

External Audit Appointment 2023/24 to 2027/28

AUDIT COMMITTEE MEETING DATE 2021/22 5th January 2022	CLASSIFICATION: Open
WARD(S) AFFECTED All Wards	
Ian Williams, Group Director Finance and Corporate Resources	

1. INTRODUCTION AND BACKGROUND

- 1.1. The Local Audit and Accountability Act 2014 ('the Act') 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. Thereafter, local authorities would be responsible for appointing their own external auditors under the overall framework required by the Act.
- 1.2 The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 accounts. The Council opted into the 'appointing person' national auditor appointment arrangements established by Public Sector Audit Appointments (PSAA) for the period covering the accounts for 2018/19 to 2022/23 and as the Committee is aware the appointed auditor for that period is Mazars.
- 1.2 PSAA is now undertaking a procurement for the next appointing period, covering audits for 2023/24 to 2027/28. At this point all local government bodies need to make decisions about their external audit arrangements from 2023/24. They have options to arrange their own procurement and make the appointment themselves or in conjunction with other bodies, or they can join and take advantage of the national collective scheme administered by PSAA. If the Council wants to opt in to the PSAA arrangements a decision is required of Full Council and notification of that decision needs to be made to the PSAA by 11th March 2022.
- 1.3 This report sets out the evaluation undertaken by officers to establish the most appropriate arrangements for the Council with this regard and recommends that the Audit Committee make a recommendation to Full Council to opt in to the PSAA procurement process. It is noted that the Audit Committee and officers have expressed concern over the external audit arrangements and particularly the delays which have ensued over the past year and will review the potential for input into the PSAA process.

2. RECOMMENDATION

- 2.1 **That the Audit Committee considers the officers recommendation to accept the Public Sector Audit Appointments (PSAA) invitation to 'opt in' to the sector led option for the appointment of external auditors for five financial years commencing 1 April 2023 and propose that recommendation to Full Council.**
- 2.2 **Note that the Audit Committee's recommendation will be included in the Council's Annual Budget report to Full Council on 23rd February 2022.**
- 2.3 **The Audit Committee recommend to Council to delegate authority to the Group Director of Finance & Corporate Resources to respond to the invitation and take the necessary steps to finalise the appointment itself following the PSAA procurement process.**

3. BACKGROUND

3.1 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).

In order to opt in to the national scheme, a council must make a decision at a meeting of the Full Council.

3.2 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.

3.3 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.

3.4 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. 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.

4 THE OPTIONS

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/Authority 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/Authority’s external audit; and

- Manage the contract for its duration, overseen by the Auditor Panel.
- 4.2 Alternatively, the Act enables the Council/Authority 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. Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each Council under the Act and the Council would need to liaise with other local authorities to assess the appetite for such an arrangement.
- 4.3 The final option is via the PSAA who is specified as the 'appointing person' for principal 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.
- 4.4 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/Authority 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.

The PSAA have contacted the Chair of the Audit Committee and the S151 officer with an invitation to opt in to these national arrangements and details of the invitation are included at Appendix one.

5. The External Audit market

- 5.1 Issues in the External Audit market are well trailed, with firms across the spectrum not achieving audit deadlines. Notwithstanding the cyber attack delayed the publication of the Council's accounts, so our auditors were not in a position to achieve the audit deadline of the end of September for 2020/21 accounts, across the spectrum, as at 24 November, only 23% of 2020/21 audit opinions had been delivered.
- 5.2 There are only a limited number of local audit firms and audit partners that are registered with the Institute of Chartered Accountants of England and Wales (ICAEW) from which local authorities can appoint from. The strength of the market and attractiveness (or otherwise) of Local Authority audit to firms has been highlighted in the recent Redmond Review. It reported that current fee structures do not enable auditors to fulfil the role in an entirely satisfactory way, and reported a significant risk that the firms currently holding local audit contracts would withdraw from the market.
- 5.3 The Government committed to take action to support stability in the local audit market. Ministers announced £15million in additional funding in 2021/22 to support local bodies to meet an anticipated rise in audit fees in 2021/22, driven by new requirements on auditors including the 2020 Code of Audit Practice.
- 5.4 The Chair of the PSAA wrote in a recent LGC article of the PSAA's strategy which aims to retain the involvement of existing experienced suppliers but also to give new firms an opportunity to join the market through a plan to offer a graduated range of lot sizes including one or two specially designed 'development lots' aimed at new entrants. Quality is also emphasised as a key theme within the procurement. As well as the need to deliver audits which meet all of the requirements of the National Audit Office's code of audit practice including the auditing and ethical standards set by the Financial Reporting Council (FRC) emphasis is on the need to meet the expectations of audited bodies and the timeliness of audit opinions is given a particular mention. Consequently it is stated that the procurement process will place increased emphasis on bidders' plans to resource audits appropriately, prioritising not only capacity but also capability including sector knowledge.

6 Evaluating the options

Individual auditor panel and procurement

- 6.1 The CIPFA Guide to Auditor Panels published in 2015 considers the possible advantages and disadvantages of the set up options for independent auditor panels. Possible advantages of an individual panel include having full ownership of the tendering process and the ability to set bespoke contract terms with the auditor, such as duration.

- 6.2 However, it should be noted that the scope of a local audit is fixed. It is determined by the Code of Audit Practice (currently published by the National Audit Office), the format of the financial statements (specified by CIPFA/LASAAC) and the application of auditing standards regulated by the FRC. The requirements are mandatory; they shape the work auditors undertake and have a bearing on the actual fees required.
- 6.3 Furthermore, some typical contract levers such as penalties for late delivery cannot be applied to an audit services contract, as fees calculated on the basis of a specified outcome (e.g. specific date completions) are classified as contingent fees, not allowed under the FRC's Ethical Standard.
- 6.4 We also need to be mindful of the administrative burden and costs of setting up a local auditor panel as set out in paragraph 4.1 above. There are also a limited number of audit providers eligible to audit local authorities and other relevant bodies under local audit legislation and we would in effect be seeking to attract the same bidders as would the national procurement exercise. The PSAA's measures to attract a wider pool as set out in paragraph 5.4 is also a factor - would the Council as a standalone authority be in a position to attract interest from the market?

Joint auditor panel and procurement

- 6.5 The running of a joint procurement, and creation of a joint auditor panel could potentially mitigate against some of the risks set out of a 'go it alone' model. There may be some increase in interest from the market as they may be able to benefit from some economies of scale as well as the potential of developing a level of specialism - for example, inner-London authorities. Of course, under this arrangement the administrative cost of running a joint audit panel would be shared by participants, and there would be a wider pool from which to attract appropriate panel members.
- 6.6 We cannot ignore, however, the complexity of arranging terms across multiple authorities and of operating a joint panel. Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each council under the Act. We have held some discussions with a neighbouring borough and discussions have also been had at the Society of London Treasurers meetings and it is clear that there is not a strong appetite for such an arrangement and no one borough is driving a proposal of this kind.
- 6.7 We could, as an authority, seek to lead such a proposal, however, we are unconvinced of the benefits this would offer us as a council and are mindful that timelines are tight, with the need to have audit arrangements in place by 31st December 2022. If we were to fail to appoint under such an arrangement attention is drawn to the PSAA letter at Appendix 1 :

you may subsequently make a request to opt in, but only after 1 April 2023. We are required to consider such requests and agree to them unless there are reasonable grounds for their refusal. PSAA must consider a request as the

appointing person in accordance with the Regulations. The Regulations allow us to recover our reasonable costs for making arrangements to appoint a local auditor in these circumstances, for example if we need to embark on a further procurement or enter into further discussions with our contracted firms.

Therefore, there is some element of a financial risk of this option. This same risk would apply under the local appointment option.

Opting in to the national PSAA scheme

- 6.8 The national PSAA scheme offers authorities the simplest and most economical route to auditor appointment. It avoids the need to undertake an auditor procurement and ongoing contract management activities (such as fee variation management), saving local time, effort and cost; and negotiating contracts with the audit firms nationally maximises the opportunities for maximising value for money for the whole sector.
- 6.9 As PSAA is set up as an independent appointing person it also negates the need to establish a local auditor panel, which could be difficult, costly and time-consuming. PSAA also provides the most independent option to auditor appointment and contract management.
- 6.10 The PSAA itself has considerable expertise and experience in the role of appointing auditors, with a dedicated team that is very familiar with the relevant regulations to appoint auditors, manage contracts with audit firms, and set and determine audit fees.

Conclusion

- 6.11 All of the above options require a local auditor to be appointed no later than 31 December 2022. Legislation requires an independent auditor panel to make the appointment.
- 6.12 Having considered the options and furthermore engaged with other boroughs on this issue, officers assess that the benefits of pursuing local control over the auditor procurement and appointment process are limited by the pre-defined scope of the audit, and the limited contract levers available for contract management. We also need to be cognisant that the relatively small market means that we may not obtain a sufficient interest in an independent procurement strategy and a real risk that an independent procurement would not achieve value for money. Audit fees are anticipated to increase from their current levels to address existing market failings (paragraphs 5.2 and 5.3 above refer) and increased audit requirements, and through economies of scale the PSAA scheme is likely to provide the best mitigation against this.
- 6.13 A joint procurement exercise could mitigate but not eliminate some of the risks of a 'go it alone' strategy, however, there are further complications not least the

current lack of appetite for such an arrangement which means this is not a recommended route.

- 6.14 The performance of our current auditors, appointed under the PSAA are of course a further consideration. In relation to the last completed audit (2019/20) Mazars standards fell well below what we have come to expect, although it would be fair to say that this was not the case in the previous year's audit. Also officers are mindful that our experience has not been unique and we are aware of similar frustrations across other London boroughs and that these concerns are not limited to Mazars audits. We are working closely with Mazars for the audit of the 2020/21 accounts, taking on board the challenges the audit may bring in the context of the impact of the cyber attack on some of our financial systems. The Audit Partner is also aware of our level of dissatisfaction and is taking steps to improve performance.
- 6.15 Having considered the options available to the Council, it is recommended that the Audit Committee propose that the Council agree to opt in to the PSAA national scheme for the five year period from 2023/24 to 2027/28. Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in to the PSAA national scheme or to appoint auditors directly must be made by a meeting of the Council as a whole. Furthermore, the Council needs to respond formally to PSAA's invitation in the form specified by PSAA by the close of the opt-in period (11 March 2022). It is recommended that authority is delegated to the Group Director of Finance and Resources to respond to the invitation and take the necessary steps to finalise the appointment itself following the PSAA procurement process.

7 SUSTAINABILITY

- 7.1 PSAA's audit services contracts covering the audits from 2018/19 to 2022/23 include a clause in relation to 'Co-operation with PSAA on environmental issues'. This states that "Throughout the Contract the Supplier shall co-operate with PSAA in seeking reasonable and practical ways to improve the sustainability of the delivery of the Services" so there is a requirement for the PSAA's contracted firms to consider environmental issues. The contract terms to be used for the 2022 procurement have yet to be determined, however the PSAA state that it is their intention to retain this contractual provision.
- 7.2 In addition, in its 2022 procurement PSAA will determine 5% of the bidders' tender evaluation score by the additional social value that they will deliver from the contract. In direct response to their June consultation on the draft scheme prospectus they have broadened the scope of social value that a bidder could provide in its response. The scope now includes sustainability and environmental concerns, and equality, diversity and inclusion, alongside apprenticeships and long term development opportunities. The intention is to ask bidders to describe how their delivery of social value will be measured and evidenced to PSAA so that it will form part of contract management arrangements.
- 7.3 When PSAA develops its auditor appointment proposals following contract award to successful firms, one of the factors that will be considered is the location of the

audit in relation to the locations of the contracted firms' local audit resources. There is the possibility that one of the outcomes from the remote working enforced by C19 is that auditors will travel less to clients, taking advantage of the significant improvements in video conferencing, but it will be some time before that can be assessed with any clarity.

7 COMMENTS OF THE GROUP DIRECTOR OF FINANCE AND CORPORATE RESOURCES

- 7.1 The current fee for the main audit has been around £175k per year. There is a risk that external audit fee levels could increase when the current contracts end. This follows the increase in the scope of audit, which requires more work and also concerns about capacity and sustainability in the local audit market.
- 7.2 Opting into a national scheme provides maximum opportunity to ensure fees are as realistic as possible, while ensuring the quality of audit is maintained, by entering into a large scale collective procurement arrangement.
- 7.3 If we opt not to use the national scheme some additional resource will be needed to establish an auditor panel and conduct a local procurement. 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.

8. COMMENTS OF THE DIRECTOR OF LEGAL

- 8.1 Section 7 of the Local Audit and Accountability Act 2014 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.
- 8.2 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 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 under those arrangements.
- 8.3 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 Council.
- 8.4 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. In July 2016 the Secretary of State specified PSAA as the appointing person.

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[Chief Executive Name], (Chief Executive)
[Authority Name]

Copied to: [name of S151 Officer], (S151 Officer)
[name of Audit Committee Chair], (Chair of Audit Committee or equivalent)

Dear [Salutation],

Invitation to opt into the national scheme for auditor appointments from April 2023

I want to ensure that you are aware the external auditor for the audit of your accounts for 2023/24 has to be appointed before the end of December 2022. That may seem a long way away but, as your organisation has a choice about how to make that appointment, your decision-making process needs to begin soon.

We are pleased that the Secretary of State has confirmed PSAA in the role of the appointing person for eligible principal bodies for the period commencing April 2023. Joining PSAA's national scheme for auditor appointments is one of the choices available to your organisation.

In June 2021 we issued a draft prospectus and invited your views and comments on our early thinking on the development of the national scheme for the next period. Feedback from the sector has been extremely helpful and has enabled us to refine our proposals which are now set out in the [scheme prospectus](#) and our [procurement strategy](#). Both documents can be downloaded from our website which also contains a range of useful information that you may find helpful.

The national scheme timetable for appointing auditors from 2023/24 means we now need to issue a formal invitation to you to opt into these arrangements. In order to meet the requirements of the relevant regulations, we also attach a form of acceptance of our invitation which you must use if your organisation decides to join the national scheme. We have specified the five consecutive financial years beginning 1 April 2023 as the compulsory appointing period for the purposes of the regulations which govern the national scheme.

Given the very challenging local audit market, we believe that eligible bodies will be best served by opting to join the scheme and have attached a short summary of why we believe that is the best solution both for individual bodies and the sector as a whole.

I would like to highlight three matters to you:

1. if you opt to join the national scheme, we need to receive your formal acceptance of this invitation by Friday 11 March 2022;
2. the relevant regulations require that, except for a body that is a corporation sole (e.g. a police and crime commissioner), the decision to accept our invitation and to opt in must be made by the members of the authority meeting as a whole e.g. Full Council or equivalent. We appreciate this will need to be built into your decision-making timetable. We have deliberately set a generous timescale for bodies to make opt in decisions (24 weeks compared to the statutory minimum of 8 weeks) to ensure that all eligible bodies have sufficient time to comply with this requirement; and
3. if you decide not to accept the invitation to opt in by the closing date, you may subsequently make a request to opt in, but only after 1 April 2023. We are required to consider such requests and agree to them unless there are reasonable grounds for their refusal. PSAA must consider a request as the appointing person in accordance with the Regulations. The Regulations allow us to recover our reasonable costs for making arrangements to appoint a local auditor in these circumstances, for example if we need to embark on a further procurement or enter into further discussions with our contracted firms.

If you have any other questions not covered by our information, do not hesitate to contact us by email at ap2@psaa.co.uk. We also publish answers to [frequently asked questions](#) on our website.

If you would like to discuss a particular issue with us, please send an email also to ap2@psaa.co.uk, and we will respond to you.

Yours sincerely

Tony Crawley
Chief Executive

Encl: Summary of the national scheme