

Open Report on behalf of Pete Moore, Executive Director Finance and Public Protection

Report to:	County Council
Date:	16 December 2016
Subject:	Appointment of External Auditors

Summary:

KPMG are the current external auditors of the Council having been appointed under a national procurement exercise undertaken by the then Audit Commission prior to its abolition. The current contract ends with the audit of the 2017/18 financial statements. Under current regulations the Council needs to have a new audit appointment concluded by December 2017 with duties commencing from April 2018. A number of options exist to the Council for taking this matter forward. Again, under existing regulations, the decision on the way forward is for full Council to take. This paper outlines those options together with their respective merits. It recommends that the option of participating in a national sector led procurement exercise is likely to deliver the best outcome in value for money terms.

Recommendation(s):

That Council agrees:

1 to appoint external auditors for an appointment commencing 1st April 2018 by means of opting in to the national scheme operated by Public Sector Appointments Limited a sector led procurement exercise undertaken by the Local Government Association; and

2 authorises the Executive Director for Finance and Public Protection in consultation with the Leader of the Council to take all decisions and approve all documentation necessary to give effect to the opt in and support the national procurement process.

1. Background

- 1.1. 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 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.
- 1.2. The Council's current external auditor is KPMG, this appointment having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the contract is currently managed by Public Sector Audit Appointments Limited (PSAA), the transitional body set up by the Local Government Association (LGA) with delegated authority from the Secretary of State (Communities & Local Government). Over recent years the Council has 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 are £107k per annum for the Council and £24k per annum for the pension fund.
- 1.3. 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. 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.
- 1.4. 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 registration process has not yet commenced and so the number of firms is not known but it is reasonable to expect that the list of eligible firms may include the top 10 or 12 firms in the country, including our current auditor. It is unlikely that small local independent firms will meet the eligibility criteria.

2. Options for local appointment of External Auditors

- 2.1. There are three broad options open to the Council under the Local Audit and Accountability Act 2014 (the Act):

Option 1 To make a stand-alone appointment

- 2.2. The Council may directly appoint its local auditor. In order to make such a stand-alone appointment the Council will need to set up an Auditor Panel under section 9 of the Act. 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.
- 2.3. The decision to appoint remains with the Council but the Council must, under section 8 of the Act consult and take into account the advice of the Auditor Panel on the selection and appointment of its auditor.

Advantages/benefit

- 2.4. 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

- 2.5. 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
- 2.6. The Council will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts.

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

- 2.7. 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. 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 need to liaise with other local authorities to assess the appetite for such an arrangement.

Advantages/benefits

- 2.8. The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities.
- 2.9. 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

- 2.10. The decision making body will be removed from wholly local input, with the different views of a number of authorities to be accommodated.

2.11. 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 an Appointing Person sector led body

2.12. In response to the consultation on the new arrangement the LGA successfully lobbied for Councils to be able to 'opt-in' to a Sector Led Body (SLB) appointed by the Secretary of State under the Act. An SLB would have the ability to negotiate contracts with the firms nationally, maximising the opportunities for the most economic and efficient approach to procurement of external audit on behalf of the whole sector.

2.13. Provision for such an LSB was made in the Local Audit (Appointing Person) Regulations 2015 ("the Regulations"). Under the Regulations an Appointing Person would be authorised to make appointments on behalf of a number of authorities. The Appointing Person invites the authorities to opt in to their scheme and where an authority opts in it is the Appointing Person who manages the appointment process and makes the appointment. There is accordingly no requirement for an Auditor Panel.

2.14. The Secretary of State has approved Public Sector Audit Appointments Limited (PSAA) (a not-for-profit company established by the LGA) as an Appointing Person under the Regulations and on 27 October 2016 PSAA formally invited the County Council to opt in to its national scheme for auditor appointments. That offer document is attached as Appendix A.

Advantages/benefits

2.15. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities.

2.16. 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.

2.17. Any conflicts at individual authorities would be managed by the SLB who would have a number of contracted firms to call upon.

2.18. PSAA would operate as a separate body set up to act in the collective interests of the 'opt-in' authorities.

Disadvantages/risks

2.19. Individual elected members will have less opportunity for direct involvement in the appointment process other than through the PSAA and/or stakeholder representative groups.

2.20. In order for the Appointing Person (PSAA) to be viable and to be placed in the strongest possible negotiating position they will need Councils to indicate their intention to opt-in before final contract prices are known.

3. The way forward

3.1. 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. If the Council wishes to opt in to the national scheme established by PSAA it will need to accept PSAA's invitation not later than 9 March 2017.

3.2. Greatest economies of scale will come from the maximum number of councils acting collectively and opting-in to a SLB.

4. Risk Management

4.1. 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.

4.2. Providing the LGA with a realistic assessment of our likely way forward will enable the LGA to invest in developing appropriate arrangements to support the Council.

5. Legal implications

5.1. 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. Paragraph 1 of Schedule 3 to the Act 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. The decision therefore falls within the remit of the full Council. Furthermore, under the same provisions the decision cannot be delegated to a Committee, sub-Committee or officer and therefore must be taken by full Council.

5.2. 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.

- 5.3. 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. Where such an Appointing Person is established and the Council opts in to the Appointing Person's scheme the Appointing Person is obliged to appoint an auditor for the Council, not the Council itself.

Equality Act 2010

- 5.4 The Council's duty under the Equality Act 2010 needs to be taken into account by the decision-maker when coming to a decision.
- 5.5 The Council must, in the exercise of its functions, have due regard to the need to:
- Eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;
 - Advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it;
 - Foster good relations between persons who share a relevant protected characteristic and persons who do not share it: Equality Act 2010 section 149(1). The relevant protected characteristics are age; disability; gender reassignment; pregnancy and maternity; race; religion or belief; sex; sexual orientation: section 149(7).
- 5.6 Having due regard to the need to advance equality of opportunity involves having due regard, in particular, to the need to:
- Remove or minimise disadvantages suffered by persons who share a relevant protected characteristic that are connected to that characteristic;
 - Take steps to meet the needs of persons who share a relevant protected characteristic that are different from the needs of persons who do not share it;
 - Encourage persons who share a relevant protected characteristic to participate in public life or in any other activity in which participation by such persons is disproportionately low.
- 5.7 The steps involved in meeting the needs of disabled persons that are different from the needs of persons who are not disabled include, in particular, steps to take account of disabled persons' disabilities.
- 5.8 Having due regard to the need to foster good relations between persons who share a relevant protected characteristic and persons who do not share it involves having due regard, in particular, to the need to tackle prejudice, and promote understanding.

- 5.9 Compliance with the duties in this section may involve treating some persons more favourably than others.
- 5.10 A reference to conduct that is prohibited by or under this Act includes a reference to:
- (a) A breach of an equality clause or rule
 - (b) A breach of a non-discrimination rule
- 5.11 It is important that the decision-maker is aware of the special duties the Council owes to persons who have a protected characteristic as the duty cannot be delegated and must be discharged by the decision-maker. The duty applies to all decisions taken by public bodies including policy decisions and decisions on individual cases and includes this decision.
- 5.12 To discharge the statutory duty the decision-maker must analyse all the relevant material with the specific statutory obligations in mind. If a risk of adverse impact is identified consideration must be given to measures to avoid that impact as part of the decision making process.
- 5.13 Equality considerations have been taken into account but the decision in question is not considered to have any implications for people with a protected characteristic.

Joint Strategic Needs Assessment (JSNA) and Joint Health and Wellbeing Strategy

- 5.14 Regard has been had to both the JSNA and the Joint Health and Wellbeing Strategy and the decision in question is not considered to impact directly on either.
- 5.15 Regard has also been had to the Council's duty under section 17 of the Crime and Disorder Act 1998 and the decision is considered to have no direct implications for the Council's fulfilment of its crime and disorder obligations.

6. Financial Implications

- 6.1. Current external fees levels are likely to increase when the current contracts end in 2018.
- 6.2. The cost of establishing a local or joint Auditor Panel outlined in options 1 and 2 above will need to be estimated and included in the Council's budget for 2016/17 and 2017/18. This will include the cost of recruiting independent appointees (members), servicing the Panel, running a bidding and tender evaluation process, letting a contract and paying members fees and allowances.

6.3. 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 auditor panel.

2. Conclusion

The Council is required to take action to appoint external auditors from April 2018. The analysis undertaken in this paper suggests the approach that will offer the best value for money is to participate in the sector led procurement initiative being coordinated by the LGA.

3. Legal Comments:

The Council is required to take action to appoint external auditors from April 2018. The available options and their legal implications are set out in the Report together with the considerations that must be taken into account in reaching a decision.

The decision is one which must be made by the full Council.

4. Resource Comments:

The use of a sector led procurement approach to the appointment of external auditors will maximise value for money both in terms of the procurement exercise itself but also, more significantly, in terms of the fee levels for the service from April 2018 onwards.

5. Consultation

a) Has Local Member Been Consulted?

n/a

b) Has Executive Councillor Been Consulted?

Yes

c) Scrutiny Comments

The concept of pursuing a sector led procurement exercise was considered and supported by the Audit Committee at its meeting on 20th June 2016.

d) Policy Proofing Actions Required

n/a

6. Appendices

These are listed below and attached at the back of the report	
Appendix A	Invitation to opt into the national scheme for auditor appointments

7. Background Papers

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

This report was written by David C Forbes, who can be contacted on 01522 553642 or david.forbes@lincolnshire.gov.uk.

This page is intentionally left blank