

PUBLIC SECTOR AUDIT APPOINTMENTS

Executive Summary

The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 accounts. The Council opted into the national auditor appointment arrangements established by Public Sector Audit Appointments (PSAA) for the period covering the accounts for 2018/19 to 2022/23 and following the procurement BDO LLP were appointed.

PSAA is now undertaking a procurement for the next appointing period, covering audits for 2023/24 to 2027/28. All local government bodies need to consider whether to arrange their own procurement, work in conjunction with other bodies, or join the national scheme administered by PSAA.

Whilst there have been issues with the audit service under the current contract, a local procurement would not address the sector wide challenges. Opting into a sector-wide procurement conducted by PSAA has a number of benefits to the Council.

- Reduction in the procurement costs which would be incurred if the Council managed its own process;
- Outside the national arrangements the Council would need to establish its own auditor panel with an independent chair and independent members to oversee a local auditor procurement and ongoing management of an audit contract; and
- It is the best opportunity to secure the appointment of a qualified, registered auditor - there are only nine accredited local audit firms, and a local procurement would be drawing from the same limited supply of auditor resources as PSAA's national procurement.

Under the local audit regulations a decision of full Council is required to opt into the national auditor appointment arrangements. The opt-in period starts on 22 September 2021 and closes on 11 March 2022. To opt into the national scheme from 2023/24, the Council needs to return completed opt-in documents to PSAA by 11 March 2022.

Recommendations

The Committee is requested to:

RECOMMEND TO COUNCIL That the Council opts into the sector-led appointment of external auditors by Public Sector Audit Appointments (PSAA) for five financial years from 1 April 2023.

The item(s) above will need to be dealt with by way of a recommendation to Council.

Background Papers: None.

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1.0 Introduction

- 1.1 The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 accounts. The Council opted into the national auditor appointment arrangements established by Public Sector Audit Appointments (PSAA) for the period covering the accounts for 2018/19 to 2022/23 and following the procurement BDO LLP were appointed.
- 1.2 PSAA is now undertaking a procurement for the next appointing period, covering audits for 2023/24 to 2027/28. All local government bodies need to consider whether to arrange their own procurement, work in conjunction with other bodies, or join the national scheme administered by PSAA.
- 1.3 Under the local audit regulations a decision of full Council is required to opt into the national auditor appointment arrangements. The opt-in period starts on 22 September 2021 and closes on 11 March 2022. To opt into the national scheme from 2023/24, the Council needs to return completed opt-in documents to PSAA by 11 March 2022.

2.0 Procurement of External Audit for the period 2023/24 to 2027/28

- 2.1 Under the Local Government Audit & Accountability Act 2014 ("the Act"), the council is required to appoint an auditor to audit its accounts for each financial year. The council has three options;
 - To appoint its own auditor, which requires it to follow the procedure set out in the Act.
 - To act jointly with other authorities to procure an auditor following the procedures in the Act.
 - To opt in to the national auditor appointment scheme administered by a body designated by the Secretary of State as the 'appointing person'. The body currently designated for this role is Public Sector Audit Appointments Limited (PSAA).
- 2.2 In order to opt in to the national scheme, a council must make a decision at a meeting of the Full Council.

3.0 The Appointed Auditor

- 3.1 The auditor appointed at the end of the procurement process will undertake the statutory audit of accounts and Best Value assessment of the council in each financial year, in accordance with all relevant codes of practice and guidance. The appointed auditor is also responsible for investigating questions raised by electors and has powers and responsibilities in relation to Public Interest Reports and statutory recommendations.
- 3.2 The auditor must act independently of the council and the main purpose of the procurement legislation is to ensure that the appointed auditor is sufficiently qualified and independent.
- 3.3 The auditor must be registered to undertake local audits by the Financial Reporting Council (FRC) and employ authorised Key Audit Partners to oversee the work. There is a currently a shortage of registered firms and Key Audit Partners.
- 3.4 Auditors are regulated by the FRC, which will be replaced by a new body with wider powers, the Audit, Reporting and Governance Authority (ARGA) during the course of the next audit contract.
- 3.5 Councils therefore have very limited influence over the nature of the audit services they are procuring, the nature and quality of which are determined or overseen by third parties.

4.0 Appointment by the Council itself or jointly

4.1 The Council may elect to appoint its own external auditor under the Act, which would require the council to;

- Establish an independent auditor panel to make a stand-alone appointment. The auditor panel would need to be set up by the Council itself, and 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, excluding 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 to which audit firm to award a contract for the Council's external audit.
- Manage the contract for its duration, overseen by the Auditor Panel.

4.2 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. Legal advice would be required on the exact constitution of such a panel having regard to the obligations of each Council under the Act.

5.0 The national auditor appointment scheme

5.1 PSAA is specified as the 'appointing person' for local government under the provisions of the Act and the Local Audit (Appointing Person) Regulations 2015. PSAA let five-year audit services contracts in 2017 for the first appointing period, covering audits of the accounts from 2018/19 to 2022/23. It is now undertaking the work needed to invite eligible bodies to opt in for the next appointing period, from the 2023/24 audit onwards, and to complete a procurement for audit services. PSAA is a not-for-profit organisation whose costs are around 4% of the scheme with any surplus distributed back to scheme members.

5.2 In summary the national opt-in scheme provides the following:

- the appointment of a suitably qualified audit firm to conduct audits for each of the five financial years commencing 1 April 2023;
- appointing the same auditor to other opted-in bodies that are involved in formal collaboration or joint working initiatives to the extent this is possible with other constraints;
- managing the procurement process to ensure both quality and price criteria are satisfied. PSAA has sought 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 during the appointment period;
- minimising the scheme management costs and returning any 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.

6.0 Pressures in the current local audit market and delays in issuing opinions

- 6.1 There have been many changes in the audit market since audit contracts were last awarded in 2017. At that time the audit market was relatively stable, there had been few changes in audit requirements, and local audit fees had been reducing over a long period. 98% of eligible bodies opted into the national scheme which attracted very competitive bids from audit firms. The resulting audit contracts took effect from 1 April 2018.
- 6.2 During 2018 a series of financial crises and failures in the private sector led to questioning about the role of auditors and the focus and value of their work. Four independent reviews were commissioned by Government: Sir John Kingman's review of the Financial Reporting Council (FRC), the audit regulator; the Competition and Markets Authority review of the audit market; Sir Donald Brydon's review of the quality and effectiveness of audit; and Sir Tony Redmond's review of local authority financial reporting and external audit.
- 6.3 The recommendations are now under consideration by Government, with the clear implication that significant reforms will follow. A new audit regulator (ARGA) is to be established, and arrangements for system leadership in local audit are to be introduced. Further change will follow as other recommendations are implemented.
- 6.4 The Kingman review led to an urgent drive for the FRC to deliver rapid, measurable improvements in audit quality. This has created a major pressure for audit firms to ensure full compliance with regulatory requirements and expectations in every audit they undertake.
- 6.5 In conducting 2018/19 local audits during 2019, the measures audit firms were putting in place to respond to a more focused regulator was apparent. To deliver the necessary improvements in audit quality, firms were requiring their audit teams to undertake additional work to gain deeper levels of assurance. This additional work required more time, posing a threat to the firms' ability to complete all their audits by the target date for publication of audited accounts. There were also many more fee variation claims than had been needed in prior years.
- 6.6 Auditor firms have also faced additional challenges through auditor recruitment and retention, the complexity of local government financial statements and increasing levels of technical challenges as authorities explore innovative ways of developing new or enhanced income streams to help fund services for residents. Further pressures have been experienced as a result of the Covid-19 pandemic.
- 6.7 Other sectors have experienced similar challenges, where there have been increased fees and disappointing responses to tender invitations during the past two years.

7.0 The PSAA process

- 7.1 PSAA is now inviting authorities to opt in for the second appointing period, for 2023/24 to 2027/28. Based on the numbers opting in, it will enter into contracts with appropriately qualified audit firms and appoint a suitable firm to be the Council's auditor. A copy of PSAA's invitation are provided in Appendix 1 to this report together with the PSAA prospectus and procurement strategy at Appendix 2 and 3.
- 7.2 The prices submitted by bidders through the procurement will be the key determinant of the value of audit fees paid by opted-in bodies. PSAA will:
 - seek to encourage realistic fee levels and to benefit from the economies of scale associated with procuring on behalf of a significant number of bodies;
 - pool scheme costs and charge fees to opted-in bodies in accordance with the published fee scale as amended following consultations with scheme members and other interested parties

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(pooling means that everyone within the scheme will benefit from the prices secured via a competitive procurement process);

- minimise its own costs, around 4% of scheme costs, and as a not-for-profit company will return any surplus funds to scheme members. In 2019 it returned a total £3.5m to relevant bodies and in 2021 a further £5.6m was returned.

7.3 PSAA will seek to encourage market sustainability in its procurement. Firms will be able to bid for a variety of differently sized contracts so that they can match their available resources and risk appetite to the contract for which they bid. They will be required to meet appropriate quality standards and to reflect realistic market prices in their tenders, informed by the scale fees and the supporting information provided about each audit. Where regulatory changes are in train which affect the amount of audit work suppliers must undertake, firms will be informed as to which developments should be priced into their bids.

7.4 The scope of a local audit is fixed. It is determined by the Code of Audit Practice, the format of the financial statements (specified by CIPFA/LASAAC) and the application of auditing standards regulated by the FRC. These factors apply to all local audits irrespective of whether an eligible body decides to opt into PSAA's national scheme or chooses to make its own separate arrangements. The requirements are mandatory; they shape the work auditors undertake and have a bearing on the actual fees required.

7.5 There are currently nine audit providers eligible to audit local authorities and other relevant bodies under local audit legislation. A local procurement exercise would seek tenders from the same firms as the national procurement exercise, subject to the need to manage any local independence issues. Local procurements must deliver the same audit scope and requirements as a national procurement, reflecting the auditor's statutory responsibilities.

8.0 Assessment of options

8.1 A local or joint procurement exercise would be more resource intensive processes to implement for the council and may result in a more costly service without the bulk buying power of the sector-led procurement.

8.2 The Council and its auditor panel would need to maintain ongoing oversight of the contract. Local contract management cannot, however, influence the scope or delivery of an audit. The council is unable to influence the scope of the audit and the regulatory regime inhibits the council's ability to affect quality.

8.3 The national offer provides the appointment of an independent auditor with limited administrative cost to the council. By joining the scheme, the council would be acting with other councils to optimise the opportunity to influence the market that a national procurement provides.

8.4 Whilst there have been many issues with the audit service the Council has received since 2018/19, it is unlikely that a local procurement would result in better outcomes. The Council would also not have the support of PSAA to enable a sector wide consistent approach is taken to contract management and fee variations. The recommended approach is therefore to again opt in to the national auditor appointment scheme.

9.0 The way forward

9.1 Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in must be made by a meeting of the Council.

9.2 The Council then needs to respond formally to PSAA's invitation in the form specified by PSAA, attached as an Appendix to this report, by the close of the opt-in period on 11 March 2022.

- 9.3 PSAA will commence the formal procurement process in early February 2022. It expects to award contracts in August 2022 and will then consult with authorities on the appointment of auditors so that it can make appointments by the statutory deadline of 31 December 2022.

10.0 Implications

Finance and Risk

- 10.1 The principal risks are that the Council fails to appoint an auditor in accordance with the requirements and timing specified in local audit legislation, or it does not achieve value for money in the appointment process.
- 10.2 The risks are considered best mitigated by opting into the sector-led approach through PSAA.
- 10.3 There is a risk that current external audit fee levels could increase when the current contracts end. It is clear that the scope of audit has increased, requiring more audit work. There are also concerns about capacity and sustainability in the local audit market.
- 10.4 Opting into a collective procurement through the national scheme provides maximum opportunity to ensure fees are as realistic as possible, while ensuring the quality of audit is maintained.
- 10.5 If the national scheme is not used some additional resource may be needed to establish an auditor panel and conduct a local procurement.
- 10.6 The audit fees charged by the PSAA will cover the costs of the PSAA appointing auditors and managing the arrangements. This avoids the costs of a procurement exercise just for the Council.
- 10.7 Until a procurement exercise is completed it is not possible to state what, if any, additional resource may be required for audit fees from 2023/24.

Equalities and Human Resources

- 10.8 There are no equalities or human resources implications.

Legal

- 10.9 Section 7 of the Local Audit and Accountability Act 2014 requires a relevant Council appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding year.
- 10.10 Section 8 governs the procedure for appointment including that the Council 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 Council is a local Council operating executive arrangements, the function of appointing a local auditor to audit its accounts is not the responsibility of an executive of the Council under those arrangements.
- 10.11 Section 12 makes provision for the failure to appoint a local auditor. The Council must immediately inform the Secretary of State, who may direct the Council to appoint the auditor named in the direction or appoint a local auditor on behalf of the Council.
- 10.12 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

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State the ability to enable a sector-led body to become the appointing person. In July 2016 the Secretary of State specified PSAA as the appointing person.

- 10.13 Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in to the national auditor appointment scheme must be made by Full Council (authority meeting as a whole). To comply with this regulation it is necessary for the Committee to make the recommendation to Council.

11.0 Conclusions

- 11.1 The sector led procurement of external auditors from 2023/24 offers the most efficient procurement solution and is most likely to achieve the best value for money for the Council.

REPORT ENDS