

Wards Affected:

All Wards

Report considered by Cabinet – 3 January 2017

CHANGES TO ARRANGEMENTS FOR THE APPOINTMENT OF EXTERNAL AUDITORS

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Executive Summary:

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 audit of the accounts.

There are in essence two options for appointing external auditors for the Council from 2018/19 which are (1) to opt-in to a sector led national procurement arrangement, and (2) to appoint an independent Auditor Panel and procure locally.

The report sets out the advantages and disadvantages of each option ultimately recommending that the Council opt-in to the sector led procurement arrangement. The rationale for this recommendation being the need to set up, service and pay for an independent Auditor Panel, the complexity in developing the specification for a local procurement of external auditors, undertaking the procurement, negotiating the final contractual position and then managing the contract on an ongoing basis. All of this would be undertaken by the sector led body meaning resources can be focussed on the actual production and quality of the Statement of Accounts.

1. Recommendations

- 1.1 That the Council be recommended to approve the opt-in to the sector led body (Public Sector Audit Appointments) for the national procurement of external auditors and ultimately the Council's external auditors from 2018/19, which is the Audit Committee's recommended approach.
- 1.2 That officer colleagues be requested to write to Public Sector Audit Appointments and request to meet with its Chief Officer to seek assurance that a single auditor be appointed for the LGSS Partners setting out the clear rationale in terms of the efficiency and value for money that this would achieve.

2. Background and Issues

- 2.1 The Local Audit and Accountability Act 2014 has established new arrangements for the audit and accountability of relevant public sector

organisations including local authorities, clinical commissioning groups and police and crime commissioners in England.

- 2.2 The Secretary of State for Communities and Local Government decided to implement a phased introduction of the new local audit framework. There is currently a transitional period for local authorities, where the role of appointing external auditors and setting fee levels has been transferred from the now defunct Audit Committee and undertaken by the Public Sector Audit Appointments Ltd (PSAA), a subsidiary of the Local Government Association.
- 2.3 This transitional arrangement comes to an end for local authorities on 31 March 2018 with the audit of the 2017-18 financial statements. The new arrangements require local authorities to opt in to the PSAA sector-led auditor appointments, or appoint their own local external auditors, which can be done either individually or jointly with one or more other authorities by 31 December 2017.
- 2.4 The scope of the audit will continue to be specified nationally, the National Audit Office (NAO) is responsible for writing the Code of Audit Practice which all firms appointed to carry out local authority audits 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. It is less likely that small local independent firms will meet the eligibility criteria.
- 2.5 At present the current auditors for the LGSS Partners are all different with KPMG, Ernst and Young and BDO currently appointed as auditors for Northamptonshire County Council (NCC), Milton Keynes Council (MKC) and Cambridgeshire County Council (CCC) respectively. KPMG are also the auditors for Northampton Borough Council (NBC), one of LGSS's customers.
- 2.6 LGSS in 2015-16 has operated with a single integrated closedown team to deliver the financial statements including the external audit management across NCC, CCC and LGSS. This team has recently been expanded to incorporate the accounts and audit for both MKC and NBC.
- 2.7 Therefore there is a strong case to have a single external auditor across all LGSS partners. This will ensure the most effective management of the external audit relationships within the integrated closedown team. In addition a single auditor will enable efficiencies to be achieved in the audit processes and arrangements to help achieve the earlier statutory deadlines for the financial statements across all LGSS Partners.

3. **Options for the Local Appointment of External Auditors**

- 3.1 There are in effect two different approaches available to appoint external auditors with effect from the 1 April 2018, which are to:
 - (a) opt in to the PSAA sector-led appointments process; or
 - (b) establish an auditor panel to advise on the appointment of the local external auditor and to ensure the maintenance of independent relationships.

3.2 A recent LGA survey of local authorities found that 58% of authorities were expecting to 'opt in' to a sector led body, rather than appoint their own auditor. A further 35% of authorities were looking to form some kind of collective procurement arrangement.

3.3 Each of these options is considered further in the following sections.

Option 1 PSAA Sector Led National Scheme for Audit Appointments

3.4 The PSAA have been confirmed as the government's sector led body to manage the auditor appointments for those authorities opting in to this arrangement.

3.5 The ability to negotiate lower fees with the firms as a result of being able to offer higher volumes of work is considered one of the main benefits of a sector led approach. The greater the number of authorities that have signed up at the outset, the better the economies of scale that are likely to be achieved. However there is a risk that being part of a sector led arrangement will increase costs due to additional requirements that the PSAA may place on any successful audit firms.

3.6 The general legal, financial and reputational risks of undertaking a new procurement process would be mitigated for each local authority with this approach. The sector led option would also reduce the finance, procurement, legal, internal audit management overhead and staff time associated with a new procurement and establishing a new Audit Panel (refer to option 2).

3.7 There will not be a fee to join the sector led arrangements, however the audit fees that opted-in bodies will be charged by PSAA will cover the costs of appointing auditors. PSAA is not for profit and will pool scheme costs and charge fees on a scale based on size, complexity and audit risk. Surplus funds will also be returned to scheme members. The PSAA believe that highly competitive audit fees will be achieved through the sector-led procurement.

3.8 Additionally assurances have not been received from the PSAA that the opt-in arrangements could and would guarantee a single appointment across NCC, MKC and CCC. This is a risk to LGSS in terms of managing the external audit arrangements and relationships within the Integrated Closedown team which is likely to prohibit the efficiencies that can be achieved by the integrated team. However the PSAA do state that the scheme "will endeavour to appoint the same auditors to bodies which are involved in formal collaboration/joint working initiatives or with combined authority areas, if the parties consider that a common auditor will enhance efficiency and value for money" (PSAA, *Developing the option of a national scheme for local auditor appointments*).

3.9 The date by which local authorities will need to formally opt-in to the PSAA sector led appointing person arrangement is 9 March 2017. In addition to the formal agreement for any authority to opt in, the decision must be approved by the Full Council. The expectation is that the PSAA will aim to award contracts to audit firms by June 2017, giving 6 months to plan and organise which firm is appointed to each individual authority before the 31 December 2017 deadline. The expected timetable for the sector-led option is set out over the page.

Action / Milestone	Date
Invitation to opt in issued	27 October 2016
Full Council approval to opt in	January/February 2017
Closing date for receipt of notices to PSAA to opt in	9 March 2017
PSAA contract notice published	20 February 2017
PSAA award audit contracts	End of June 2017
PSAA consult on and make auditor appointments	End of December 2017
PSAA consult on and publish scale fees	End of March 2018

- 3.10 Authorities will not be prevented from joining the sector-led arrangements in later years but the earliest opportunity to opt in after the closing date will be after 1 April 2018 with the appointment of auditors for 2019-20 accounts. However, in order to be in the best position to negotiate good rates for authorities the PSAA is encouraging as many authorities as possible to opt in from the outset.

Option 2 Appoint an Independent Audit Panel and Locally Procure

- 3.11 There are different options available if an Audit Panel approach is to be adopted which are:
- (a) a separate and individual auditor panel, solely for one Council only;
 - (b) a joint auditor panel with one or more other authorities, such as the LGSS Partner Authorities;
 - (c) using the services of or using an existing committee or sub-committee to act as the auditor panel (subject to compliance with the other provisions and regulations relating to auditor panels); or
 - (d) using another authority's auditor panel to carry out the functions for another Council.
- 3.12 The use of an Auditor Panel and a local procurement would achieve the intended outcome of having a single external auditor for the LGSS Partners. However there are further complexities, risks and costs associated with this approach. For each option above a procurement exercise will be necessary as well as full Council approval along with funding to meet the costs of a local procurement process. Costs will include the recruitment of independent appointees (members), servicing the Panel, running a bidding and tender evaluation process (and any retenders in subsequent years), letting a contract and managing the contract, and paying members fees and allowances.
- 3.13 CIPFA has issued guidance on the Auditor panel the link to which can be found in the Source Documents section.

- 3.15 The Auditor Panel must comply with the following requirements:
- (a) the minimum number of members that an auditor panel must have is three;
 - (b) there must be a majority of independent members as well as an independent Chair. For a panel meeting to be quorate, there must be a majority of independent members present at the meeting;
 - (c) for joint auditor panels, it is likely that each authority will want to have representative members. For each additional member, there will need to be an additional independent member;
 - (d) specific regulations clarify how independence is to be defined for the purposes of auditor panels;
 - (e) panel members should have a certain level of specific knowledge and experience to ensure that the panel carries out its duties effectively. Authorities will need to ensure that they draft panel member job descriptions carefully and advertise widely enough to reach those potential candidates with the correct skills and experience and maximise the number of suitable applicants for those vacancies; and
 - (f) panel members may be paid an allowance and any reasonable expenses covered, but it is for authorities to determine such arrangements themselves.
- 3.16 Following these principles would mean that the audit panel responsibility could not be transferred to an existing LGSS partner authority Audit Committee, due to the lack of independent members. As such a new Committee would need to be established, which would be expected to work alongside the existing Audit Committees at each LGSS Partner.
- 3.17 CIPFA have indicated that there is likely to only be the requirement for a few audit panel meetings during the external audit procurement exercise, and very few meetings once the external auditor has been procured. CIPFA have also advised that there would be little involvement from existing Audit Committees other than being informed of progress and decisions and offering comment.
- 3.18 There are a number of advantages and disadvantages of a local audit procurement exercise, overseen by an Auditor Panel, which vary depending on the specific type of Auditor Panel that is established. These are set out in the attached **Annex**.

Audit Committee Endorsement

- 3.19 The Auditor Appointment arrangements have been discussed with the Audit Committee at its meeting on 28 September 2016. The Audit Committee supports the recommendation of opting into the sector led procurement.

4. Implications

4.1 Policy

The decision required is linked to the Council's statutory requirement to prepare and have independently audited its annual Statement of Accounts.

4.2 Resources and Risk

There are no resources or risk implications arising directly from the recommended decision.

N	Capital	N	Revenue	N	Accommodation
N	IT	N	Medium Term Plan	N	Asset Management

4.3 Carbon and Energy Management

The proposal of this report does not have any implications regarding the Council's Carbon and Energy Management Policy.

4.4 Legal

The legal position is set out within Section 3 of this report. In addition the following should be noted.

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 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. Schedule 3 of the Act 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.

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

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.

4.5 Other Implications

There are no other significant implications arising directly from this decision.

N	Equalities/Diversity	N	Sustainability	N	Human Rights
N	E-Government	N	Stakeholders	N	Crime and Disorder

Annex: Advantages and Disadvantages of the Auditor Panel Approach

Background Papers:

Source Documents	Location
The Local Audit and Accountability Act 2014	http://www.legislation.gov.uk/ukpga/2014/2/contents
CIPFA Guide to Auditor Panels	http://www.cipfa.org/policy-and-guidance/publications/g/guide-to-auditor-panels-pdf
Developing the Option of a National Scheme for Local Auditor Appointments	http://www.psaa.co.uk/wp-content/uploads/2016/08/PSAA-A5-web-portrait-August-2016.pdf