

**MEETING: 14<sup>TH</sup> FEBRUARY 2022**

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**SUBJECT: EXTERNAL AUDITOR APPOINTMENT FROM 1st APRIL 2023**

**JOINT REPORT OF THE CHIEF FIRE OFFICER/CHIEF EXECUTIVE (THE CLERK  
TO THE AUTHORITY) AND THE FINANCE DIRECTOR**

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**1. PURPOSE OF THE REPORT**

- 1.1 This report informs the Authority of the options available for the appointment of the external auditors for the financial year beginning on 1 April 2023 and covering the five financial years audits for 2023/24 to 2027/28), and seeks approval to opt into the national sector-led arrangement for the appointment of external auditors (using PSAA) with effect from 1 April 2023.

**2. BACKGROUND INFORMATION**

- 2.1 Under the Local Government Audit and Accountability Act 2014 ("the Act"), the Authority is required to appoint an auditor to audit its accounts for each financial year. The Authority currently has three options available:
1. To appoint its own auditor, which requires it to follow the procedure set out in the Act;
  2. To act jointly with other authorities to procure an auditor following the procedures in the Act; or
  3. To opt into the national auditor appointment scheme administered by the Secretary of State as the 'appointing person'. The body currently designated for this role is Public Sector Auditor Appointments (PSAA).
- 2.2 At its December 2016 meeting, the Authority agreed to opt into the 'appointing person' national auditor appointing arrangements, established by Public Sector Auditor Appointments (PSAA) for the period covering the accounts for 2018/19 to 2022/23.
- 2.3 The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 Statement of Accounts, after which they expire and PSAA is surveying local authorities with a view to undertaking another procurement exercise for the next appointing period, covering audits for the five financial years from 2023/24 to 2027/28.

- 2.4 The Authority thus needs to make a decision about its external audit procurement arrangements from 2023/24 onwards and if it wishes to again opt into the national scheme, using PSAA then it must notify them no later than 11<sup>th</sup> March 2022.

### **3. THE APPOINTED AUDITOR ROLE**

- 3.1 The auditor appointed at the end of the procurement process will undertake the statutory audit of the Authority's Statement of Accounts and also provide its detailed opinion and assessments of the Authority's Value for Money Arrangements in each financial year, in accordance with all relevant codes of practice and guidance.
- 3.2 The appointed auditor is also responsible for investigating questions raised by electors and has powers and responsibilities in relation to matters in the Public Interest.

### **4. EXTERNAL AUDITOR REQUIREMENTS**

- 4.1 The auditor must act independently of the Authority and the main purpose of the procurement legislation is to ensure that the appointed auditor is sufficiently qualified and independent.
- 4.2 The auditor must be registered to undertake local audits by the Financial Reporting Council (FRC) who employ authorised Key Audit Partners to oversee the work. There is a currently a shortage of registered firms and Key Audit Partners.
- 4.3 Auditors are regulated by the FRC, which will be replaced during the course of the next audit contract by a new body with wider powers, the Audit, Reporting and Governance Authority (ARGA).
- 4.4 Authorities 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.

### **5. OPTIONS FOR THE AUTHORITY TO PROCURE ITS OWN EXTERNAL AUDITOR OR BY USING A JOINT ARRANGEMENT**

- 5.1 Should the Authority wish to appoint its own external auditor under the Act, it would need to:
- a. establish an independent auditor panel to make a stand-alone appointment. The auditor panel would need to be set up by the Authority itself, and the members of the panel would have to 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 would not have a majority input to assessing bids and choosing which audit firm to award a contract for the Authority's external audit.

- b. manage the contract for its duration, overseen by the auditor panel.
- 5.2 Alternatively, the Act enables the Authority to join with other local 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 authority under the Act and the Authority would need to liaise with other local authorities to assess the appetite for such an arrangement.
- 5.3 These two options would be more resource-intensive and without the bulk buying power of the sector-led procurement service, would likely result in a more costly process for the Authority to implement. It would also be more difficult to manage quality and independence requirements through a local appointment process. The Authority would not be able to influence the scope of the audit and the regulatory regime would inhibit the Authority's ability to affect quality.
- 5.4 The Authority and its auditor panel would in addition need to maintain ongoing oversight of the contract.

## **6. THE NATIONAL AUDITOR APPOINTMENT SCHEME**

- 6.1 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.
- 6.2 The benefits of opting into the national scheme are as follows:
- a) the appointment of a suitably qualified audit firm to conduct audits for five financial years commencing 1 April 2023;
  - b) 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;
  - c) 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;

- d) ensuring suitable independence of the auditors from the bodies they audit and managing any potential conflicts as they arise during the appointment period;
- e) minimising the scheme management costs and returning any surpluses to scheme members;
- f) consulting with authorities on auditor appointments, giving the Authority the opportunity to influence which auditor is appointed;
- g) consulting with authorities on the scale of audit fees and ensuring these reflect scale, complexity, and audit risk; and
- h) ongoing contract and performance management of the contracts once these have been let.

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

## **7. CURRENT PRESSURES IN THE LOCAL AUDIT MARKET**

7.1 Much has changed in the local audit market since audit contracts were last awarded by PSAA 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 bodies who were eligible opted into the national scheme and attracted competitive bids from audit firms.

7.2 The resulting audit contracts took effect from 1 April 2018, however 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, following which four independent reviews were commissioned by Government:

- a. Sir John Kingman's review of the Financial Reporting Council (FRC), the audit regulator;
- b. the Competition and Markets Authority review of the audit market;
- c. Sir Donald Brydon's review of the quality and effectiveness of audit; and recently
- d. Sir Tony Redmond's review of local authority financial reporting and external audit.

7.3 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.

7.4 The Kingman review has 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. By the time firms were conducting 2018/19 local audits during 2019, the measures they were putting in place to respond to a more focused regulator were clearly visible.

- 7.5 To deliver the necessary improvements in audit quality, firms were requiring their audit teams to undertake additional work to gain deeper levels of assurance. However, additional work requires more time, posing a threat to the firms' ability to complete all their audits by the target date for publication of audited accounts. Delayed opinions are not the only consequence of the FRC's drive to improve audit quality. Additional audit work must also be paid for. As a result, many more fee variation claims have been needed than in prior years.
- 7.6 This situation has been exacerbated by growing auditor recruitment and retention challenges, the complexity of local government financial statements and increasing levels of technical challenges as bodies explore innovative ways of developing new or enhanced income streams to help fund services for local people. These challenges have increased in subsequent audit years, with COVID19 creating further significant pressure for finance and audit teams.
- 7.7 None of these problems are unique to local government audit. Similar challenges have played out in other sectors too, where increased fees and disappointing responses to tender invitations have been experienced during the last two years in particular.
- 7.8 It should be noted that despite the wider problems outlined above, the experiences of the Authority under the current arrangements have been positive, benefitting from an effective working relationship with our appointed auditor.

## **8. AUDIT PROCUREMENT**

- 8.1 The prices submitted by bidders through the procurement exercise will be the key determinant of the value of audit fees paid by opted-in bodies. PSAA will:
- a. seek to encourage realistic fee levels and benefit from the economies of scale associated with procuring on behalf of a significant number of bodies;
  - b. continue 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 principle and benefit of the national collective scheme;



- c. continue to 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 £3.5 million to relevant bodies and returned a further £5.6 million in 2021).
- 8.2 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 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.
- 8.3 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. 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.
- 8.4 There are currently nine audit providers eligible to audit local authorities and other relevant bodies under local audit legislation. This means that 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 firms cannot be invited to bid. Local procurements must deliver the same audit scope and requirements as a national procurement, reflecting the auditor's statutory responsibilities.
- 9. NEXT STEPS**
  - 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 Full Authority or equivalent (meeting as a whole), except where the authority is a corporation sole (e.g. Police and Crime Commissioner) in which case this decision can be taken by the holder of that office.
  - 9.2 Therefore, the Authority must approve formal acceptance of the invitation to opt in to the PSAA National Scheme for auditor appointments from April 2023.
  - 9.3 PSAA will commence the formal procurement process in early February 2022. It expects to award contracts in August 2022, then consult with authorities on

the appointment of auditors in order to make appointments by the statutory deadline of 31 December 2022.

## **10. FINANCIAL IMPLICATIONS**

- 10.1 The financial implications are not known at this time but the use of the proposed opt in arrangements using PSAA are viewed as the best value arrangements available based upon their proven track record of procuring good value and effective external audit services and the fact they are not for profit organisation and have a track record of re-distributing savings generated over the past four years of the current contract.

## **11. EQUALITY AND FAIRNESS IMPLICATIONS**

- 11.1 There are no equality and fairness implications in respect of this report.

## **12. HEALTH AND SAFETY IMPLICATIONS**

- 12.1 There are no health and safety implications in respect of this report.

## **13. RECOMMENDATION**

- 13.1 The Authority is requested to review the Options set out in the report, and is recommended to accept the PSAA invitation to opt into the sector-led option for the appointment of external auditors for five financial years commencing 1 April 2023.

