

Appointment of External Auditors

Report by Head of Internal Audit (Internal Audit Consortium Manager)

Summary: This report outlines the Local Audit and Accountability Act (2014) and the necessity for local authorities to establish an auditor panel and manage their own procurement. The report explores the options available, the associated benefits, and concludes with a preferred route for the authority for the appointment of the External Auditor.

Recommendations:

- (i) That the Financial Scrutiny and Audit Committee recommend to the Full Authority, that the authority agrees to join the national collective scheme, led by the Public Sector Audit Appointment (PSAA).
- (ii) That delegated authority be given to the Section 17 Officer to communicate the willingness of the authority to join the scheme to PSAA and to enter into the scheme after a satisfactory examination / negotiation of the proposed terms and conditions is concluded.

1 Introduction

- 1.1 The Local Audit and Accountability Act 2014 (the Act) introduced the necessity for local authorities to establish an auditor panel and manage their own procurement.
- 1.2 Therefore all local authorities will need to decide how their auditors will be appointed in the future, whether they make the appointment themselves, or in conjunction with other bodies, or join a national collective scheme.
- 1.3 The current audit contracts are administered by Public Sector Audit Appointments (PSAA), which is a not-for-profit organisation established by the Local Government Association (LGA). These powers are time limited and will cease when these contracts with audit firms expire with the completion of the 2017/18 audits.
- 1.4 Thereafter the Authority will need to have exercised a choice about whether to opt in to the authorised national scheme, or whether to make arrangements to appoint their own auditors.
- 1.5 The LGA has played a leadership role in anticipating the changes and influencing the range of options available to local bodies. In particular it had lobbied to ensure that, irrespective of size, scale, responsibility or location,

local government bodies can, if they wish, subscribe to a specially authorised national scheme which will take full responsibility for local auditor appointments which offer a high quality professional service and value for money.

- 1.6 PSAA is leading the development of this national option and ideally are looking for principal bodies to give firm commitment to join during autumn 2016.
- 1.7 High quality independent audit is one of the cornerstones of public accountability, it gives assurance that taxpayers' money has been well managed and properly expended. It helps inspire trust and confidence in the organisations and people responsible for managing public money.

2 Options

- 2.1 The Authority can appoint auditors directly but this is not recommended as it would be costly to run our own procurement exercise, and being an individual authority we would be unlikely to benefit from economies of scale and achieve a competitive price. In addition an auditor panel would need to be set up to undertake the functions as set out in the Act.
- 2.2 Auditors can be appointed in conjunction with other local authorities. This was initially explored with Norfolk County Council leading on a potential County-wide procurement exercise. However again this is not recommended as it would incur procurement costs for the authorities involved and would also mean each authority would need to manage and monitor the performance of the contract that was entered into. Again an auditor panel would need to be set up.
- 2.3 To avoid prohibitive costs and ensure a sound contractual framework is in place for the assessment of auditors it is recommended that the Authority join the national collective scheme, subject to the applicable terms and conditions being acceptable to the Authority.
- 2.4 To do nothing is not recommended as this would contravene the Act.

3 Expected Benefits

- 3.1 Auditors must be independent of the bodies they audit, to enable them to carry out their work with objectivity and credibility, and in a way which commands public confidence. PSAA will ensure that every auditor appointment passes this test.
- 3.2 The scheme will endeavor to appoint the same auditor to bodies which are involved in formal collaboration / joint working initiatives or within combined authority areas thereby avoiding duplication or effort wherever possible.
- 3.3 PSAA will only contract with firms which have a proved track record in undertaking public audit work. In accordance with the Act the firms must be

registered with one of the chartered accountancy institutes acting in the capacity of a Recognised Supervisory Body (RSB), and the quality of the work will be subject to scrutiny by both the RSB and the Financial Reporting Council (FRC).

4 Reasons for Chosen option / Recommendation

- 4.1 A top priority for PSAA is to seek to obtain the best possible price; the current thinking is that this can be achieved by letting a three year contract, with the option to extend to five years, to a relatively small number of appropriately registered firms in two or three large contracts nationally. By having contracts with a number of firms PSAA will be able to ensure independence and avoid dominance of the market by one or two firms.
- 4.2 The procurement strategy will prioritise the importance of demonstrably independent appointments, in terms of both the audit firm appointed to each audited body and the procurement and appointment processes used.
- 4.3 PSAA will ensure that fee levels are carefully managed by securing competitive prices from firms and by minimising PSAA's own cost. PSAA will pool scheme costs and charge fees to audited bodies in accordance with a fair scale of fees which has regard to size, complexity and audit risk. Pooling therefore means that everyone within the scheme will benefit from the most competitive prices (current fees are set on this basis).

5 Conclusion

- 5.1 Due to the expected benefits, as outlined in the report, the authority should agree to join a national collective scheme for the appointment of the External Auditors.

Background papers: PSAA Corporate Plan 2015-2018

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Broads Plan Objectives: None

Appendices: APPENDIX 1 - Objectives of PSAA

**Full Council
19 September 2016**

Agenda Item No

Appointment of External Auditors

**Report of the Internal Audit Consortium Manager
Cabinet Member: Cllr Edney**

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1. Introduction

- 1.1 This report outlines the Local Audit and Accountability Act (2014) and the necessity for Local Authorities to establish an auditor panel and manage their own procurement. The report explores the options available, the associated benefits, and concludes with a preferred route for the Council for the appointment of the External Auditor.
- 1.2 The report was emailed, in August 2016, to Members of the Finance, Resources, Audit and Government Committee who were in favour of the recommendations.

2. Background

- 2.1 The Local Audit and Accountability Act 2014 (the Act) introduced the necessity for local authorities to establish an auditor panel and manage their own procurement.
- 2.2 Therefore all local authorities will need to decide how their auditors will be appointed in the future, whether they make the appointment themselves, or in conjunction with other bodies, or join a national collective scheme.
- 2.3 The Local Government Association (LGA) has played a leadership role in anticipating the changes and influencing the range of options available to local bodies. In particular, it has lobbied to ensure that, irrespective of size, scale, responsibility or location, local government bodies can if they wish, subscribe to a specially authorised national scheme which will take full responsibility for local auditor appointments which offer a high quality professional service and value for money.
- 2.4 Public Sector Audit Appointments Limited (PSAA), which is a not-for-profit company established by the LGA is leading the development of this national option and ideally is looking for principal bodies to give firm commitment to join the scheme during Autumn 2016.
- 2.5 High quality independent audit is one of the cornerstones of public accountability, it gives assurance that taxpayers' money has been well managed and properly expended. It helps inspire trust and confidence in the organisations and people responsible for managing public money.

3. Current Position/Findings

- 3.1** The current audit contracts are administered by PSAA. These powers are time limited and will cease when these contracts with audit firms expire with the completion of the 2017/18 audits for local government bodies.
- 3.2** Thereafter the Council will need to have exercised a choice about whether to opt in to the authorised national scheme, or whether to make other arrangements to appoint their own auditors.
- 3.3** The first option, for the Council to appoint auditors directly is not recommended as it would be costly to run our own procurement exercise, and being an individual Authority we would be unlikely to benefit from economies of scale and achieve a competitive price. In addition an auditor panel would need to be set up to undertake the functions as set out in the Act.
- 3.4** Secondly auditors could be appointed in conjunction with other local authorities. This was initially explored with Norfolk County Council leading on a potential County-wide procurement exercise. However again this is not recommended as it would incur procurement costs for the authorities involved and would also mean each Authority would then need to manage and monitor the performance of the contract that was entered into. Again an auditor panel would need to be set up.
- 3.5** The third option is for the Council to join the National Scheme proposed by the PSAA.
- 3.6** To do nothing is not recommended as it would contravene the Act.

4. Proposals

- 4.1** To avoid prohibitive costs and ensure that a sound contractual framework is in place for assessment of Auditors, it is recommended that the Council joins the National Scheme, subject to applicable terms and conditions being acceptable to the Council and within the Constitution.

Reasons for proposal

- 4.2** A top priority for PSAA is to seek to obtain the best possible price; the current thinking is that this can be achieved by letting a three year contract, with the option to extend to five years, to a relatively small number of appropriately registered firms in two or three large contract areas nationally. By having contracts with a number of firms, PSAA will be able to ensure independence and avoid dominance of the market by one or two firms.
- 4.3** The procurement strategy will prioritise the importance of demonstrably independent appointments, in terms of both the audit firm appointed to each audited body and the procurement and appointment processes used.
- 4.4** PSAA will ensure that fee levels are carefully managed by securing competitive prices from firms and by minimising PSAA's own costs. PSAA will pool scheme costs and charge fees to audited bodies in accordance with a fair scale of fees which has regard to size, complexity and audit risk. Pooling therefore means that everyone within the scheme will benefit from the most competitive prices (current fees are set on this basis).

Expected Benefits

- 4.5** Auditors must be independent of the bodies they audit, to enable them to carry out their work with objectivity and credibility, and in a way that commands public confidence. PSAA will ensure that every auditor appointment process passes this test and the Committee will be informed of the parameters used in this assessment.
- 4.6** The scheme will endeavour to appoint the same auditors to bodies which are involved in a formal collaboration / joint working initiatives or within combined authority areas, thereby avoiding duplication of effort wherever possible.
- 4.7** PSAA will only contract with firms which have a proven track record in undertaking public audit work. In accordance with the Act firms must be registered with one of the chartered accountancy institutes acting in the capacity of a Recognised Supervisory Body (RSB) and the quality of the audit work will be subject to scrutiny by both the RSB and the Financial Reporting Council (FRC).
- 4.8** Opting in to the appointing person arrangement will remove the need to set up an auditor panel. This is set out in the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015.

5. Risks and implications arising

- 5.1** Constitution and Legal – In Part 3 – Rules of Procedure, of the Constitution, the Finance, Resources, Audit and Governance Committee specifically reviews, and makes recommendations to Cabinet where appropriate, on the following external audit matters:

The external auditors report on the statement of accounts, and the external auditors annual plans.

- 5.2** Contracts – the current contract is with Ernst Young and this will expire after the end of the 2017/18 Audit.
- 5.3** Financial – Scale fees are currently set by PSAA and the fee for 2015/16 audit of the accounts is proposed to be £50,949, the final actual fee will exceed the scale fee set by the PSAA due to the additional work on group accounts, which are included in the financial statements for the first time in 2015/16.
- 5.4** Risk Management – The national framework will be subject to scrutiny at all levels to ensure that it is acceptable to the Council and all other Authorities who choose to enter into the scheme. This will ensure that the appropriate level of competence for Auditors is assured.

In the event that there are onerous terms and conditions in the National Framework these will be reported back to the Committee before any decision by the Section 151 Officer is taken in respect of joining the scheme.

6. Recommendation

- 6.1** That South Norfolk Council agrees to join a national collective scheme for the appointment of the Auditors, led by the Public Sector Audit Appointments (PSAA).
- 6.2** That delegated authority be given to the Section 151 Officer to communicate the willingness of the Council to join the scheme to PSAA and to enter into the scheme after satisfactory examination / negotiation of the proposed terms and conditions is concluded.

Appendix A – Objectives of PSAA

Background Papers:

PSAA Corporate Plan 2015-18 (available from Internal Audit Consortium Manager)

Local Audit and Accountability Act 2014 - <http://www.legislation.gov.uk/ukpga/2014/2/contents/enacted/data.htm>

The Local Audit (Appointing Persons) Regulations 2015 - <http://www.legislation.gov.uk/uksi/2015/192/body/made>