



## **TELFORD & WREKIN COUNCIL**

**AUDIT COMMITTEE 20TH SEPTEMBER 2016**

**APPOINTMENT OF EXTERNAL AUDITORS BY 31/12/17 FOR APRIL 2018 ONWARDS**

**REPORT OF THE CHIEF FINANCIAL OFFICER**

### **1. Purpose of Report**

- 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 Audit Committee changed their terms of reference at the June 2016 meeting and these changes were ratified by Council in July 2016. The changes included that the “Committee recommend the appointment of the External Auditors to the Council”.
- 1.3. This report:
  - a) sets out the options available for the future appointment of external auditors under the relevant legislation;
  - b) seeks the agreement of the Audit Committee for the Council to opt into the Sector Led Body (Public Sector Audit Appointment Ltd - PSAA) procurement route and recommends that the Council approves opting into the PSAA for the procurement of the External Auditors;
  - c) a further report will be presented to the September 2017 Audit Committee so that the Audit Committee can recommend to full Council the appointment of External Auditors by 31 December 2017 ready for 1<sup>st</sup> April 2018.

### **2. Recommendations**

#### **2.1 Members are required to:**

- a) Note the information and options available as set out in section 4 of the report;**
- b) That the Audit Committee agrees that the Council uses option 3, the national Sector Led Body (SLB) appointed by the Government – Public Sector Audit Appointments Ltd to undertake the procurement;**
- c) That the Audit Committee recommends that full Council approves opting into the PSAA for the purpose of appointing External Auditors for 2018/19 onwards;**

- d) Agree that the CFO (or their delegated officer) takes appropriate actions following the Council decision to opt into the PSAA procurement process and engages with the PSAA to inform their specifications and proposed supplier in order to ensure appropriate independence; and**
- e) Note that a further report will be presented to the Audit Committee in September 2017 so that the Committee can agree and recommend the appointment of the External Auditor to full Council by 31 December 2017.**

### **3. Background**

- 3.1. The Local Audit and Accountability Act 2014 (“the Act”) brought to a close the Audit Commission and established transitional arrangements for the appointment of external auditors and the setting of external audit fees for all local government and NHS bodies in England.
- 3.2 On 5 October the Secretary of State Communities and Local Government (CLG) 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 KPMG, this appointment having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the contract is currently being managed by Public Sector Audit Appointments Limited (PSAA Ltd), the transitional body set up by the LGA with delegated authority from the Secretary of State CLG. Over recent years we have benefited from reductions in fees in the order of 50% compared with historic levels. 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. The Council’s current external audit fees are just over £117,000 per annum (excluding grant certification fees).
- 3.4 When the current transitional arrangements come to an end on 31 March 2018 the Council will be able to move to local appointment of the external auditor. There are three options 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.

- 3.5 The scope of the audit will still be specified nationally, the National Audit Office (NAO) is responsible for writing the Code of Audit Practice which all firms appointed to carry out the Council’s external 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. The registration process has not yet commenced and so the number of firms is not known but it is reasonable to expect that the list of eligible firms may include the top 10 or 12 firms in the country, including our current auditor. It is unlikely that small local independent firms will meet the eligibility criteria.

3.6 In accordance with Regulation 19 of the Local Audit (Appointing Person) Regulations 2015, a principal authority will need to make the decision to opt in at full Council.

#### **4. Options for local appointment of External Auditors**

4.1. There are three broad options open to the Council under the Act:

##### **Option 1 To make a stand-alone appointment**

4.2. 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 wholly or a majority of independent members as defined by the Act. Independent members for this purpose are independent appointees, this excludes current and former elected members (or officers) and their close families and friends. This option means that the current Audit Committee/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/recommending the auditor appointment to the Council. This is because we do not have an existing independent committee suitably constituted to do this.

##### *Advantages/benefit*

4.3. Setting up an auditor panel allows the Council to take maximum advantage of the new local appointment regime and have local input to the decision.

##### *Disadvantages/risks*

4.4. Recruitment and servicing of the Auditor Panel, running the bidding exercise and negotiating the contract is estimated by the LGA to cost at least £15,000 plus on going expenses and allowances

4.5. The Council will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts.

4.6. The assessment of bids and decision on awarding contracts will be taken by independent appointees and not solely by elected members.

##### **Option 2 Set up a Joint Auditor Panel/local joint procurement arrangements**

4.7. The 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 (members). 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 and the Council need to liaise with other local authorities to assess the appetite for such an arrangement.

##### *Advantages/benefits*

4.8. The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities.

4.9. There is an opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.

### *Disadvantages/risks*

- 4.10. The decision making body will be further removed from local input, with potentially no input from elected members 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.
- 4.11. The choice of auditor could be complicated where individual Councils have independence issues. An independence issue occurs 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.

### **Option 3 Opt-in to a sector led body**

- 4.12. In response to the consultation on the new arrangement the LGA successfully lobbied for Councils to be able to 'opt-in' to a Sector Led Body (SLB) appointed by the Secretary of State under the Act. The Secretary of State has concluded the process of appointing the sector led body and this is Public Sector Audit Appointments Ltd (an independent company limited by guarantee incorporated by the Local Government Association). The PSAA will be able 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. The benefits to members of joining the PSAA are set out in their prospectus (July/August 2016) to develop the national scheme and are listed in Appendix A.
- 4.13. In accordance with Regulation 19 of the Local Audit (Appointing Person) Regulations 2015, a principal authority will need to make the decision to opt into the PSAA at a full council meeting. The Audit Committee would therefore need to recommend this option for the decision to be made by full council.

### *Advantages/benefits*

- 4.14. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities
- 4.15. By offering large contract values the firms would be able to offer better rates and lower fees than are likely to result from local packages and negotiation
- 4.16. Any conflicts at individual authorities would be managed by the PSAA who would have a number of contracted firms to call upon.
- 4.17. The Council will not need to set up an Auditor Panel and so the process of appointing local independent members would not be required. Instead the PSAA will act in the collective interests of the 'opt-in' authorities.

### *Disadvantages/risks*

4.18. Individual elected members will have less opportunity for direct involvement in the appointment process other than through the PSAA and/or stakeholder representative groups.

4.19. In order for PSAA to be placed in the strongest possible negotiating position they may need Councils to indicate their intention to opt-in before final contract prices are known.

4.20. All options comply with the Councils contract regulations.

## **5. OTHER CONSIDERATIONS**

<b>AREA</b>	<b>COMMENTS</b>
Equal Opportunities	Any procurement and ensuing external audit work will comply with equalities and diversity legislation.
Environmental Impact	Any procurement and contracts established will encompass appropriate sustainability issues.
Legal Implications	<p>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.</p> <p>Section 12 of the Act 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.</p> <p>Regarding option 3 in the report above, section 17 of the Act gives the Secretary of State the power to make regulations in relation to an ‘appointing person’ specified by the Secretary of State. This power was exercised in the Local Audit (Appointing Person) Regulations 2015/192 (“the Regulations”) and this gave the Secretary of State the ability to enable a Sector Led Body to become the appointing person.</p> <p>. Effectively this means that the Council will ask the ‘appointed person’ (sector led body) to undertake the local auditor selection process on its behalf and make recommendations back to the council for approval. Regulation 19 of the Local Audit (Appointing Person) Regulations 2015, sets out that a principal authority will need to make the decision to opt into the PSAA at a full council meeting.</p>
Links with Corporate Priorities	Independent External Auditors contribute to the good governance arrangements of the Council and serving the community in the most cost effective way.
Risks and Opportunities	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 manage the risks and achieve successful transition to the new arrangement in a timely and efficient manner.
Financial Implications	It is anticipated that the Sector Led Body option will result in a lower fee than could be negotiated by an individual authority locally, through economies of scale from the large scale contracts negotiated by PSAA Ltd. In addition PSAA Ltd have indicated that:

	<ul style="list-style-type: none"> <li>• there will not be a fee to join the sector led arrangements;</li> <li>• the greater number of authorities who opt in will result in greater economies of scale; therefore PSAA have requested that authorities indicate their intention early in 2017, prior to the actual audit fees being known;</li> <li>• The actual audit fees will not be known until later in the process and will reflect the size of the authority, the audit risk and complexity of work required;</li> <li>• PSAA Ltd is a not-for-profit organisation and will return any surpluses to participating authorities.</li> </ul> <p>Following this option the Council will also avoid the costs of running a separate procurement process and the costs associated with having an independent Auditor Panel.</p> <p>It is hoped that the audit fee will be accommodated within the current revenue budget available; however as the external audit function is a statutory requirement any additional cost incurred will be built into the budget strategy as appropriate. PH 30/8/2016</p>
Ward Implications	The work of the external auditor encompasses all Council activities and all Council locations. Therefore all Council Wards could be affected by its operations.

## 6. BACKGROUND PAPERS

Local Audit and Accountability Act 2014

Local Audit (Appointing Person) Regulations 2015 (SI 192)

PSAA Ltd – Developing the option of a national scheme for local auditor appointments

**Report by Jenny Marriott, Audit, Information Governance, Insurance & Investigation services SDM 383101; Matthew Cumberbatch – Democratic & Legal Services Manager; Pauline Harris – Finance Manager – Corporate Finance & Customer Services.**

### PSAA - Developing the National Scheme for Local Auditor Appointments

Benefits for participating bodies include:

- assured appointment of a qualified, registered, independent auditor
- appointment, if possible, of the same auditors to bodies involved in significant collaboration/ joint working initiatives or combined authorities, if the parties believe that it will enhance efficiency and value for money
- on-going management of independence issues
- securing highly competitive prices from audit firms
- minimising scheme overhead costs
- savings from one major procurement as opposed to a multiplicity of small procurements
- distribution of surpluses to participating bodies
- a scale of fees which reflects size, complexity and audit risk
- a strong focus on audit quality to help develop and maintain the market for the sector
- avoiding the necessity for individual bodies to establish an auditor panel and to undertake an auditor procurement
- enabling time and resources to be deployed on other pressing priorities
- setting the benchmark standard for audit arrangements for the whole of the sector