
REPORT TO:	AUDIT SUB COMMITTEE	AGENDA ITEM: 9
DATE OF MEETING:	8th DECEMBER 2021	CATEGORY: RECOMMENDED
REPORT FROM:	STRATEGIC DIRECTOR (CORPORATE RESOURCES)	OPEN
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SUBJECT:	APPOINTMENT OF AN EXTERNAL AUDITOR 2023/24 to 2027/28	
WARD(S) AFFECTED:	ALL	TERMS OF REFERENCE: AS 04

1.0 Recommendations

- 1.1 That the Council opts into the national procurement framework for the appointment of its External Auditor from the financial year 2023/24 and this is recommended to Full Council on 13 January 2022.

2.0 Purpose of the Report

- 2.1 To consider whether the Council remains opted-in to the national procurement framework for the appointment of its External Auditor, which will commence for five years from 1 April 2023.

3.0 Detail

- 3.1 Following the abolition of the Audit Commission on 31 March 2015, the responsibility for managing the local government audit process was transferred to the Public Sector Audit Appointments (PSAA) a government appointed agency.
- 3.2 The PSAA's responsibilities, as a recognised appointing body under the Local Audit and Accountability Act 2014, includes appointing external auditors for applicable public sector bodies. The Act also allows local authorities to appoint their own auditors in accordance with procurement regulations.
- 3.3 Previously, auditors were appointed and assigned to councils directly by the Audit Commission. The Commission also set audit fees.
- 3.4 However, due to concerns regarding the cost of external audit at that time, the legislation introduced a competitive element into the appointment of external auditors.
- 3.5 The legislation gives councils flexibility to make appointments alone, in collaboration with other councils, or the appointment can be made through the specified appointing body, i.e., the PSAA.

- 3.6 The appointment of auditors under this process became effective from the financial years 2018/19. During 2016/17, the PSAA introduced a national procurement framework for appointments and invited all councils to opt into this process.
- 3.7 Along with almost every other council in England, the Council agreed to opt-in.
- 3.8 At that time, it was considered that a sector wide procurement conducted by the PSAA would produce a more cost-effective method of appointing auditors. The benefits were considered to be:
- Assurance that auditor appointments would be completed in a proper and timely manner.
 - The independence of auditors would be maintained.
 - More competitive pricing would likely be achieved.
 - No procurement costs involved for individual councils.
 - It would save time and resources on setting up and administering an Audit Panel, which is required if a council wishes to appoint its own auditor.

Independent Audit Panels

- 3.9 If a council wishes to appoint its own auditor, it is required to establish a local independent audit panel. A panel assumes the role of an appointed body and is responsible for considering and recommending an external auditor to the Council. It also monitors and manages the relationship with the external auditor.
- 3.10 A panel could be the local Audit or Governance Committee if it can be demonstrated that this Committee is independent for this purpose.
- 3.11 The 2014 Act specifies that to demonstrate independence, a panel must consist of a majority of independent persons and be chaired by an independent person, i.e. not a council officer, elected member or any person connected to them.

Appointment of Auditors for 2018/19 to 2022/23

- 3.12 Under the new procurement framework, the PSAA received and evaluated tenders from several audit bodies. Consequently, five firms were appointed, and the contract was shared amongst opted-in bodies in lots.
- 3.13 The Council's appointed auditors under this framework are Ernst and Young (EY) and are contracted to the Council until 2022/23. As part of the process, the PSAA are required to consult on and then set a scale of fees for audit, which opted-in councils are required to pay.
- 3.14 At the outset of this Contract, the cost of external audit to local authorities reduced and has continued to do so over the intervening years. This was based on prices submitted by the audit firms as part of the tender process.
- 3.15 The cost of external audit to the Council prior to the current contract was approximately £50,000 per year. This has since fallen by 25% to approximately £37,000 per year and is set to reduce further by 2022/23, as it currently stands.

Issues within the Current Public Sector Audit

- 3.16 Including reports and briefings to this Committee, it has been widely reported that over the last two to three years, the quality and timeliness of external audits has fallen significantly. This has to some extent been exacerbated by Covid 19 and the introduction of additional regulation through accounting and reporting standards for councils, all of which have placed a greater burden on auditors.
- 3.17 However, it is also recognised that there has been an underlying and systemic problem in the sector for some time, affecting most audit firms. Increasingly, audit firms have been hit with resourcing issues, some of which may be a consequence of the pricing in existing contracts, which although tendered and contracted, do not appear sustainable in the long term under current arrangements.
- 3.18 These issues have been recognised and borne out in several Government led reviews into the sector over the last year. The Government have accepted a host of recommendations regarding governance, financial reporting, and standards, etc. which are in the process of being reviewed and worked through.
- 3.19 It is considered that major reform will arise in the external audit sector for public authorities, and it seems inevitable that at some point, the price of audit fees will increase from their current level.

Appointment of Auditors for the Period 2023/24 to 2027/28

- 3.20 In the meantime, councils are being asked by the PSAA whether they wish to opt-in to the next procurement round. To enable the PSAA to conduct a timely procurement exercise during 2022, they have set a deadline of 11 March 2022 for councils to signify their intentions.
- 3.21 The PSAA are clearly aware of the current issues and are keen to address these in the procurement exercise. The prices submitted by bidders through the procurement will still be the key determinant of the value of audit fees paid by opted-in bodies.

The PSAA's Outline Prospectus/Strategy

- 3.22 The PSAA have been in contact with all opted-in councils to outline the aims of the procurement process. As part of this, the PSAA are committed to helping the sector become sustainable and to once again deliver timely and quality audits. In particular by:
- Seeking to encourage realistic fee levels and to benefit from the economies of scale associated with procuring on behalf of a significant number of bodies.
 - Continuing to 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 (*pooling means that everyone within the scheme will benefit from the prices secured via a competitive procurement process – a key tenet of the national collective scheme*).
 - Continuing to minimise its own costs, and as a not-for-profit company will return any surplus funds to scheme members. In 2019 it returned a total of £3.5million to relevant bodies and in 2021 a further £5.6million was returned, the Council's share being approximately £5,000 to £10,000 per year.

- 3.23 PSAA are seeking 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.
- 3.24 Where regulatory changes are being implemented which affect the amount of audit work firms must undertake, firms will be informed as to which developments should be priced into their bids.

Factors to Consider

- 3.25 The scope of a local government audit is heavily regulated. It is fixed and is determined by a Code of Audit Practice. The format of financial statements is also fixed, and the application of auditing standards are regulated by the Financial Reporting Council.
- 3.26 These factors apply to all audits irrespective of whether a council 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 which have a bearing on the actual fees.
- 3.27 There are currently **nine** audit providers who are eligible to audit local authorities and other relevant bodies under Audit Legislation. This means that a local or a stand-alone procurement exercise, would be seeking tenders from the same firms as the national procurement exercise.
- 3.28 Local procurements must deliver the same audit scope and requirements as a national procurement, reflecting the auditor's statutory responsibilities.
- 3.29 Although there have clearly been problems with external audit which have been a huge frustration for many councils, it is still considered that the reasons for opting-in to the national procurement (as highlighted earlier in the report) are still valid.
- 3.30 Many other authorities have already indicated that they will be opting in again. Informal discussions with other Derbyshire authorities, have also indicated the same.
- 3.31 Some discussions have also taken place regarding a regional procurement, but again it is considered that this would not be beneficial compared to a national procurement exercise and there seems little appetite to pursue this option amongst authorities.
- 3.32 Therefore, there would seem little point in the Council pursuing its own procurement as potentially it could spend disproportionate resources appointing an audit firm (assuming bids were received) and then managing the successful firm through an audit panel.
- 3.33 Under Regulation 19 of the Local Audit (Appointing Person) Regulations 2015, a final decision to opt-in must be taken by Full Council. 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.

4.0 Financial Implications

- 4.1 There is a risk that current audit fees could increase when the current Contract ends. It is acknowledged that the scope of audit has increased, requiring more audit work. There are also concerns about capacity and sustainability in the external audit market.
- 4.2 By opting into a collective procurement, this provides more opportunity to ensure fees are as realistic and competitive as possible.
- 4.3 If the national scheme is not used, some additional resource will be needed to establish an audit panel and conduct a local procurement.

5.0 Corporate Implications

Risk

- 5.1 The main risks are that the Council:
- Fails to appoint an auditor in accordance with the requirements and timing specified in legislation.
 - Does not achieve value for money in the appointment process.
- 5.2 It is considered that these risks are best mitigated by opting into the national process.

Legal Implications

- 5.3 Section 7 of the Local Audit and Accountability Act 2014 requires a relevant body to appoint an external auditor to audit its accounts for a financial year not later than 31 December in the preceding year.
- 5.4 Section 8 governs the procedure for appointment as highlighted in the report.
- 5.5 Section 12 makes provision for the failure to appoint an external auditor. A council must immediately inform the Secretary of State, who may direct a council to appoint the auditor named in a direction or appoint an auditor on behalf of a council.
- 5.6 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.

6.0 Community Implications

- 6.1 None directly.

7.0 Background Papers

- 7.1 The Audit and Accountability Act 2014

<http://www.legislation.gov.uk/ukpga/2014/2/contents/enacted/data.htm>