

## **COUNCIL**

**26 JANUARY 2017**

### **APPOINTMENT OF EXTERNAL AUDITOR - DECISION TO OPT IN TO THE NATIONAL SCHEME FOR AUDITOR APPOINTMENTS**

Report from: Phil Watts, Chief Finance Officer

#### **Summary**

This report deals with the appointment of the External Auditor to the Council for the 2018/19 accounts and beyond, as the current arrangements only cover up to and including the 2017/18 audits. The report also deals with a consequential change to the Constitution.

#### **1. Budget and Policy Framework**

1.1 Decisions on how the external auditor should be appointed are a matter for Full Council.

#### **2. Background**

2.1 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 audit fees for all local government and NHS bodies in England. On 5 October 2015 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.

2.2 The Act also set out the arrangements for the appointment of auditors for subsequent years, with the opportunity for authorities to make their own decisions about how and by whom their auditors are appointed. Regulations made under the Act allow authorities to 'opt in' for their auditor to be appointed by an 'appointing person'.

2.3 In July 2016 Public Sector Audit Appointment Limited (PSAA) were specified by the Secretary of State as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015. PSAA is an independent, not-for-profit company limited by guarantee and wholly owned by the IDeA (the IDeA is wholly owned by the LGA).

2.4 The appointing person is sometimes referred to as the sector led body and PSAA has wide support across local government. PSAA was originally established to operate the transitional arrangements following the closure of the Audit Commission under powers delegated by the Secretary of State.

- 2.5 PSAA has now invited the Council to opt in, along with all other authorities, so that PSAA can enter into a number of contracts with appropriately qualified audit firms and appoint a suitable firm to be the Council's auditor.
- 2.6 The principal benefits from such an approach are as follows:
- PSAA will ensure the appointment of a suitably qualified and registered auditor and expects to be able to manage the appointments to allow for appropriate groupings and clusters of audits where bodies work together;
  - PSAA will monitor contract delivery and ensure compliance with contractual, audit quality and independence requirements;
  - Any auditor conflicts at individual authorities would be managed by PSAA who would have a number of contracted firms to call upon;
  - It is expected that the large-scale contracts procured through PSAA will bring economies of scale and attract keener prices from the market than a smaller scale competition;
  - The overall procurement costs would be lower than an individual smaller scale local procurement;
  - The overhead costs for managing the contracts will be minimised through a smaller number of large contracts across the sector;
  - There will be no need for the Council to establish alternative appointment processes locally, including the need to set up and manage an Auditor Panel;
  - The new regime provides both the perception and reality of independent auditor appointment through a collective approach; and
  - A sustainable market for audit provision in the sector will be easier to ensure for the future.
- 2.7 The Council's current external auditor is BDO, this appointment having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the contract was novated to PSAA, and since this date PSAA has demonstrated its capability in terms of auditor appointment, contract management, and monitoring audit quality. Over recent years authorities have benefited from a reduction in fees in the order of 55% compared with fees in 2012. This has been the result of a combination of factors including new contracts negotiated nationally with the audit firms and savings from closure of the Audit Commission.
- 2.8 For the 2015-16 audit, the Council's external audit fee is £142,627 for the core audit work. PSAA contracts will cover this work, but the authority will need to separately arrange for the certification of its government grants; for the 2015-16 audit these amounted to £9,188 for Certification and £4,200 for the Review of Teachers Pension Return.
- 2.9 The proposed fees for the subsequent years cannot be known until the procurement process has been completed, as the costs will depend on proposals from the audit firms.
- 2.10 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 audit must follow. Not all audit 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.

2.11 Currently, there are only nine providers that are eligible to audit local authorities and other relevant bodies; all of these being firms with a national presence. This means that a local procurement exercise, as described below, would seek tenders from these same firms, subject to the need to manage any local independence issues. Local firms could not be invited to bid.

2.12 At its meeting held on 13 October 2016 Council considered the options for appointing the External Auditor and decided to agree Option 3 (opt in to a sector led body).

### 2.13 **The invitation to opt in**

2.14 Since the October 2016 Council meeting, PSAA has now formally invited the Council to become an opted in authority to the national auditor arrangements (Appendix 1).

2.15 In summary the national opt-in scheme provides the following:

- The appointment of a suitably qualified audit firm for each of the five financial years commencing 1 April 2018;
- Appointing the same auditor to other opted in bodies that are involved in formal collaboration or joint working initiatives to the extent this is possible with other constraints;
- Managing the procurement process to ensure both quality and price criteria are satisfied. PSAA will seek views from the sector to help inform its detailed procurement strategy;
- Ensuring suitable independence of the auditors from the bodies they audit and managing any potential conflicts as they arise;
- Minimising the scheme management costs and returning any surpluses to scheme members;
- Consulting with authorities on auditor appointments, giving the Council the opportunity to influence which auditor is appointed;
- Consulting with authorities on the scale of audit fees and ensuring these reflect scale, complexity and audit risk; and
- Ongoing contract and performance management of the contracts once these have been let.

### 2.16 **Next Steps**

2.17 A decision to accept an invitation from PSAA to become an opted in authority must be made by a meeting of the Full Council. The Council then needs to formally respond to PSAA's invitation by 7 March 2017.

2.18 PSAA will commence the formal procurement process after this date. It expects to award contracts in summer 2017 and consult with authorities on the appointment of auditors so that it can make an appointment by the statutory deadline of December 2017.

2.19 PSAA will also consult on and publish audit fees by 31 March 2018. It is suggested that the Chief Finance Officer respond to these consultations on behalf of the Council, following consultation with the Audit Committee if the timescales allow.

2.20 As the Council has a number of shared services with Gravesham Borough Council there are clear benefits in the same auditor being appointed to both Councils. PSAA have advised that, in setting up the new arrangements, one of their aims is to make auditor appointments that take account of joint working and shared service arrangements. However, requests for the same auditor as other authorities will need to be balanced with auditor independence considerations.

### 3. Options

3.1 If the Council decides not to accept the invitation to opt in, then the Council would either have to make a stand alone appointment and set up an independent auditor panel or enter in to local joint procurement arrangements and establish a joint auditor panel. The report to the October Council meeting set out more details about these options.

### 4. Change to the Constitution

4.1 There is a need to add the following function of the Full Council in paragraph 4.2 of Chapter 2 (Articles of the Constitution):

*Appointing the Local Auditor in accordance with the Local Audit and Accountability Act 2014.*

### 5. Risk management

Risk	Description	Action to avoid or mitigate risk	Risk rating
Fail to appoint an auditor.	The principal risks are that the Council fails to appoint an auditor in accordance with the new frameworks or does not achieve value for money in the appointment process.	These risks are considered best mitigated by opting in to the sector led approach through PSAA.	E2

### 6. Consultation

6.1 There was no requirement to consult with the public on this issue but the views of the Audit Committee were sought before Council decided on its preferred option in October 2016.

### 7. Financial implications

7.1 There is a risk that current external fees levels could increase when the current contracts end in 2018.

7.2 Opting-in to a national scheme provides maximum opportunity to ensure fees are as low as possible, whilst ensuring the quality of audit is maintained by entering in to a large scale collective procurement arrangement.

- 7.3 If the national scheme is not used, some additional resource may be needed to establish an auditor panel and conduct a local procurement. Until a procurement exercise is completed it is not possible to state what, if any, additional resource may be required for audit fees for 2018/19.

## **8. Legal implications**

- 8.1 Section 7 of the Local Audit and Accountability Act 2014 requires a relevant Council 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 Council 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 Council is a local Council operating executive arrangements, the function of appointing a local auditor to audit its accounts is not the responsibility of an executive of the Council under those arrangements.
- 8.2 Section 12 makes provision for the failure to appoint a local auditor: the Council must immediately inform the Secretary of State, who may direct the Council to appoint the auditor named in the direction or appoint a local auditor on behalf of the Council.
- 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 192) and this gives the Secretary of State the ability to enable a Sector Led Body to become the appointing person. In July 2016 the Secretary of State specified PSAA as the appointing person.
- 8.4 Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to accept an invitation to become an opted in authority must be made by a meeting of the Full Council

## **9. Recommendations**

- 9.1 That, under the provisions of the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015, the Council accepts Public Sector Audit Appointments' invitation to become an opted in authority for the purposes of the appointment of external auditors for five financial years commencing 1 April 2018.
- 9.2 That the Chief Finance Officer is authorised to sign the notice of acceptance of the invitation to become an opted in authority.
- 9.3 That the Chief Finance Officer is authorised, following consultation with the Audit Committee if the timescales allow, to respond to consultations from the PSAA regarding the appointment of the Council's auditor and the proposed scale of audit fees.
- 9.4 That the Council agrees the proposed amendment to the Constitution set out in paragraph 4.

**Lead officer contact**

Phil Watts, Chief Finance Officer, 01634 332220, [phil.watts@medway.gov.uk](mailto:phil.watts@medway.gov.uk).

**Appendices**

Appendix 1 – Invitation from PSAA to opt in.

**Background papers**

None

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**Text of email sending invitation to opt in to all principal LG bodies**

To: [email address for Chief Executive and Director of Finance for each audited body]

cc: [monitoring officer]

Date: 27 October 2016

Subject: [Name of audited body]

**Invitation to become an opted-in authority**

**The Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015 (the Regulations)**

Public Sector Audit Appointments Limited (PSAA), being an appointing person for the purposes of the Regulations, invites [name of audited body] (the authority) to become an-opted in authority in accordance with the Regulations.

Further information is contained in the opt-in letter and additional information attached to this email. The length of the compulsory appointing period is the 5 consecutive financial years commencing 1 April 2018.

A decision to become an opted-in authority must be taken in accordance with the Regulations, that is by the members of an authority meeting as a whole, except where the authority is a corporation sole, such as a police and crime commissioner, in which case this decision can be taken by the holder of that office.

The closing date to give notice to PSAA of the authority's acceptance of our invitation is: **9 March 2017**.

A form of notice of acceptance is enclosed with this invitation to opt in. The notice of acceptance must be sent by email to: [appointingperson@psaa.co.uk](mailto:appointingperson@psaa.co.uk) and must be received before **5pm on Thursday 9 March 2017**.

PSAA confirms it is willing to receive notices of acceptance by email to this address and will confirm receipt of all notices of acceptance by email.



Jon Hayes  
Chief Officer