reviews

The FRC’s AQR team uses thematic reviews to supplement its annual programme of audit inspections of individual firms. In a thematic review, firms’ policies and procedures are reviewed in respect of a specific aspect of auditing to test their application in practice. Thematic reviews analyse further aspects of auditing which are not considered in detail during the FRC’s routine audit inspections. Thematic reviews seek to identify both good practice and areas of common weakness among audit firms.

During the year, the FRC published a thematic report on ‘other information in the annual report’ focusing on the work performed by auditors to meet their reporting responsibilities in this area. We find these thematic reviews valuable as the benchmarking style provides insight to audit firms and other interested parties, and it provides a focus on best practice which we use to inform our actions in related areas. The FRC is undertaking thematic reviews on audit quality indicators and a follow up review on the use of technology in audits which will be delivered during 2019/20.
### iii) Inspection by the QAD of the ICAEW

<table>
<thead>
<tr>
<th>Results</th>
<th>FY19</th>
<th>FY18</th>
<th>FY17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Satisfactory or generally acceptable</td>
<td>80%</td>
<td>100%</td>
<td>69%</td>
</tr>
<tr>
<td>Improvements required</td>
<td>20%</td>
<td>-</td>
<td>23%</td>
</tr>
<tr>
<td>Significant improvements required</td>
<td>-</td>
<td>-</td>
<td>8%</td>
</tr>
</tbody>
</table>

The QAD undertakes inspections of UK statutory audits which are outside the scope of the AQR’s inspections as well as inspecting local audits that are not major local audits. The firm receives a private annual report from the QAD documenting its findings. The QAD report had not been formally approved by the ICAEW Audit Registration Committee at the date of this transparency report. The comments below are provisional and subject to any further changes recommended by that committee.

The overall conclusion in the 2019 report, which covered reviews of statutory audit reports signed in 2018, was that “overall, the audit work we reviewed was of a good standard. Four files were satisfactory, four were generally acceptable and two files required improvement. No files were in need of significant improvement. This continues a positive trend of results since 2016. Our last visit in 2017 produced a particularly strong set of results, with all files being satisfactory or generally acceptable”.

There were some areas for improvement identified across the files which related mainly to documentation issues. There were two key findings in the reviews. One file needed improvement as the substantive analytical review was flawed. The second file needed improvement because of weaknesses in a number of key areas including group audit considerations and completion procedures. There was also a finding across four reviews in relation to our methodology of substantive analytical review. We have taken action to address this through the implementation of an additional consultation requirement for engagement teams in circumstances such as those highlighted in the QAD reviews.
Independence

As a leading professional services firm, we have a responsibility to serve our clients and wider public interest with integrity, objectivity and free from conflicts of interest, while proactively maintaining and demonstrating our independence.

Our firm-wide independence policies are based on the requirements of the International Ethics Standards Board for Accounting (IESBA), US Securities and Exchange Commission (SEC) and the UK Financial Reporting Council (FRC). The specific independence requirements applicable to local audits include the requirements of the National Audit Office’s Code of Audit Practice and Auditor Guidance Note 1 ‘General Guidance Supporting local audit’.

Independence is of the utmost importance to us - our dedicated Independence Team is committed to advising engagement teams, reinforcing our policies and maintaining effective systems and processes, whilst continuously improving them so that we remain independent in fact and appearance. Our local audit engagement leads and staff, together with our Independence Team, are experienced in considering local audit specific requirements where they add to those of the FRC’s Ethical Standard.

Systems and processes

We continue to invest in systems and processes to safeguard the independence and objectivity of our firm, our professionals and our engagement teams, and to avoid conflicts of interest on engagements. Key changes to our systems & processes in FY19 were:

- Global Investment Tracking System: Migrated to a new more user friendly global system which will also help make it easier for our people to record and monitor their financial interests.

- Enquiry Platform: Developed and launched a consultation platform to enable the business to consult with the Independence Team more effectively and to drive consistent documentation and trend analysis.

- Strategic and targeted approach to communications and awareness: Implemented a more strategic and targeted approach to increase the impact of communications and awareness campaigns, particularly around personal independence.

- Interim confirmation process: Introduced a bi-annual confirmation process for partners to assist them in complying with personal independence requirements.
Our engagement take-on, continuance, compliance, audit appointment and client database tools are all internally developed and comprise solutions to address the complexity of global regulatory requirements. The tools are designed to be intuitive, while facilitating timely compliance, reporting and monitoring, and to ensure that we (including our partners, professionals and any of their close connections) do not engage in certain transactions or relationships with entities from which we are required to maintain independence (‘restricted entities’).

The main systems and processes of internal control in this area are:

- **Conflict Checking System**: Identifies and communicates potential independence conflicts and pre-approval requirements in respect of proposed engagements, business and financial relationships.

- **Global Independence Monitoring System**: Assists Deloitte member firms and their professionals monitor their personal financial interests. UK Partners and staff were migrated to GIMS during 2019 replacing Personal Connections in the UK.

- **Restricted Entities Database**: Records comprehensive details on every restricted entity, allowing partners and staff to check independence requirements for any type of investment or product before they enter into any financial relationship.

- **Business Relationships Monitoring System**: Records all business relationships and alliances of the firm.

- **Inspection and Testing**: Assessment of the financial holdings of a sample of partners and client facing staff of manager grade and above is carried out each year by a dedicated team.

- **Annual Confirmations**: Obtains confirmation from partners, professionals and support staff, upon joining the firm and annually thereafter, that they are aware of our policies and that they are not engaged in any restricted transactions or business relationships. An interim independence confirmation has been introduced in 2019 for partners to assist partners in complying with independence requirements and increase the frequency of confirmations.

If any queries arise in respect of these areas, dedicated support is provided through our Quality & Risk Management teams. Additionally, on independence related matters, they may consult with Deloitte Global’s independence group if they determine that the circumstances require global input or advice. Where it is determined that it is not possible to sufficiently mitigate the independence risk identified, the engagement or relationship is declined.

The Independence Partner presented to the UKOB during the year to 31 May 2019, covering current key matters and trends related to independence. This also included a summary of recent interactions with the FRC, ICAEW and other regulators as well as communications and training provided to partners and professional staff.
Raising awareness
In addition to our systems and processes of internal control, we continue to raise awareness and improve education of independence requirements. The key components of our 2018/19 awareness & education program are as follows:

**Partner Awareness Workshops**
A mandatory personal independence awareness workshop has been launched to partners for completion by end 2019. These sessions raise awareness as well as gain personal commitment on actions to improve compliance in their business area.

**Educational Videos**
Additional educational videos focusing on complex areas and adherence to independence policies were developed and launched.

**Targeted Communication Campaigns**
A targeted communication plan is in place and being implemented with regular communications on key independence topics through various channels.

**One to One Meetings**
We continue to have one to one meetings with all new partners joining the firm or being promoted internally to advise them of their personal independence.

**Tailored Presentations & Webinars**
Targeted communication, presentations and webinars on independence requirements and the impact on individuals and client relationships are provided to partners and professional staff.

---

**Deloitte Global Independence**
Sets independence policies and procedures based upon the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants and the independence standards of the US Securities and Exchange Commission and the Public Company Accounting Oversight Board. Performs full reviews of independence quality controls on a three-year cycle; annual focused reviews for the off-cycle years; and in-depth follow-up reviews as needed.

Performs on-going monitoring activities of firms—enabling continuous enhancements to global policies, quality controls, tools, and practice support activities.

Delivers global systems to provide professionals with entity information to support compliance with personal and professional independence requirements, including financial interests and scope of service approvals.

Supports independence awareness across the Deloitte network through active engagement with independence and business leadership groups, periodic communications and alerts, and development of guidance, learning and instructions.
Dealing with conflicts of interest

Deloitte provides a diverse range of services to a broad client base. As such, from time to time, situations will arise where the firm has relationships with two or more parties involved in a particular transaction or matter, potentially giving rise to conflicts of interest or threats to confidentiality. Professional standards and regulations require us to have effective policies and processes in place to identify and address these situations. It is also an imperative for us in order to retain the trust of our clients and wider stakeholders, including the general public.

Recent corporate failures and other events have led to intense public scrutiny around how accountancy firms manage potential conflicts of interest. We acknowledge that this requires us to consider not only the letter, but also the spirit, of professional standards and regulation and also to give due regard not only to whether a proposed engagement could be accepted, but also to whether it should be.

Our policy is that all proposed new engagements are subject to a confidential conflict check using the firm’s bespoke conflict checking system prior to acceptance. This check is reviewed by our central conflicts team and references the firm’s databases of existing and past engagements, opportunities, business relationships and other connections with the involved entities to identify potential conflicts. Following the completion of the conflict check, the proposed engagement will either be cleared to proceed from a conflicts perspective or declined. Where the engagement is cleared to proceed this may be conditional on specified safeguards and measures being implemented, designed to address any threats prior to, during and following the completion of the engagement. Such safeguards will vary depending on the specific facts and circumstances, but may include:

• notifying the affected parties of the circumstances giving rise to the potential conflict of interests and obtaining their informed consent to act in the circumstances;

• limiting the scope of services provided to one or more of the affected parties;

• the use of separate engagement teams to serve the affected parties;

• the physical separation of teams serving the affected parties;

• procedures to prevent unauthorised access to confidential information (for example through confidential and secure data filing);

• the use of confidentiality agreements signed by employees and partners of the firm; and/or

• regular review of the application of safeguards by a senior individual not involved with relevant client engagements.
The above safeguards are subject to monitoring and review by the central conflicts team or other Quality & Risk Management teams.

Where a potential conflict of interest is identified and the threat posed cannot be eliminated or reduced to an acceptable level through the implementation of sufficient safeguards, the proposed engagement is not accepted.

In addition to the above procedures, before commencing work on an engagement, each prospective engagement team member considers whether they have any personal relationships with, or interests in, any of the involved entities that could give rise to potential conflicts of interest. Any potential issues are discussed with the engagement partner or the conflicts team, as appropriate, to determine whether the individual should participate in the engagement.

The above procedures must be revisited by the engagement team in the event of a change in the facts and circumstances of an ongoing engagement, such as a significant change in the scope of our work or the parties involved.

Based on the circumstances surrounding the proposed engagement and on their knowledge and expertise, the central conflicts team will assess whether escalation is required to determine whether an engagement should be accepted. The points of escalation available for this purpose include:

- The relevant business area's Quality & Risk Management team and/or Head of Quality & Risk Management
- The firm's Managing Partner Quality & Risk
- The firm's Ethics Partner
- The Tax Review Panel
- The Public Interest Review Group
- The firm's regulators, in exceptional circumstances where their guidance is needed

Conflict checks are included within the scope of our firm-wide take-on monitoring process including existence, timeliness and accuracy of information provided. The results of this take-on monitoring are taken into account in partners’ annual performance evaluation.

In circumstances where potential conflicts involve entities audited by the firm and have the potential to impact audit independence, the firm's engagement acceptance and continuance procedures include appropriate involvement of the audit partner. Such involvement would be initiated by the central conflicts team. If the audit partner concludes that the potential conflict would not affect audit independence, the engagement may be accepted subject to the implementation of appropriate safeguards. The audit partner would determine the nature and timing of any communication with the audited entity, including the audit committee.
Appendix 1: List of local audits

Major local audits on which we made an audit report on the annual financial statements during the year ended 31 May 2019

Disclosures in accordance with the schedule of The Local Auditors (Transparency) Instrument 2015 (as defined in The Local Audit (Professional Qualifications and Major Local Audit) Regulations 2014).

Regulatory context

The organisation below is the only relevant authority:

(a) Which constitutes a ‘major local audit’ for the purposes of Regulation 12 of The Local Audit (Professional Qualifications and Major Local Audit) Regulations 2014 (SI 2014/1627); and

(b) For which Deloitte LLP signed an audit report on its annual financial statements during year ended 31 May 2019.

Name of audited entity:
Imperial College Healthcare NHS Trust

Other local audits for which we were appointed auditor for the year ended 31 March 2019, but for which we had not made an audit report on the annual financial statements during the year ended 31 May 2019

Major local audits – Name of audited entity:
Blackpool Council
City of Wakefield Metropolitan District Council
Dorset County Council
London Borough of Ealing
London Borough of Tower Hamlets
North Yorkshire County Council
Royal Borough of Windsor and Maidenhead
South Yorkshire Pensions Authority
Wiltshire Council

Other local audits – Name of audited entity:
Avon Fire Authority
Berkshire Pension Fund
Dorset Pension Fund
Dorset and Wiltshire Fire and Rescue Authority
Ealing Pension Fund
Eastbourne Borough Council
Epping Forest District Council
Fylde Borough Council
Gloucester City Council
Lancaster City Council
Lewes District Council
Maldon District Council
North Dorset District Council
North Yorkshire Pension Fund
Purbeck District Council
Reigate and Banstead Borough Council
South Yorkshire Fire and Civil Defence Authority
Southend on Sea Borough Council
Stroud District Council
Tandridge District Council
Tower Hamlets Pension Fund
West Dorset District Council
West Yorkshire Fire and Rescue Authority
Western Riverside Waste Authority
Weymouth and Portland Borough Council
Wiltshire Pension Fund
Wyre Borough Council

Name of audited entity:
Coventry and Warwickshire Partnership NHS Trust
Avon and Wiltshire Mental Health Partnership NHS Trust

Other local audits on which we made an audit report on the annual financial statements during the year ended 31 May 2019

Name of audited entity:
Appendix 2: Financial information

Disclosure in accordance with the schedule of The Local Auditors (Transparency) Instrument 2015

<table>
<thead>
<tr>
<th>Revenue</th>
<th>£'000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local audits (audit services)</td>
<td>200</td>
</tr>
<tr>
<td>Local audits (non-audit services*)</td>
<td>41</td>
</tr>
<tr>
<td>Other audit and non-audit services to all other entities**</td>
<td>3,430,508</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>3,430,749</td>
</tr>
</tbody>
</table>

* All non-audit services provided to local audits are assurance services in respect of Quality Accounts that are required to be provided by the auditor

** Relates to the UK, incl. the Channel Islands and Isle of Man, and Gibraltar
# Appendix 3: The Local Auditors (Transparency) Instrument 2015 – disclosure requirements

This appendix sets out the disclosure requirements from the schedule of the Instrument and where the relevant disclosures can be found within this report.

<table>
<thead>
<tr>
<th>REQUIREMENT from Schedule Regulation 3(2)</th>
<th>Page reference where disclosure is made</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. A description of the legal structure, governance and ownership of the transparency reporting local auditor.</td>
<td>4 and 5</td>
</tr>
<tr>
<td>2. Where the transparency reporting local auditor belongs to a network, a description of the network and the legal, governance and structural arrangements of the network.</td>
<td>8</td>
</tr>
<tr>
<td>3. A description of the internal quality control system of the transparency reporting local auditor and a statement by the administrative or management body on the effectiveness of its functioning in relation to local audit work.</td>
<td>24 and 25</td>
</tr>
<tr>
<td>4. A description of the transparency reporting local auditor’s independence procedures and practices including a confirmation that an internal review of independence practices has been conducted.</td>
<td>32 to 36</td>
</tr>
<tr>
<td>5. Confirmation that all engagement leads are competent to undertake local audit work and staff working on such assignments are suitably trained;</td>
<td>15</td>
</tr>
<tr>
<td>6. A statement of when the last monitoring of the performance by the transparency reporting local auditor of local audit functions, within the meaning of paragraph 23 of Schedule 10 to the Companies Act 2006, as applied in relation to local audits by Section 17 and paragraphs 1, 2 and 28(7) of Schedule 5 to the Act, took place.</td>
<td>25</td>
</tr>
<tr>
<td>7. A list of major local audits in respect of which an audit report has been made by the transparency reporting local auditor in the financial year of the auditor; and any such list may be made available elsewhere on the website specified in regulation 4 provided that a clear link is established between the transparency report and such a list.</td>
<td>38</td>
</tr>
<tr>
<td>8. A statement on the policies and practices of the transparency reporting local auditor designed to ensure that persons eligible for appointment as a local auditor continue to maintain their theoretical knowledge, professional skills and values at a sufficiently high level.</td>
<td>15</td>
</tr>
<tr>
<td>9. Turnover for the financial year of the transparency reporting local auditor to which the report relates, including the showing of the importance of the transparency reporting local auditor’s local audit work.</td>
<td>39</td>
</tr>
<tr>
<td>10. Information about the basis for the remuneration of partners.</td>
<td>13 to 14</td>
</tr>
</tbody>
</table>