

Corporate Governance and Standards Committee

Report of Managing Director

Author: Joan Poole

Tel: 01483 444854

Email: joan.poole@guildford.gov.uk

Lead Councillor responsible: Michael Illman

Tel: : 07742 731535

Email: michael.illman@guildford.gov.uk

Date: 24 November 2016

## Future of External Audit

### Executive Summary

This report provides councillors with an update on arrangements for local authorities to appoint their own external audit provision following the closure of the Audit Commission.

### Recommendation to Council (6 December 2016):

That the Council approves Option 3, as described in this report, which is to opt-in to the appointing person arrangements made by Public Sector Audit Appointments (PSAA) for the appointment of external auditors from 2018-19.

### Reason for Recommendation:

To enable the Council to comply with statutory obligations under Section 7 of the Local Audit and Accountability Act 2014.

### 1. Purpose of Report

- 1.1 This report sets out the proposals for the future of external audit and the options open to the Council. The Committee is asked to endorse the recommendation that the Council appoints PSAA Ltd as its external auditor.

### 2. Strategic Priorities

- 2.1 The 'Your Council' theme within the revised Corporate Plan 2015-20 includes the Council's key priorities of ensuring sound financial governance and improving value for money and efficiency in service delivery. The appointment of the external auditor contributes to the achievement of those priorities.

### **3. The future of External Audit in Local Government**

- 3.1 Following enactment of the Local Audit and Accountability Act 2014 ('the Act'), the Audit Commission ceased to exist on 31 March 2015. Since then, external audit has been provided through a series of framework contracts for the audit of local bodies, which will run until 2018.
- 3.2 Responsibility for managing the audit contracts for local government bodies, along with the Commission's statutory functions for audit (e.g. setting the standards of performance, appointing auditors, setting and determining fees) and value for money work has transferred to an independent private company created by the Local Government Association (LGA).
- 3.3 Once the current audit contracts run out in 2018, local bodies will be able to appoint their own external and independent auditor and will need to do so by 31 December 2017. The length of appointment, which is yet to be finally determined, is expected to be between three and five years. The decision will need to be made by full Council and cannot be delegated. Local bodies have to establish, consult and take into account the advice of an independent auditor panel on the selection and appointment of a local auditor.

### **4. Options**

#### Option1 – Stand Alone Appointment

- 4.1 In order to make a stand-alone appointment, the Council will need to set up an Auditor Panel. The panel must be made up of 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 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.
- 4.2 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. However, recruitment and servicing of the Auditor Panel, running the bidding exercise and negotiating the contract is estimated by the LGA to cost in the order of £15,000 plus ongoing expenses and allowances. The Council will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts and the assessment of bids and the decision on awarding contracts will be taken by independent appointees and not solely by elected members.

#### Option 2 – Joint Auditor Panel

- 4.3 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). 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 would need to liaise with other local authorities to assess the appetite for such an arrangement.

- 4.4 The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities and there is greater opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.
- 4.5 However, 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. 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 a 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 chooses 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 – Sector Led Body (PSAA)

- 4.6 In response to the consultation on the new arrangements, the government have appointed a national provider, Public Sector Audit Appointments Ltd (PSAA) to make auditor appointments to opted-in local government bodies. The (PSAA) 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. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities and 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. Any conflicts at individual authorities would be managed by the PSAA who would have a number of contracted firms to call upon. If we wish to be included, it is anticipated that the Council would have to opt in before December 2016. In addition to the economies of scale, which could be achieved under the national scheme, other benefits include:

- assured appointment of a qualified, registered, independent auditor
- appointment, if possible, of the same auditors to bodies involved in significant collaboration and joint working initiatives or combined authorities
- distribution of surpluses to participating authorities
- a scale of fees which reflects size, complexity and audit risk
- avoiding the necessity for individual authorities to establish an auditor panel and to undertake an auditor procurement
- enabling time and resources to be deployed on other pressing priorities

Option 3 is recommended as the Council's preferred option.

- 4.7 However, individual elected members will have less opportunity for direct involvement in the appointment and the final fee structure from the PSAA will require councils to indicate their intention to opt-in before final contract prices are known.

## **5. Consultations**

- 5.1 None

## **6. Equality and Diversity Implications**

- 6.1 There are no equality and diversity implications associated with the decision in respect of this matter.

## **7. Financial Implications**

- 7.1 Opting-in to the PSAA provides maximum opportunity to limit the extent of any increases by entering in to a large scale collective procurement arrangement and would remove the costs of establishing an auditor panel.

## **8. Legal Implications**

- 8.1 Section 7 of 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. Section 8 also 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.
- 8.2 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.
- 8.3 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 2015 No. 192) and this gives the Secretary of State the ability to enable a Sector Led Body to become the appointing person.

## **9. Human Resource Implications**

- 9.1 There are no human resource implications associated with the decision in respect of this matter.

## **10. Summary of Options**

Option 1: To make a stand-alone appointment;

Option 2: To set up a joint Auditor Panel / local joint procurement arrangements; and

Option 3: To opt-in to a sector led body.

- 10.1 The Council needs to take a decision on the preferred option for the future of external audit at Guildford. There is no immediate risk to the Council; however, early consideration of the preferred option of the three available will enable detailed planning to take place to achieve successful transition to the new arrangement in a timely and efficient manner. Officers recommend Option 3 as the Council's preferred option.

## **11. Conclusion**

- 11.1 The Council has until December 2017 to make an appointment. In practical terms, this means one of the three 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. There has been strong interest in the national scheme and we are one of the 58% of respondents who have expressed an interest in this option (Option 3). The LGA is supportive of the national approach, as it believes this offers best value to councils by reducing set-up costs and having the potential to negotiate lower audit fees. It is likely that a sector wide procurement conducted by PSAA will produce better outcomes for the Council than any procurement we undertook by ourselves or with a limited number of partners. Use of the PSAA will also be less resource intensive than establishing an auditor panel and conducting our own procurement. Officers recommend Option 3 as the Council's preferred option.
- 11.2 Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in must be made by Full Council (authority meeting as a whole). To comply with this regulation, the Committee is asked to endorse the recommendation to Council.

## **12. Background Papers**

None

## **13. Appendices**

None