



<u>Committee and Date</u>
Council
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<u>Item</u>
<b>18</b>
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## **CHANGES TO ARRANGEMENTS FOR APPOINTMENT OF EXTERNAL AUDITORS**

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### **1. Summary**

On the 21<sup>st</sup> July 2016, Council agreed with the Audit Committee's proposal that Shropshire Council support the Local Government Association (LGA) in setting up a National Sector Led Body to appoint external auditors. This report, with support from the Audit Committee, now seeks a formal decision from Council to "opt-in" to the Public Sector Audit Appointments Ltd (PSAA) national auditor appointment arrangements. The Council can elect to remain in the appointment arrangements for a period of five years, commencing 1 April 2018. The form of notice to PSAA Ltd, following the decision, is to be received by the 9<sup>th</sup> March 2017.

### **2. Recommendations**

#### **Council**

Members are requested to formally opt-in to the Public Sector Audit Appointments Ltd (PSAA), Local Government Association National Sector Led Body.

## **REPORT**

### **3. Risk Assessment and Opportunities Appraisal**

- 3.1 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 the requirement for the authority to 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.

- 3.2 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.
- 3.3 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 applied 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.
- 3.4 The Secretary of State has enabled PSAA Ltd to be an appointing person for local auditors under a national scheme.
- 3.5 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998. There are no direct environmental, equalities, consultation or climate change consequences of this proposal.

#### **4. Financial Implications**

- 4.1 Existing external fee levels are likely to increase when the current contracts end in 2018. The Council's annual external audit fees for the 2015/16 audit were £133,845.
- 4.2 Opting-in to a national Sector Led Body (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. There will not be a fee to join the sector led arrangements. The audit fees that opted-in bodies will be charged by the sector led body will cover the costs of appointing auditors. The LGA believes that audit fees achieved through block contracts will be lower than the costs that individual authorities would be able to negotiate. In addition, by using the SLB, councils will avoid having to undertake their own procurement and the legal requirement to set up a panel of independent members.
- 4.3 PSAA Ltd commit to ensure that fee levels are carefully managed by securing competitive prices from firms and by minimising their own costs. Any surplus funds will be returned to scheme members under the articles of association and memorandum of understanding with the Department for Communities and Local Government and the LGA.
- 4.4 PSAA Ltd expect annual operating costs to be lower than current costs because they expect to employ a smaller team to manage the scheme. They are intending to fund an element of the costs of establishing the scheme, including the costs of procuring audit contracts, from local government's share of their current deferred income. This is considered appropriate because the new scheme will be available to all relevant principal local government bodies.
- 4.5 Contracts are likely to be awarded at the end of June 2017 and, at this point, the overall cost and therefore the level of fees required will be clear. They will consult on the proposed scale of fees in autumn 2017 and publish the fees applicable for 2018/19 in March 2018.

## **5. Background**

- 5.1 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.
- 5.2 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 the Council has 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 accountancy firms and savings from closure of the Audit Commission.
- 5.3 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. Audit Committee members considered the possibilities in June 2016 and recommended to, and were supported by, Council in July 2016 when they agreed to show initial interest to opt-in to a sector led body (SLB) if established. PSAA Ltd has now been appointed by the Secretary of State under the Act to be that SLB with 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.

## **6 Information on the national scheme**

- 6.1 The Council have until December 2017 to make an auditor appointment. PSAA Ltd have written to the Council confirming that the Secretary of State has awarded them the role of appointing local auditors under a national scheme.
- 6.2 PSAA Ltd have set out their proposed scheme, further details of which can be found at: <http://www.psaa.co.uk/supporting-the-transition/appointing-person/>. As part of the scheme, and under their timetable for appointing auditors, they are now formally inviting the Council to decide if it wants to join the national scheme. PSAA Ltd need to receive formal acceptance by 9 March 2017 and the decision to accept the invitation and to opt-in needs to be made by full Council.
- 6.3 The scheme is intended to save time and resources for local government bodies and, through collective procurement, secure the best prices without compromising on audit quality.
- 6.4 Given their current role PSAA Ltd feel they have a unique experience and understanding of auditor procurement and the local public market. Using the scheme will avoid the need for the Council to:
- establish an audit panel with independent members;
  - manage its own auditor procurement and cover its costs;

- monitor the independence of its appointed auditor for the duration of the appointment;
- deal with the replacement of any auditor and
- manage the contract with the auditor.

6.5 The scheme will endeavour to appoint the same auditors to other opted-in bodies that are involved in formal collaboration with the Council or joint working initiatives, if it is considered that a common auditor will enhance efficiency and value for money. PSAA Ltd will also try to be flexible about changing the Council's auditor during the five-year appointing period if there is good reason, for example where new joint working arrangements are put in place.

6.6 PSAA Ltd are looking to secure a high level of acceptance to the opt-in invitation to provide the best opportunity for the company to achieve the most competitive prices from audit firms. The LGA has previously sought expressions of interest in the appointing person arrangements, and received positive responses from over 270 relevant authorities, of which Shropshire Council was one. They hope to achieve participation from the majority of eligible authorities.

### **High quality audits**

6.7 The Local Audit and Accountability Act 2014 provides that firms must be registered as local public auditors with one of the chartered accountancy institutes acting in the capacity of a Recognised Supervisory Body (RSB). The quality of registered firms' work will be subject to scrutiny by both the RSB and the Financial Reporting Council (FRC), under arrangements set out in the Act.

6.8 PSAA Ltd will:

- only contract with audit firms that have a proven track record in undertaking public audit work;
- include obligations in relation to maintaining and continuously improving quality in the Council's contract terms and in the quality criteria of the tender evaluation;
- ensure that firms maintain the appropriate registration and will liaise closely with RSBs and the FRC to ensure that any quality concerns are detected at an early stage; and
- take a close interest in any feedback and in the rigour and effectiveness of firms' own quality assurance arrangements.

6.9 They will also liaise with the National Audit Office to help ensure that guidance to auditors is updated as necessary.

### **Procurement strategy**

6.10 In developing their procurement strategy for the contracts with audit firms, PSAA Ltd will have input from their established advisory panel. The panel will assist the company in developing arrangements for the national scheme, provide feedback on proposals as they develop, and help maintain effective channels of communication. PSAA Ltd are keen to understand the Council's preferences and priorities, to ensure they develop a strategy that reflects needs within the constraints set out in legislation and in professional requirements.

- 6.11 In order to secure the best prices PSAA Ltd are minded to let audit contracts:
- for five years;
  - in two large contract areas nationally, with three or four contract lots per area, depending on the number of bodies that opt-in; and
  - to a number of firms in each contract area to help them manage independence issues.
- 6.12 The value of each contract will depend on the prices bid, with the firms offering the best value being awarded larger amounts of work. By having contracts with a number of firms, PSAA Ltd will be able to manage issues of independence and avoid dominance of the market by one or two firms. Limiting the national volume of work available to any one firm will encourage competition and ensure the plurality of provision.

### **Auditor appointments and independence**

- 6.13 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.
- 6.14 PSAA Ltd plan to take great care to ensure that every auditor appointment passes this test. They will also monitor significant proposals for auditors to carry out consultancy or other non-audit work, to protect the independence of auditor appointments.
- 6.15 They will consult the Council on the appointment of its auditor, most likely from September 2017. To make the most effective allocation of appointments, it will help them to tell them about:
- any potential constraints on the appointment of the auditor because of a lack of independence, for example as a result of consultancy work awarded to a particular firm;
  - any joint working or collaboration arrangements that should influence the appointment; and
  - other local factors that are relevant to making the appointment.
- 6.16 The PSAA Ltd will ask for this information if the Council choose to opt-in.
- 6.17 Auditor appointments for the audit of the accounts of the 2018/19 financial year must be made by 31 December 2017.

### **Opting in**

- 6.18 The closing date for opting in is 9 March 2017. PSAA Ltd have allowed more than the minimum eight week notice period, because the formal approval process for most eligible bodies, except police and crime commissioners, requires a decision made by the members of an authority meeting as a whole, i.e. Full Council.
- 6.19 PSAA Ltd will confirm receipt of all opt-in notices, and will publish a list of authorities on their website. On receipt of an opt-in notice they will write to request information on any joint working arrangements relevant to the auditor appointment, and any potential independence matters that would prevent them appointing a particular firm.

6.20 If it is decided not to accept the invitation to opt-in by the closing date, a late request can be submitted *after* 1 April 2018. If the Council choose to do this, the first accounts which could be audited by a PSAA appointed auditor would be the 2019/20 accounts. PSAA Ltd are required to consider such requests, and agree to them unless there are reasonable grounds for their refusal.

**Timetable**

6.21 The timetable for the new arrangements is:

Invitation to opt-in issued	27 October 2016
Closing date for receipt of notices to opt-in	9 March 2017
Contract notice published	20 February 2017
Award audit contracts	By end of June 2017
Consult on and make auditor appointments	By end of December 2017
Consult on and publish scale fees	By end of March 2018

6.22 The Council has been asked by the LGA to opt-in to the national scheme for auditor appointments. Audit Committee endorse this approach to Council following their meeting on the 24<sup>th</sup> November 2016.

**List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)**

Local Audit and Accountability Act 2014  
 CIPFA’s Auditor Panels  
 Audit Committee, June 2016: Audit appointments 201718  
 Council, July 2016: Changes to Arrangements for Appointment of External Auditors  
 Audit Committee, November 2016: Audit appointments 201718

**Cabinet Member (Portfolio Holder)** Malcolm Pate (Leader of the Council) and Tim Barker (Chairman of Audit Committee)

**Local Member** n/a

**Appendices**  
 None