

FAREHAM

BOROUGH COUNCIL

Report to Council 15 December 2016

Subject: **New Arrangements for the Appointment of External Auditors
from April 2018**

Report of: **Director of Finance and Resources**

SUMMARY

This report sets out the proposals for appointing the external auditor to the Council for the 2018/19 accounts and beyond, as the current arrangements only cover up to and including 2017/18 audits. The auditors are currently working under a contract originally let by the Audit Commission. The contract was novated to Public Sector Audit Appointments (PSAA) following the closure of the Audit Commission in 2014.

This report was considered at the Audit and Governance Committee on 28 November 2016. The Committee recommends that Council accepts the invitation to 'opt in' to the sector led appointment of external auditors.

RECOMMENDATION

That Council accepts Public Sector Audit Appointments (PSAA) invitation to 'opt in' to the sector led option for the appointment of external auditors for five financial years commencing 1 April 2018.

INTRODUCTION

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 for the Department of Communities and Local Government (DCLG) 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. The Act also set out the arrangements for the appointment of auditors for subsequent years, with the opportunity for authorities to now make their own decisions about how and by whom their external auditors are appointed. Regulations made under the Act also allow authorities to 'opt in' to having their auditor appointed by an 'appointing person'.
3. This report sets out the options now available to the Council for the appointment of their next External Auditor.

OPT IN TO USING AN APPOINTING PERSON

4. In July 2016 Public Sector Audit Appointments (PSAA) were specified by the Secretary of State as an 'appointing person'. PSAA is an independent, not-for-profit company limited by guarantee and established by the Local Government Association (LGA). 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.
5. PSAA is now inviting 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 auditor.
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 though a smaller number of large contracts across the sector;

- The will be no need for the Council to establish alternative appointment processes locally, including the need to set up and manage an 'auditor panel', see below;
 - 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.
7. The Council's current external auditor is Ernst & Young, 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. Over recent years the Council has benefited from a 54% reduction in fees compared with fees in 2011/12. This has been the result of a combination of factors including new contracts negotiated nationally with the firms of accountants, changes in the scope of external audit work and savings from closure of the Audit Commission.
8. 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 providers.
9. 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.
10. 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.
11. 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;
 - 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 management costs and returning 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.

OTHER OPTIONS

12. If the Council did not opt in there would be a need to establish an independent auditor panel. In order to make a stand-alone appointment the auditor panel would need to be set up by the Council itself. The members of the panel must 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 will not have a majority input to assessing bids and choosing which audit firm to award a contract for the Council's external audit.
13. Alternatively 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 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 would need to liaise with other local authorities to assess the appetite for such an arrangement.
14. Neither of these options are recommended. Both these options would be more resource-intensive processes to implement and without the bulk buying power of the sector led procurement, would be likely to result in a more costly service.
15. It would also be more difficult to manage quality and independence requirements through a local appointment process.

THE WAY FORWARD

16. The formal invitation from PSAA is in appendix A.
17. The Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in must be made by Council. At its meeting on 28 November 2016, the Audit and Governance Committee agreed a formal recommendation to Council that the Council joins the national scheme for local auditor appointments via PSAA. The Council then needs to formally respond to PSAA's invitation in the form specified by PSAA by early March 2017.
18. PSAA will commence the procurement process after this date. It expects to award contracts in summer 2017 and consult with councils on the appointment of auditors so that it can make an appointment by the statutory deadline of December 2017.

FINANCIAL IMPLICATIONS

19. There is a risk that current external audit fees could increase when the current contracts end in 2018. The Council's current external fees are **£59,540** for 2016/17.
20. 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.
21. 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.

RISK ASSESSMENT

22. 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 let approach through PSAA.

Appendices:

Appendix A: Invitation to opt into the national scheme for auditor appointments

Contact: For further information on this report please contact Caroline Hancock. (Ext 4589)