

# Changes to arrangements for appointment of an External Auditor

Cabinet

Date: 7<sup>th</sup> December 2016

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Author:	Cabinet Member for Finance and Corporate Services and Head of Internal Audit
Wards:	All
Locality Affected:	All
Parishes Affected:	All

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## 1. Purpose and Reasons

- 1.1 This report summarises the changes to the arrangements for appointing External Auditors following the closure of the Audit Commission and the end of the transitional arrangements at the conclusion of the 2017/18 audits.
- 1.2 The report also sets out the various options the Council has with regard to appointing and putting in place new arrangements in time to make a first appointment by 31<sup>st</sup> December 2017.

## 2. Recommendations

Cabinet is recommended to:

- 2.1 Recommend to Council that the appointment of an External Auditor be made through the national sector led body, Public Sector Audit Appointments Ltd.

## 3. Detail

Background to the issue

- 3.1 The Local Audit and Accountability Act 2014 ("the 2014 Act") brought to a close the Audit Commission and established transitional arrangements for the appointment of external auditors and the setting of audit fees for all local government and NHS bodies in England.
- 3.2 On 5<sup>th</sup> October 2015 the Secretary of State Communities and Local Government determined that the transitional arrangements for local government bodies would be extended by one year to also include the audit of the accounts for 2017/18.
- 3.3 The Council's current external auditor is Grant Thornton, this appointment having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the contract is currently managed by Public Sector Audit Appointments Limited, the transitional body set up by the Local Government Association (LGA) with delegated authority from the Secretary of State Communities and Local Government.

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- 3.4 Over recent years the Council has benefited from a reduction in fees. This has been the result of a combination of factors including new contracts negotiated nationally with the firms of accountants and savings from closure of the Audit Commission.
  - 3.5 When the current transitional arrangements come to an end on 31<sup>st</sup> March 2018 the Council will be able to move to a local appointment of the auditor.
  - 3.6 There are a number of routes by which this can be achieved, each with varying risks and opportunities. Current fees are based on discounted rates offered by the firms in return for substantial market share. When the contracts were last negotiated nationally by the Audit Commission they covered NHS and local government bodies and offered maximum economies of scale.
  - 3.7 The scope of the audit will still be specified nationally, the National Audit Office is responsible for writing the Code of Audit Practice which all firms appointed to carry out the Council's audit must follow. Not all accounting firms will be eligible to compete for the work, they will need to demonstrate that they have the required skills and experience and be registered with a Registered Supervising Body approved by the Financial Reporting Council.
  - 3.8 The number of firms is not known but it is reasonable to expect that the list of eligible firms may include the top ten or twelve firms in the country, including our current auditor. It is unlikely that small local independent firms will meet the eligibility criteria.
  - 3.9 Audit Committee has received regular updates regarding the new arrangements for the appointment of an External Auditor. The Government has recently confirmed that Public Sector Audit Appointments Ltd has been authorised to make future appointments on behalf of principal local authorities.
  - 3.10 The Council will need to opt in formally to the scheme if this is the option selected (see below).

## Options for local appointment of External Auditors

### Option 1 - Opt-in to a sector led body (Public Sector Audit Appointments Ltd)

- 3.11 In response to the consultation on the new arrangements the Local Government Association successfully lobbied for councils to be able to 'opt-in' to a sector led body appointed by the Secretary of State under the 2014 Act.
- 3.12 A sector led body will have the ability to negotiate contracts with the firms nationally, maximising the opportunities for the most economic and efficient approach to procurement of external audit on behalf of the whole sector.

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- 3.13 The Government has recently confirmed that Public Sector Audit Appointments Ltd has been authorised to make future appointments on behalf of principal local authorities that have opted in to the scheme.
  - 3.14 Securing a high level of acceptances to the opt-in invitation will provide the best opportunity for Public Sector Audit Appointments to achieve the most competitive prices from audit firms. The LGA has previously sought expressions of interest in the sector led body option and received positive expressions of interest from over 270 relevant authorities.
  - 3.15 Public Sector Audit Appointments Ltd has since issued a letter to the Council regarding the invitation to opt in to the national scheme for auditor appointments. Also included is additional information regarding the national scheme which sets out the proposed timescales for the appointment process. The closing date for opting in to the scheme is 9<sup>th</sup> March 2017 and the award of contracts is due by the end of June.
  - 3.16 The intention would be for the External Auditor to be appointed for a period of five financial years beginning 1<sup>st</sup> April 2018.

## *Advantages/benefits*

- 3.17 The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities.
- 3.18 By offering large contract values the firms would be able to offer better rates and lower fees than are likely to result from local negotiation.
- 3.19 Any conflicts at individual authorities would be managed by the Public Sector Audit Appointments Ltd who would have a number of contracted firms to call upon.
- 3.20 The appointment process would not be ceded to locally appointed independent members, instead a separate body set up to act in the collective interests of the 'opt-in' authorities would do this. There would be no need to establish an Auditor Panel.
- 3.21 Earlier in the year the Local Government Association wrote to all local authority Chief Executives inviting them to express an interest in using a sector led body. Audit Committee agreed to express a (non-binding) interest in using the sector led body.
- 3.22 Public Sector Audit Appointments would deal with the replacement of an External Auditor if required.

## *Disadvantages/risks*

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- 3.23 Individual councillors would have less opportunity for direct involvement in the appointment process other than through the Local Government Association and/or stakeholder representative groups.
- 3.24 In order for Public Sector Audit Appointments Ltd to be viable and to be placed in the strongest possible negotiating position the sector led body will need councils to indicate their intention to opt-in before final contract prices are known.

## Option 2 – To make a stand-alone appointment

- 3.25 In order to make a stand-alone appointment the Council will need to set up an Auditor Panel. The members of the panel must be made up wholly, or with a majority, of independent members as defined by the 2014 Act.
- 3.26 Independent members for this purpose are independent appointees, which excludes current and former councillors (or officers) and their close families and friends. This means that elected members will not have a majority input to assessing bids and choosing which firm of accountants to award a contract for the Council's external audit. A new independent Auditor Panel established by the Council will be responsible for selecting the auditor.

## *Advantages/benefit*

- 3.27 Setting up an Auditor Panel would allow the Council to take maximum advantage of the new local appointment regime and have local input to the decision.

## *Disadvantages/risks*

- 3.28 Recruitment and servicing of the Panel, running the bidding exercise and negotiating the contract is estimated by the Local Government Association to cost in the order of £15,000 plus on-going expenses and allowances.
- 3.29 The Council would not be able to take advantage of reduced fees that may be available through joint or national procurement contracts.
- 3.30 The assessment of bids and decision on awarding contracts would be taken by independent appointees and not solely by elected Members.

## Option 3 – Set up a Joint Auditor Panel / Local procurement arrangements

- 3.31 The 2014 Act enables the Council to join with other authorities to establish a joint Auditor Panel. Again this will need to be constituted of wholly, or a majority, of independent appointees. Further legal advice will be required on the exact constitution of such a panel having regard to the obligations of each Council under the Act. Council would need to liaise with other local authorities to assess the appetite for such an arrangement.

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## *Advantages/benefits*

- 3.32 The costs of setting up the panel, running the bidding exercise and negotiating the contract would be shared across a number of authorities.
- 3.33 There is greater opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms than if option 2 was selected.

## *Disadvantages/risks*

- 3.34 The decision making body would be further removed from local input, with potentially no input from councillors where a wholly independent Auditor Panel is used or possibly only one elected member representing each Council, depending on the constitution agreed with the other bodies involved.
- 3.35 The choice of auditor could be complicated where individual Councils have independence issues. An independence issue could occur where the auditor has recently or is currently carrying out work such as consultancy or advisory work for the Council. Where this occurs some auditors may be prevented from being appointed by the terms of their professional standards. There is a risk that if the joint auditor panel choose a firm that is conflicted for this Council then the Council may still need to make a separate appointment with all the attendant costs and loss of economies possible through joint procurement.

## Conclusion and next steps

- 3.36 The Council has until December 2017 to make an appointment. In practical terms this means one of the options outlined in this report will need to be in place by spring 2017 in order that the contract negotiation process can be carried out during 2017.
- 3.37 Audit Committee recommends that the Council pursue Option 1 on the basis that it should provide a more cost effective option in both the contracting process and for on-going external audit fees (Audit Committee Minute number 33 2016/17 refers). It is therefore recommended to Cabinet that it recommends to Council that Option 1 is approved.
- 3.38 Public Sector Audit Appointments Ltd will be communicating with all Local Government bodies shortly to outline the next steps in the process of letting external audit contracts, and to provide more information on their own offer.
- 3.39 If opting in to the option to the procurement of the external audit contract by Public Sector Audit Appointments Ltd, this will need to go through a full Council meeting before February 2017 so that their timescales can be met (deadline is 9<sup>th</sup> March 2017). The next scheduled meeting is 16<sup>th</sup> January 2017.

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3.40 If option 1 is selected the expected timescale is as follows:

Invitation to opt in issued	27 <sup>th</sup> October 2016
Closing date for receipt of notices to opt in	9 <sup>th</sup> March 2017
Contract notice published	20 <sup>th</sup> February 2017
Award audit contracts	By end of June 2017
Consult on and make auditor appointments	By end of December 2017
Consult on and publish scale fees	By end of March 2018

## 4. Alternative Options

4.1 Not Applicable, the Council is required by law to appoint external auditors.

## 5. Implications, Diversity Impact Assessment and Risk Management

### Financial and Procurement Implications

- 5.1 Should the Council decide to establish a local or joint Auditor Panel as outlined in options 2 and 3 above, the cost will need to be estimated and a suitable funding source be identified. This will include the cost of recruiting independent appointees (members), servicing the Panel, running a bidding and tender evaluation process, letting a contract and paying members fees and allowances.
- 5.2 Opting-in to a national Sector Led Body provides maximum opportunity to benefit from economies of scale by entering in to a large scale collective procurement arrangement and would remove the costs of establishing an auditor panel.

### Legal and Human Rights Implications

- 5.3 Section 7 of the Local Audit and Accountability Act 2014 (the Act) requires a relevant authority to appoint a local auditor to audit its accounts for a financial year not later than 31<sup>st</sup> December in the preceding year. Section 8 governs the procedure for appointment including that the authority must consult and take account of the advice of its auditor panel on the selection and appointment of a local auditor. Section 8 provides that where a relevant authority is a local authority operating executive arrangements, the function of appointing a local auditor to audit its accounts is not the responsibility of an executive of the authority under those arrangements;
- 5.4 Section 12 makes provision for the failure to appoint a local auditor: the authority must immediately inform the Secretary of State, who may direct the authority to

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appoint the auditor named in the direction or appoint a local auditor on behalf of the authority.

- 5.5 Section 17 gives the Secretary of State the power to make regulations in relation to an 'appointing person' specified by the Secretary of State. This power has been exercised in the Local Audit (Appointing Person) Regulations 2015 (SI 192) and this gives the Secretary of State the ability to enable a Sector Led Body to become the appointing person.
- 5.6 The Local Audit (Appointing Person) Regulations 2015 require that a principal authority may only make the decision to opt into the sector led body arrangement by the members of the authority meeting as a whole.
- 5.7 Legal and Human Rights considerations have been taken fully into account in compiling this report. It is considered that the recommendations of this report are compatible with Convention Rights.
- 5.8 The Council is required to comply with the statutory provisions referred to in the report. All other legal and human rights implications have been considered in the preparation of this report.

## All Other Implications (including Staff, Sustainability, Health, Rural, Crime and Disorder)

- 5.9 None.

## Diversity Impact Assessment

- 5.10 A Diversity Impact Assessment has not been completed for this report. This is because the external audit provision will continue to be provided but the responsibility for doing this will potentially transfer to a different external supplier. There will be no change to staffing or service eligibility.

## Risk Management

- 5.11 There is no immediate risk to the Council. However, early consideration by the Council of its preferred approach will enable detailed planning to take place so as to achieve successful transition to the new arrangement in a timely and efficient manner.
- 5.12 Providing the Local Government Association with a realistic assessment of our likely way forward will enable the Local Government Association to invest in developing appropriate arrangements to support the Council.

## **6. Consultees**

- 6.1 The Chief Executive.



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- 6.2 The Corporate Director: Resources (Section 151 Officer) and Director of Law and Democratic Services (Monitoring Officer) are consulted in respect of all reports.

## **7. Background Papers**

- 7.1 Invitation letter from Chief Officer, Public Sector Audit Appointments.
- 7.2 Information on the national scheme and Form of notice of acceptance of the invitation to opt in.

## **8. Appendices**

- 8.1 None.

## **9. Key Decision/Decision in Cabinet Work Programme and Forward Plan**

- 9.1 This is not a key decision and is included in the Cabinet Work Programme and Forward Plan for October 2016.