

COUNCIL

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APPOINTMENT OF EXTERNAL AUDITOR

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Summary

This report sets out the options for the Council to appoint an external auditor for the 2023/24 financial year onwards, following the end of the current contract arrangement with Grant Thornton.

The report seeks Council approval to 'opt-in' to a Sector Led Body appointed by the Secretary of State under the Act, as recommended by the Audit Committee when it considered the report on 11 November 2021.

1. Budget and policy framework

1.1. The decision on how the external auditor should be appointed is a matter for Full Council, though Audit Committee has an advisory role.

2. Background

2.1. The Local Audit and Accountability Act 2014 brought to a close the Audit Commission and established new arrangements for the appointment of external auditors, applicable to audits of the accounts of principal local government bodies from 2018/19 onwards.

2.2. In July 2016, Public Sector Audit Appointments (PSAA) was selected by the Secretary of State for Communities and Local Government to take on the role of Appointing Person for principal local government and police bodies. After consideration by the Audit Committee, on 13 October 2016 Council resolved to accept the invitation to opt into the appointing persons arrangements made by PSAA for the appointment of external auditors.

2.3. On 15 August 2017, the Council received communication from PSAA of the intention to appoint Grant Thornton (UK) LLP as the auditor for Medway Council, and on 28 September 2017 the Audit Committee noted the appointment of Grant Thornton as the Council's auditor for five years from 1 April 2018. The audit of the 2022/23 accounts (which will take place during the 2023/24 financial year) will be the last under the current contract arrangement.

2.4. The Secretary of State has confirmed PSAA in the role of the appointing person for eligible principal bodies for the period commencing April 2023. In September 2021 the Council received a formal invitation to opt-in to the national scheme for local auditor appointments.

3. Options for the appointment of an External Auditor

3.1. There are three broad options open to the Council under the Local Audit and Accountability Act 2014 (the Act):

Option 1: To make a stand-alone appointment

3.2. In order to make a stand-alone appointment the Council would need to set up an Auditor Panel. The Members of the panel must be wholly or a majority 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 family and friends. This means that elected Members would not have a majority input into assessing bids and recommending which firm of accountants to award a contract for the Council's external audit. The role of an Auditor Panel would be to advise the Council on:

- The selection and appointment of a local auditor
- The maintenance of an independent relationship with the local auditor appointed to audit its account
- Any proposal by the Council to enter into a liability limitation agreement
- Whether to adopt a policy on purchasing non-audit services from the local auditor
- The outcome of any investigation of an auditor's resignation from office, if this occurs, or on any proposal to remove a local auditor from office.

Advantages/benefit

3.3. Setting up an auditor panel allows the Council to ensure that there is local input into the decision.

Disadvantages/risks

3.4. 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 on-going expenses and allowances.

3.5. The Council would need to consider the national requirements of the procurement exercise, which could increase the timescale of the exercise and the level of resources required.

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

3.7. The assessment of bids and decision on awarding contracts would be taken by independent appointees and not solely by elected Members. Setting up an auditor panel allows the Council to ensure that there is local input into the decision.

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

- 3.8. The Act enables the Council to join with other authorities to establish a joint auditor panel. Again, this would need to be constituted of wholly or a majority of independent appointees (Members). Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each Council under the Act.

Advantages/benefit

- 3.9. The costs of setting up the panel, running the bidding exercise and negotiating the contract would be shared across a number of authorities.
- 3.10. There would be greater opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.

Disadvantages/risks

- 3.11. The decision-making body would 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.
- 3.12. 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 into a sector led body (recommended option)

- 3.13. Councils are able to 'opt-in' to a Sector Led Body appointed by the Secretary of State under the Act. The Secretary of State has confirmed PSAA in the role of the appointing person for eligible principal bodies for the period commencing April 2023. This means that PSAA can make auditor appointments for audits of the accounts from 2023/24 of authorities that choose to opt into its arrangements. Before an authority opts into these arrangements it must formally accept an invitation to become an opted in authority. This decision is a matter for Full Council.
- 3.14. 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 Act enables the Council to join with other authorities to establish a joint auditor panel. Again, this would need to be constituted of wholly or a majority of independent appointees (Members). Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each Council under the Act.

- 3.15. If the Council was to decide on this option then there is no requirement to establish an Auditor Panel.

Advantages/benefit

- 3.16. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities.
- 3.17. 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.
- 3.18. Any conflicts at individual authorities would be managed by PSAA who would have a number of contracted firms to call upon.
- 3.19. The appointment process would not be ceded to locally appointed independent Members. Instead PSAA would act in the collective interests of the 'opt-in' authorities.

Disadvantages/risks

- 3.20. Individual elected Members will have less opportunity for direct involvement in the appointment process other than through the LGA and/or stakeholder representative groups.
- 3.21. In order for PSAA to be viable and to be placed in the strongest possible negotiating position, they will need Councils to indicate their intention to opt in before final contract prices are known.

4. Advice and analysis

- 4.1. Discussion with the Kent Finance Officers Association found that there is no local appetite to set up a Joint Auditor Panel/local joint procurement arrangements as set out at Option 2 above.
- 4.2. A standalone appointment, as set out at Option 1 above is considered to present financial risks as the Council may suffer higher audit fees as it would not benefit from the bulk purchasing discounts offered by Option 3. Option 1 would require significant investment in the recruitment, training, servicing and allowances to maintain an Auditor Panel.
- 4.3. As such officers would recommend the Council's interests would be best served by opting in to a Sector Led Body, as set out in Option 3. Following the Audit Committee having recommended this option to Council, Council is also formally asked to agree, under the provisions of the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015, to accept 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 2023.

4.4. The Council have until December 2022 to make an appointment. In order to opt into the national scheme as set out in Option 3, the PSAA must receive formal acceptance of the invitation to join by Friday 11 March 2022.

5. Audit Committee – 11 November 2021

5.1. The Audit Committee considered the report at its meeting on 11 November 2021 and its comments are set out below.

5.2. **Discussion:**

This report provided details of the options for the Council to appoint an external auditor for the 2023/24 financial year onwards, following the end of the current contract arrangement with Grant Thornton.

5.3. The Chief Finance Officer highlighted a number of matters set out in the report, noting that the Council had initially agreed to enter into arrangements made by Public Sector Auditor Appointments (PSAA) for the appointment of external auditors. Subsequently, Grant Thornton was appointed as the Council's auditor for five years from 1 April 2018. The audit of the 2022/23 accounts (which would take place during the 2023/24 financial year) would be the last under the current contract arrangement. He informed the Committee that he expected 99% of Local Authorities to go down this route (sector led body) again for the next contract.

5.4. Members then raised a number of questions and comments which included:

5.5. **Other options** – in response to a question regarding whether there would be a material difference by following an alternative option, the Chief Finance Officer explained that the report set out the advantages and disadvantages of the alternative options, and that in his view, there was no advantage to be gained by pursuing an alternative option.

5.6. **Increases in external audit fees** – in response to a question regarding the likelihood and level of increases in fees, the Chief Finance Officer stated that it was widely publicised that the fees which had been agreed by the PSAA had been insufficient owing to a number of factors including changes to accounting regulations and an increased burden of scrutiny on the auditor industry. In terms of fees, PSAA had set the fees for Medway Council just under £110,000 for the 2018/19 audit, whilst the eventual sum was £120,000. He advised the Committee that the Council was still in negotiations for the 2019/20 and 2020/21 audits. The PSAA recognised this burden and had recommended that fees should increase in the region of 40% for the new contracts. There had been government grants to take account of this burden, therefore, the increases should not have an impact on the Council's revenue budgets.

5.7. Members expressed some concern regarding the increase in audit fees.

5.8. **Grant Thornton – consultancy advice** – in response to a question, the Chief Finance Officer advised the Committee that, as far as he was aware, Grant Thornton were not currently undertaking any consultancy work for the Council

but in any such circumstances, consultancy services would be provided by a completely separate arm of the company, therefore, there should not be any conflict of interest.

- 5.9. **Role of the Council in the process** – in response to a question regarding whether the Council had the ability to take part and/or influence the process to ensure value for money and to ensure that it was not necessary to have to re-negotiate fees again, the Chief Finance Officer advised that the Local Authority sector had had a number of conversations with PSAA to express concern regarding PSAA’s lack of contract management, particularly given that Local Authorities had been left to negotiate the uplifts with auditors separately leading to inconsistencies and variations in fees. The Chief Finance Officer referred to Unitary Treasurers and Kent Finance Officers meetings where the PSAA had attended and had outlined their plans going forward with particular reference to contract management. He considered that the PSAA had accepted there were shortcomings in the current process.
- 5.10. **Local employment** – in response to a question on whether a requirement to support the use of local employment/apprentices could be included as part of the procurement process, the Chief Finance Officer explained that there were a small number of companies in what was a specialist market (auditing local authority accounts).
- 5.11. **Costs** – in response to a comment relating to the lack of information on costs in the report, the Chief Finance Officer stated that whilst he had referred to costs in the meeting, he acknowledged that the report should have included this information. He reiterated that Government grants would cover the uplift in fees.
- 5.12. **Other local authorities** – in response to a question, the Chief Finance Officer expected 99% of local authorities to opt into the sector led body (PSAA).
- 5.13. **Decision:**
- a) The Committee noted the future implications for external audit procurement arrangements.
 - b) The Committee recommended to Council to adopt option 3 (opt into a sector led body), as set out in section 3 of the report.

6. Risk management

Risk	Description	Action to avoid or mitigate risk	Risk rating
Failure to appoint external auditor	External audit is a statutory requirement for local authorities and the Secretary of State must appoint an auditor if the Council fails	The process to appoint an external auditor has begun well in advance of the end of the current contract.	E2

Risk	Description	Action to avoid or mitigate risk	Risk rating
	to make arrangements, risking higher cost and reputational damage.		
Increased cost of external audit	With increases in the scope and complexity of public sector audit and public scrutiny through the Redmond Review, it is highly likely that the next contract will be at higher cost.	Collective procurement as recommended at Option 3, would enable the Council to benefit from economies of scale.	A3

7. Financial implications

- 7.1. Current external fees levels are likely to increase when the current contracts end in 2023.
- 7.2. The cost of establishing a local or joint Auditor Panel outlined in options 1 and 2 above would need to be estimated and included in the Council's budget for 2023/24 onwards. This would 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.
- 7.3. Opting-in to a national Sector Led Body 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 Local Audit and Accountability Act 2014 (the Act) requires a relevant authority to appoint a local auditor (a statutory defined term) 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 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 nor can the responsibility be delegated by full council.
- 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 192) and this gives the Secretary of State the ability to enable a Sector Led Body to become the appointing person.
- 8.4. Section 19 of the Local Audit (Appointing Person) Regulations 2015 specifies that the decision to accept an invitation to become an opted in authority is a matter for Full Council.

9. Recommendations

9.1. The Council is recommended to:

- a) Note the comments of the Audit Committee, as set out in section 5 of the report.
- b) Note the future implications for external audit procurement arrangements.
- c) Agree option 3 (opt into a sector led body), as set out in section 3 of the report.
- d) Agree, under the provisions of the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015, to accept 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 2023.

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Appendices

None

Background papers

None