

## County Council

<b>Report Title:</b>	Arrangements for appointment of External Auditors
<b>Meeting Date:</b>	15 September 2016
<b>Lead Councillor(s):</b>	Cllr Richard Smith MVO
<b>Local Councillor(s):</b>	All
<b>Director:</b>	Geoff Dobson, Director of Resource Management
<b>Assistant Director or Head of Service:</b>	Geoff Dobson, Director of Resource Management
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### Brief summary of report

1. This report summarises 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. The Council will need to consider the options available and put in place new arrangements in time to make a first appointment by 31 December 2017.

### Action recommended

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| <ol style="list-style-type: none"> <li>3. (a) The Council to recognise the available arrangements for appointing External Auditors at the conclusion of the 2017/18 audit; and<br/><br/>           (b) to 'opt-in' to the Local Government Association(LGA) sector led body (Public Sector Audit Appointments Ltd (PSAA)) for the independent appointment of the Council's External Auditor, beginning with responsibilities for the financial year 2018/19.</li> </ol> |
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### Reason for recommendation

4. It is the Council's statutory responsibility to appoint an external auditor to audit its 2018/19 accounts by the 31 December 2017.

### Available options

5. The Council can choose one of the following options:
  - a) Establishing a stand-alone Auditor Panel to make the appointment on behalf of the Council;
  - b) Commencing work on exploring the establishment of local joint procurement arrangements with neighbouring authorities; or

- c) Using an existing independent panel of the Authority (there is no suitable constituted panel within SCC and therefore this option will not be covered further).

## **Who will be affected by this decision?**

6. All stakeholders.

## **Main body of report**

### **Background to the issue**

7. The Local Audit and Accountability Act 2014 abolished 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 for Communities and Local Government (CLG) determined that the transitional arrangements for local government bodies would be extended by one year to include the audit of the accounts for 2017/18.
8. The Council's current external auditor is Ernst & Young LLP; this appointment was 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 for CLG. Over recent years, the Council has benefited from a reduction in fees in the order of 50% compared with historic levels. This has been due to a combination of factors including new contracts negotiated nationally with the firms of accountants and savings from the closure of the Audit Commission. The Council's current external audit fee is £91k per annum.
9. When the current transitional arrangements end on 31 March 2018, the Council will move to the local appointment of its 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 not yet commenced but it is reasonable to expect that the list of eligible firms may include the top 10 or 12 firms in the country, including the Council's 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 Establish a stand-alone Auditor Panel to make the appointment**

12. 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 have a limited role in assessing bids and choosing which firm of accountants should be awarded the contract for the Council's external audit. This new independent Auditor Panel would be responsible for selecting the auditor. The existing Audit Committee could not carry out this role unless it were to meet the criterion of having a majority of independent members.

#### **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 would 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 decisions on awarding contracts would be taken by independent appointees and not solely by elected members.

### **Option 2 Explore the establishment of a Joint Auditor Panel/local joint procurement arrangements**

17. 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, and the Council will need to liaise with other local authorities to assess the appetite for such an arrangement.

#### **Advantages/benefits**

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

#### **Disadvantages/risks**

20. 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.
21. 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 selects a firm that is ineligible 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**

22. In response to the consultation on the new appointment arrangements, 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.

#### **Advantages/benefits**

23. The costs of setting up the appointment arrangements would be shared across all opt-in authorities
24. Being offered large contract values, the firms would be able to offer better rates and lower fees than are likely to result from local negotiation
25. Any conflicts at individual authorities would be managed by the SLB who would have a number of contracted firms to call upon.
26. The appointment process would not be ceded to locally appointed independent members. Instead a separate body is set up to act in the collective interests of the 'opt-in' authorities.

#### **Disadvantages/risks**

27. Individual elected members will have less opportunity for direct involvement in the appointment process other than through the LGA and/or stakeholder representative groups.
28. For the SLB to be workable 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**

29. The Council 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.
30. The LGA are working with the PSAA. The DCLG have recently approved the PSAA to become the Sector Led Body. In a recent survey, 58% of respondents expressed an interest in this option. Greatest economies of scale will come from the maximum number of councils acting collectively and opting-in to a SLB.
31. The Suffolk Councils' Section 151 officers and internal audit staff have already met with the LGA to discuss the advantages of the sector led approach. Collectively the officers recommend this approach.

#### **Risk Management**

32. There is no immediate risk to the Council. However, a swift decision by the Council on choosing an option would enable detailed planning to take place to achieve a successful transition to the new arrangement in a timely and efficient manner.

33. Providing the LGA of our likely way forward will enable the LGA to invest in developing appropriate arrangements to support the Council.

### **Legal implications**

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 to become the appointing person.

### **Financial Implications**

37. Current external fee levels are likely to increase when the current contracts end in 2018.
38. 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 if either of those options were chosen. 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.
39. Opting-in to a national SLB would provide maximum opportunity to limit the extent of any increases by entering in to a large scale collective procurement arrangement and would obviate the costs of establishing an independent auditor panel.

### **Conclusion**

40. The Council must, by the 31 December 2017, 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 Council is recommended to approve the sector led body arrangements for the appointment of its external auditor from April 2018.
41. The Council 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 Councils. The LGA is strongly supportive of the SLB approach as it believes this offers best value to Councils by reducing set-up costs and having the potential to negotiate lowest fees.

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