

Audit, Governance and Standards Committee

19 September
2016

Is the final decision on the recommendations in this report to be made at this meeting?

No

External Audit Procurement

Final Decision-Maker	Council
Lead Director	Director of Finance and Business Improvement
Lead Officer and Report Author	Director of Finance and Business Improvement
Classification	Public
Wards affected	All

This report makes the following recommendation to the final decision-maker:

1. That the Audit, Governance and Standards Committee notes the latest information on external audit procurement.
2. That the Committee recommends to Council that it adopt the option of outsourced procurement as set out at paragraph 3.9.

This report relates to the following corporate priorities:

- Keeping Maidstone Borough an attractive place for all
- Securing a successful economy for Maidstone Borough

Timetable

<i>Meeting</i>	<i>Date</i>
Audit, Governance and Standards Committee	19 September 2016
Council	7 December 2016

External Audit Procurement

1. PURPOSE OF REPORT AND EXECUTIVE SUMMARY

- 1.1 This reports sets out the Council's alternatives for the appointment of external auditors.
 - 1.2 The Council's current contract with its external auditor is due to expire at the end of 2017/18, and the Council will need to appoint a new auditor before 31 December 2017. The new auditor will take on responsibility for examining the 2018/19 financial statements and will deliver their first opinion in July 2019.
 - 1.3 This reports sets out the options open to the Council for routes to obtain a new auditor.
 - 1.4 The final decision about which route to take is to be made by full Council.
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2. INTRODUCTION AND BACKGROUND

- 2.1 From the creation of the original District Audit Service in 1844, originally as part of the Treasury, local authorities have always been allocated an external auditor. The role of the external auditor has varied over time but always retained a fundamental element of safeguarding public money by ensuring true and fair financial reporting. From 1983, local authorities had their external auditor selected on their behalf by the Audit Commission.
- 2.2 In 2010, the Secretary of State for Communities and Local Government in the newly formed Coalition Government set out the Government's intention to abolish the Audit Commission and move towards a position where local authorities were able to select their own external auditors.
- 2.3 This intention initially materialised in outsourcing the Audit Commission's in-house audit service to private providers in a competitive tender to the private sector. It was at this point - in 2012 - that most of Kent's external audit provision moved to Grant Thornton on a contract scheduled to expire with the 2016/7 financial statements audit but with a potential two year extension.
- 2.4 In the meantime, the Government made the necessary legislative changes to disband the Audit Commission and create the new external audit framework. This resulted in the Local Audit and Accountability Act 2014 (the Act) and various pieces of secondary legislation such as the Local Audit (Auditor Panel) Regulations 2014 and Local Audit (Appointing Persons) Regulations 2015 (the Regulations).
- 2.5 On 5 October 2015 the Government announced a decision to take one of the two year extensions written into the original 2012 contract. This fixed the date by which local authorities must have acted to appoint an auditor -

before 31 December 2017. The new auditor will take on responsibility for examining the 2018/19 financial statements and deliver their first opinion in July 2019.

- 2.6 The Act and the Regulations give every local authority a choice of three different routes to choosing its auditor. Note that the decision on which path to pursue must be made by full Council.
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3. AVAILABLE OPTIONS

- 3.1 Before considering the procurement alternatives it should be noted that suppliers must have permission from the Financial Conduct Authority (FCA) to provide public audit services. Currently the following suppliers provide public audit services in local authorities:
- BDO LLP (Currently auditing 39 authorities)
 - Ernst & Young LLP (232 authorities)
 - Grant Thornton UK LLP (265 authorities, including Maidstone Borough Council)
 - KPMG LLP (218 authorities)
 - Mazars LLP (40 authorities)
- 3.2 More providers may seek permission as decisions move closer. However, it is unlikely that small local independent firms will be able to meet the FCA's demands, so limiting the Council's choice of auditor.

Solo Procurement and Auditor Panels

- 3.3 The Council could opt to take the decision alone on procuring a new auditor. To do this the Council would have to establish an *Auditor Panel* as set out in the 2014 Regulations. The Panel must be independently chaired and contain a majority of independent members. Under the Regulations 'independent' means someone who is not a councillor or officer of the authority or employed by a prospective auditor and has not been so for at least five years. The member must also not be a relative or close friend of any serving councillor or officer.
- 3.4 Should it choose this route, the *Auditor Panel* could be entirely separate from the Council's committee structure or a sub-committee within its existing governance (for example a sub-committee of the audit committee). However, it must meet the composition requirements of the Regulations, including a majority of independent members and an independent chair.
- 3.5 An *Auditor Panel* is an advisory body only. It recommends actions to full Council but the Council is not bound to follow its recommendation.

3.6 Beyond the appointment of an auditor, the *Auditor Panel* should remain as a standing committee, as it has other functions, including:

- Reviewing the Council’s policy on obtaining non-audit services from the auditor,
- Maintaining an independent relationship to the auditor,
- Monitoring the quality and effectiveness of the auditor,
- Considering any investigation into the circumstances of an auditor’s resignation from office or any proposal to remove, and
- Receiving any Public Interest Reports published by the auditor.

3.7 Further details on *Auditor Panels* are included in CIPFA’s comprehensive guide produced with CLG and available for free download at <http://www.cipfa.org/policy-and-guidance/publications/g/guide-to-auditor-panels-pdf>.

Advantages/Benefits	Disadvantages/Risks
Maximum (though not complete) control over auditor procurement.	Costs of recruiting and maintaining an <i>Auditor Panel</i> .
Ability to shape auditor requirements to local circumstances	May struggle to recruit sufficient independent members.
	Unlikely to achieve economies of scale.

Joint Procurement

3.8 The Act allows bodies to establish a joint *Auditor Panel*. Alternatively authorities can decide to ask the *Auditor Panel* of another authority to advise them (a joint procurement, but not a joint *Panel*). Joint panels need not be restricted by geography or sector (for instance, a joint panel with Police or Fire authorities could meet the requirements). However, the *Auditor Panel* will still require a majority of independent members.

Advantages/Benefits	Disadvantages/Risks
Spreads the cost of procurement	Some loss of local control of process
Potentially easier to recruit independent members	May encounter complexities if participants have differing procurement aims.

Outsourced Procurement (the ‘Sector Led Body’)

3.9 A late addition to the Act as it progressed through Parliament, Section 17 allows the Secretary of State to authorise a *Specified Person* who would have the authority to make auditor appointment decisions on behalf of those authorities who opt-in to those arrangements. There is nothing in the Act or Regulations that limits the Secretary of State to authorise only

one *Specified Person*, nor any requirements that such *Persons* be public bodies or associations. The Secretary of State has not made any authorisation and so at this time no *Specified Person* exists. Authorities that choose to procure via a *Specified Person* do not need to create or maintain an *Auditor Panel*.

- 3.10 In this route, once full Council decides to opt-in, the *Specified Person* would negotiate contracts and make the appointment on behalf of councils. The *Specified Person* would also take on all of the existing tasks of an *Auditor Panel* on behalf of the opted-in councils.
- 3.11 Under the 2015 Regulations, the decision of full Council to opt-in (or not) following invitation by a *Specified Person* is final. The Council will not have the option of waiting to see what arrangements the Sector Led body is able to make with auditors, including prices, before deciding, nor can it leave the arrangement if it does not support the eventual appointment.
- 3.12 Public Sector Audit Appointments Ltd (PSAA) has issued a prospectus setting out its intention to seek designation as a *Specified Person*. This is attached as Appendix 1 to this report. PSAA is an independent, not-for-profit company limited by guarantee. It is established by the Local Government Association (LGA) and is therefore led by the local authority sector. It already carries out a number of functions in relation to auditor appointments under powers delegated by the Secretary of State for Communities & Local Government. PSAA is a not-for-profit company and it states that any surplus funds from running a local auditor appointment scheme would be returned to scheme members.
- 3.13 Given the sponsorship of the LGA, PSAA is a highly credible candidate to act as a *Specified Person*. Early indications are that many local authorities would opt in to a scheme run by PSAA. In a recent LGA survey more than 200 have expressed an interest in joining the scheme.
- 3.14 Further information is set out in a 'Frequently Asked Questions' document published by the PSAA and included as Appendix 2 to this report.
- 3.15 The benefits cited by the PSAA of joining their scheme include the following:
 - it will save time and resources for local authorities, as they will avoid the necessity to establish an auditor panel and the need to manage their own auditor procurement
 - assuming a high level of participation, PSAA will be able to attract the best audit suppliers and command highly competitive prices.

Advantages/Benefits	Disadvantages/Risks
Likely to deliver economies of	Loss of local control of process

scale.
No requirement to run procurement exercise or create <i>Auditor Panel</i>
Assured appointment from a nationally accredited panel of auditors
Surpluses from running scheme passed on to members

4. PREFERRED OPTION AND REASONS FOR RECOMMENDATIONS

- 4.1 No decision is required now; we present this report for information. The final decision on which route to take must be one of Full Council. This includes a decision, following invitation, on whether or not to opt into any arrangements proposed by a sector-led body.
- 4.2 At this stage we seek the views and comments of the Committee to assist Officers in engaging with the LGA (and any other bodies) and providing any further support to members ahead of taking the decision.

5. CONSULTATION RESULTS AND PREVIOUS COMMITTEE FEEDBACK

- 5.1 Various earlier stages of this discussion (which dates back to the original decision to seek abolition of the Audit Commission in August 2010) have occurred at this Committee and elsewhere but this is the first paper dedicated to the topic. As the situation develops, in particular once the situation is clear on the offer presented by a sector-led body, we will bring further information for members' consideration.

6. NEXT STEPS: COMMUNICATION AND IMPLEMENTATION OF THE DECISION

- 6.1 The next step will be preparation of a report to full Council, incorporating the comments of the Audit, Governance and Standards Committee, setting out the available options and making a recommendation as to which one to adopt.

7. CROSS-CUTTING ISSUES AND IMPLICATIONS

Issue	Implications	Sign-off
Impact on Corporate Priorities	Effective external audit procurement will help to ensure value for money and maintain good governance.	Director of Finance and Business Improvement
Risk Management	External audit	Head of Audit

	complements the Council's internal risk management processes	Partnership
Financial	The Council's external audit fee is currently £50,475. Effective procurement will help to ensure that the fee continues to provide value for money.	Director of Finance and Business Improvement
Staffing	None	
Legal	The Council will need to appoint a new auditor and have a suitable contract in place before 31 December 2017.	Team Leader – Contracts and Commissioning
Equality Impact Needs Assessment	No detrimental impact on the protected characteristics of individuals identified.	Equalities and Corporate Policy Officer
Environmental/Sustainable Development	None	
Community Safety	None	
Human Rights Act	None	
Procurement	Effective external audit procurement will help to ensure value for money.	Director of Finance and Business Improvement
Asset Management	None	

8. BACKGROUND PAPERS

None.