

## External Auditor Appointment

### REPORT TO AUDIT AND STANDARDS COMMITTEE



<b>DATE</b>	11/01/2017
<b>PORTFOLIO</b>	Resources and Performance
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#### PURPOSE

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.
2. To seek a recommendation to Full Council in February for the approach to appointing an External Auditor for the 2018/19 Accounts.

#### RECOMMENDATION

3. Members are requested to consider their preferred approach of either:
  - a. Using the national Public Sector Auditor Appointments body to make the appointment on behalf of the Council.
  - b. Establishing a stand-alone Auditor Panel to make the appointment on behalf of the Council.
  - c. Commencing work on exploring the establishment of local joint procurement arrangements with neighbouring authorities
4. The recommended approach is 3a in that this would provide the greatest level of independence and value for money.

#### REASONS FOR RECOMMENDATION

5. Option 3a represents the better option for value for money and supports the independent appointment of an external auditor.
6. The Council has to make a decision to prepare for the appointment of external auditors for the 2018/19 accounts.

#### SUMMARY OF KEY POINTS

## **Changes in External Auditor Appointment**

7. The Local Audit and Accountability Act 2014 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.
8. The Council'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 we have benefited from reduction 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 £50,567 per annum for the work on the final accounts and approximately £10,000 for grant certification work.
9. 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 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.
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 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 commenced and so far these include the top accountancy firms in the country, including our current auditor. It is unlikely that small local independent firms will meet the eligibility criteria.

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

11. 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**

12. 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 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. (assuming there is no existing independent committee such as the Audit Committee that might already be suitably constituted).

### *Advantages/benefit*

13. 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*

14. 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
15. The Council will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts.
16. The assessment of bids and decision on awarding contracts will be taken by a majority of independent appointees and not solely by elected members.
17. Internal officer and member resources would be required to support this option.

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

18. 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*

19. The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities.
20. 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*

21. 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 Council, depending on the constitution agreed with the other bodies involved.
22. 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 chose 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**

23. 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. 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. The Secretary of State has

appointed PSAA (who currently manage the external auditor contracts) as a SLB.

#### *Advantages/benefits*

24. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities.
25. 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.
26. Any conflicts or independence issues at individual authorities would be managed by the SLB who would have a number of contracted firms to call upon.
27. The appointment process would not be ceded to locally appointed independent members. Instead a separate body has been set up to act in the collective interests of the 'opt-in' authorities.
28. There would be a lower internal resource requirement to support this option.
29. The PSAA are a not for profit organisation and distribute any surplus funds back to scheme members

#### *Disadvantages/risks*

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

#### **The way forward**

32. The Council have until December 2017 to make an external auditor 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.
33. The Council has received an invitation to opt in to the national scheme for auditor appointments. The Full Council will need to take this decision at its February meeting to enable a response to the invitation by 9 March 2017.

#### **Legal Issues**

34. 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.
35. 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.

36. 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 (SLB) to become the appointing person.
37. 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 Executive is asked to make the recommendation to Council.

## **FINANCIAL IMPLICATIONS AND BUDGET PROVISION**

38. External audit fee levels are likely to increase when the current contract ends in 2018.
39. 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 Council's budget for 2016/17 and 2017/18. This will 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.
40. 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. The costs of operating the SLB will be recovered as part of the auditor fees.
41. The actual costs will not be known for the audit fees in 2018/19 but it is anticipated that any increase will be minimised by going through the PSAA.

## **POLICY IMPLICATIONS**

42. Depending on the decision, the Council may need to make constitutional changes to appoint a local panel or joint panel.
43. The consideration of collective procurement is a requirement of the Council's Standing Orders for Contracts to avoid unnecessary costs and duplication.

## **DETAILS OF CONSULTATION**

44. None

## **BACKGROUND PAPERS**

45. PSAA Opting In details - <http://www.psa.co.uk/supporting-the-transition/appointing-person/becoming-an-opted-in-authority/>

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46. CIPFA Guide to Auditor Panels - <http://www.cipfa.org/policy-and-guidance/publications/g/guide-to-auditor-panels-pdf>

**FURTHER INFORMATION**

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