

REPORT FOR: Governance, Audit, Risk Management & Standards Committee

Date of Meeting: 06 December 2016

Subject: **INFORMATION REPORT** – Changes to arrangements for appointment of External Auditors

Responsible Officer: Dawn Calvert - Director of Finance

Exempt: No

Wards affected: All

Enclosures: Appendix 1- PSAA Prospectus
Appendix 2 - Invitation to opt in to the National Scheme for Auditor Appointments

Section 1 – Summary

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. The Council is required to consider the options available and put in place new arrangements in time to make a first appointment by 31 December 2017.

The formal approval process is a decision made by the members of an authority meeting as a whole. The closing date for opting in is 9 March 2017 and the decision will be considered by Council on 23 February 2017.

FOR INFORMATION

Section 2 – Report

Background

- 2.1 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 for 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. The Act also provides for the appointment by the secretary of state of a 'sector led body' to be an appointing person. This body would provide the option of a managed appointment process for those who wished to select it. Public Sector Audit Appointments Ltd (PSAA) has now been approved by the DCLG to be a sector led body for principal authorities – councils, police and fire bodies.
- 2.2 Under Regulation 19 of the Local Audit (Appointing Person) Regulations 2015, a decision for the Council to join the sector led approach must be made by Full Council and cannot be delegated.
- 2.3 The Council have 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.
- 2.4 Following the appointment of PSAA in July 2016 they issued a prospectus about the scheme (Appendix 1) and sent an invitation to opt in to the national scheme for auditor appointments on 27th October 2016 (Appendix 2). The Regulations specify a minimum period of eight weeks for invitation for Councils to accept the invitation to opt into the Sector Led Body arrangement being run by PSAA once the formal invitation has been received. However the PSAA has allowed more than the minimum eight week notice period because the formal approval process is a decision made by the members of an authority meeting as a whole. The closing date for opting in is 9 March 2017 and the decision will go to Council 23 February 2017.

Current situation

- 2.5 The Council's current external auditor is KPMG, who were appointed under a contract let by the Audit Commission in 2014/15. Following closure of the Audit Commission the contract is currently managed by PSAA, the transitional body set up by the Local Government Association (LGA) with delegated authority from the Secretary of State for 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 for the accounts, including the Pension Fund, are £199,459 per annum.

Why a change is needed

- 2.6 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 for a period of up to five years. 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.
- 2.7 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 Local Audit Register maintained by the Institute for Charter Accountants (England and Wales) currently contains nine firms, including our current auditor.

Main options

- 2.8 There are three broad options open to the Council under the Local Audit and Accountability Act 2014 (the Act) which are set out below, along with consideration of the advantages and risks for each option:

Option 1: Make a stand-alone appointment

- 2.9 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 would need to be established by the Council, in addition to the GARMS Committee. The Panel would be responsible for selecting the auditor and recommending their appointment to Full Council.

Advantages/benefits

- 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

- 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.
- The Council will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts.
- The assessment of bids and decision on awarding contracts will be taken by independent appointees and not solely by elected members.

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

2.10 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 (non-elected 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 will need to liaise with other local authorities to assess the appetite for such an arrangement.

Advantages/benefits

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

- 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.
- 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 choose 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 (SLB)

2.11 To follow a sector led approach by which an ‘appointing person’ operates a nationwide, EU compliant procurement and appoints on the Council’s behalf, maximising the opportunities for the most economic and efficient approach to procurement of external audit on behalf of the whole sector. PSAA was confirmed as an appointing person by the Secretary of State in July 2016. PSAA is a subsidiary of the Improvement and Development Agency (IDeA) which is wholly owned by the LGA.

Advantages/benefits

- The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities.
- 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.
- Any conflicts at individual authorities would be managed by the SLB who would have a number of contracted firms to call upon.
- Opting into the appointing person scheme removes the need to set up a separate independent auditor panel, comprising a majority of independent (non-elected) members.

Disadvantages/risks

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

Preferred option

2.12 Officers recommend Option 3, the sector led approach, as the most appropriate option for the Council to follow for the reasons set out above. The recommendation will be made to Council on 23 February 2017 to approve a sector led approach and opt in to appointing person arrangements.

Section 3

Financial Implications

3.1 Current external audit fees levels are likely to increase when the current contracts end in 2018.

- 3.2 The cost of establishing a local or joint Auditor Panel outlined in options 1 and 2 above have not been included in the Council's budget for 2016/17 and would need to be estimated and included in the Council's budget for 2017/18 if either of these options were recommended to Council. This would include the cost of recruiting independent appointees (members), servicing the independent Panel, running a bidding and tender evaluation process, letting a contract and paying independent members fees and allowances.
- 3.3 Opting-in to a national 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 independent auditor panel.

Risk Management Implications

- 3.4 There is no immediate risk to the Council, however, early consideration by the Council of its preferred approach will enable detailed planning to take place so as to achieve successful transition to the new arrangement in a timely and efficient manner.
- 3.5 Opting in to the PSAA arrangement, which indications suggest is the approach likely to be taken by most local authorities, will enable the PSAA to obtain greatest economies of scale through competition and to invest in developing appropriate arrangements to support the Council through the management of these contracts and future procurement of contracts when they are due for renewal.
- Risk included on Directorate risk register? ~~Yes~~/No
 - Separate risk register in place? ~~Yes~~/No

Equalities implications

- 3.6 Was an Equality Impact Assessment carried out? ~~Yes~~/No – not applicable.

Legal Implications

- 3.7 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 9 sets out the requirement to have an auditor panel. Paragraph 1(1) of Schedule 3 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.

- 3.8 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.
- 3.9 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. The Regulations also make certain modifications to the Act to dis-apply or modify the provisions of the Act in relation to opted in authorities, including that the requirement to have an auditor panel does not apply to such an authority and similarly that the authority does not have to consult and take into account the advice of the auditor panel.

Council Priorities

- 3.10 The work of the External Auditor's helps the Council to achieve its vision and priorities.

The Council's vision:

Working Together to Make a Difference for Harrow

- Making a difference for the vulnerable
- Making a difference for communities
- Making a difference for local businesses
- Making a difference for families

Section 3 - Statutory Officer Clearance

Name: Dawn Calvert	<input checked="" type="checkbox"/>	Chief Financial Officer
Date: 24/11/16		
Name: Caroline Eccles...	<input checked="" type="checkbox"/>	on behalf of the* Monitoring Officer
Date: 24/11/16		

Ward Councillors notified:	YES/ NO
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Section 4 - Contact Details and Background Papers

Contact: Susan Dixson, Head of Internal Audit, 0208 424 1420

Background Papers: None

If appropriate, does the report include the following considerations?

1.	Consultation	YES / NO
2.	Priorities	YES / NO