

**CHANGES TO ARRANGEMENTS FOR APPOINTMENT OF EXTERNAL  
AUDITORS**  
**WDA/30/16**

**Recommendation**

That:

- 1.1 Members are requested to support the Local Government Association (LGA) in setting up a national Sector Led Body by indicating an intention to “opt-in”
- 1.2 A further report is brought to Members on the preferred approach by June 2017, including details of any costs included in the 2017/18 budget.

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**Report of the Treasurer**

**1. Purpose of the 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 Authority will need to consider the options available and put in place new arrangements in time to make a first appointment by 31 December 2017.

**2. Background**

- 2.1 The Local Audit and Accountability Act 2014 brought to a close the Audit Commission and established transitional arrangements for both 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 Authority's current external auditor is Grant Thornton, this appointment having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the contract is currently managed by Public Sector Audit Appointments Limited (PSAA), the transitional body set up by the LGA with delegated authority from the Secretary of State CLG. Over recent years the Authority has benefited from a reduction in fees of some £20k 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 Authority's current external audit fees are some £29,000 per annum.

- 2.3 When the current transitional arrangements come to an end on 31 March 2018 the Authority will be able to move to a local appointment of the auditor. There are a number of routes 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.
- 2.4 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 any firm appointed to carry out the Authority's 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. Options for local appointment of External Auditors**

- 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 Authority would need to set up an Auditor Panel. Proposed members of the panel would have to 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 means that elected members would not have a majority input to assessing bids and choosing which firm of accountants to award a contract for the Authority's external audit. A new independent auditor panel established by the Authority would be responsible for selecting the auditor, which the Authority would then appoint.

#### Advantages/benefit

- 3.3 Setting up an auditor panel would allow the Authority to take maximum advantage of the new local appointment regime and have local input to 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 Authority would not be able to take advantage of reduced fees that may be available through joint or national procurement contracts.
- 3.6 The assessment of bids and decision on awarding contracts would be taken by independent appointees and not solely by elected members.

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

- 3.7 The Act enables the Authority 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 local authority under the Act and the Authority would need to liaise with other local authorities to assess the appetite for such an arrangement.

#### Advantages/benefits

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

#### Disadvantages/risks

- 3.10 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 possible only one elected member representing each local authority, depending on the constitution agreed with the other bodies involved.

- 3.11 The choice of auditor could be complicated where individual local authorities may have independence issues. An independence issue may occur where the auditor has recently or is currently carrying out work such as consultancy or advisory work for the local authority. 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 local authority then the authority 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 (Recommended option)**

- 3.12 In response to the consultation on the new arrangement the LGA successfully lobbied for local authorities to be able to 'opt-in' to a Sector Led Body (SLB) appointed by the Secretary of State under the Act. An SLB would 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. More information is included in the letter from Public Sector Audit Appointments attached at Appendix 1 to this report.

#### Advantages/benefits

- 3.13 The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities.
- 3.14 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.
- 3.15 Any conflicts at individual authorities would be managed by the SLB who would have a number of contracted firms to call upon.
- 3.16 The appointment process would not be ceded to locally appointed independent members. Instead a separate body would be set up to act in the collective interests of the 'opt-in' authorities. The LGA are considering setting up such a body utilising the knowledge and experience acquired through the setting up of the transitional arrangements.

#### Disadvantages/risks

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

- 3.18 In order for the SLB to be viable and to be placed in the strongest possible negotiating position the SLB will need local authorities to indicate their intention to opt-in before final contract prices are known

#### **4. The way forward**

- 4.1 The Authority has until December 2017 to make an appointment. In practical terms this means one of the 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.
- 4.2 The LGA are working on developing a Sector Led Body. In a recent survey, 58% of respondents expressed an interest in this option. The greatest economies of scale are likely to come from the maximum number of local authorities acting collectively and opting-in to a SLB. In order to strengthen the LGA's negotiating position and enable it to more accurately evaluate the offering the Authority is asked to consider whether it is interested in the option of opting in to a SLB. A formal decision to opt-in will be required at a later date.

#### **5. Risk Implications**

- 5.1 There is no immediate risk to the Authority; however, early consideration by the Authority of its preferred approach will enable detailed planning to take place so as to achieve successful transition to the new arrangement in a timely and efficient manner.
- 5.2 Providing the LGA with a realistic assessment of our likely way forward will enable the LGA to invest in developing appropriate arrangements to support the Authority.

#### **6. HR Implications**

- 6.1 There are no HR implications associated with this report.

#### **7. Environmental Implications**

- 7.1 There are no environmental implications associated with this report.

#### **8. Financial Implications**

- 8.1 Current external fees levels are likely to increase when the current contracts end in 2018.

- 8.2 The cost of establishing a local or joint Auditor Panel outlined in options 1 and 2 above will need to be estimated and included in the Authority's budget for 2017/18 and beyond. This will include the cost of recruiting independent appointees (members), servicing the Panel, running a bidding and tender evaluation process, letting a contract and potentially paying independent members' fees and allowances.
- 8.3 Opting-in to a national SLB 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.

## **9. Legal Implications**

- 9.1 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. 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;
- 9.2 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.
- 9.3 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

## **10. Conclusion**

- 10.1 The Authority will need to take action to implement new arrangements for the appointment of external auditors from April 2018. In order that more detailed proposals can be developed the Authority is asked to give early consideration to the preferred approach.
- 10.2 The Authority has been asked by the LGA for an indication of the preferred approach in order that it can invest resources in providing appropriate

support to local authorities. The LGA is strongly supportive of the SLB approach as it believes this offers best value to local authorities by reducing set-up costs and having the potential to negotiate lowest fees

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The background documents to this report are open to inspection in accordance with Section 100D of The Local Government Act 1972 - Nil.