

GOVERNANCE COMMITTEE

MEETING: 19TH MARCH 2012

SUBJECT: LOCAL PUBLIC AUDIT

REPORT OF THE CHIEF FINANCE OFFICER

1. Introduction

- 1.1 To provide a summary of the Government's response to the recent consultation regarding their proposals for the future arrangements for local public audit. The report also includes a brief commentary on the proposals in bold italics.

2. Description of Decision

- 2.1 The Governance Committee is asked to consider the report.

3. Background

- 3.1 On the 13 August 2010 the Secretary of State for Communities and Local Government announced plans to disband the Audit Commission, and refocus the audit of local public bodies on helping local people hold those bodies to account for local spending decisions. Following this announcement, the Government consulted on its proposals for a new local public audit framework.
- 3.2 The design principles of the new framework for local public audit are that it should be localist and transparent, achieve a reduction in the overall cost of audit, and uphold high standards of auditing, ensuring that there is effective and transparent regulation of public audit, and conformity to the principles of public audit.
- 3.3 The Secretary of State's aim is to replace the current, centralised audit systems managed by the Audit Commission, with a new decentralised regime, which will support local democratic accountability, and one that will also cut bureaucracy and costs, while ensuring that there continues to be robust local public audit.

4. Government's Response to the Consultation

- 4.1 The following sections provide a summary of the Governments response to the consultation and the new proposals.

Regulation

- 4.2 The National Audit Office is considered best placed to produce the Code of Practice and supporting guidance for audit of local public bodies, subject to Parliamentary approval. The National Audit Office will be required to consult key partners in developing the Code.
- 4.3 The Financial Reporting Council will be the overall regulator, mirroring its role under the Companies Act 2006. The Financial Reporting Council will be responsible for recognition and supervision of Recognised Supervisory Bodies (professional accountancy bodies responsible for supervising the work of auditors, and setting criteria which their members must fulfil before they can be registered auditors) and for Recognised Qualifying Bodies (professional accountancy bodies responsible for awarding audit qualifications).

Auditor Regulation

- 4.4 Mirroring the Companies Act 2006, Recognised Supervisory Bodies will:
- have the roles of registration, monitoring and discipline for local public audit,
 - put in place rules and practices covering eligibility of firms to undertake local public audit; and
 - keep a register of firms eligible to undertake local public audit.

Monitoring and Enforcement

- 4.5 As under the Companies Act 2006, Recognised Supervisory Bodies will monitor the quality of audits undertaken by their member firms, and investigate complaints, disciplinary cases and issues identified during the monitoring of firms on the register of local public auditors.
- 4.6 The Accountancy and Actuarial Disciplinary Board (part of the Financial Reporting Council) investigates significant public interest disciplinary cases and can impose sanctions on those auditors found guilty of misconduct in both the companies and public sectors. This arrangement is to continue.
- 4.7 There will be additional oversight and monitoring of the audits of significant local public bodies (referred to as “Bodies of Significant Public Interest”) - the Financial Reporting Council will monitor the quality of the audits of these bodies, mirroring the arrangements for Public Interest Entities under the Companies Act.

Commissioning Local Public Audit Services

4.8 Auditor Appointment:

- Local public bodies will have a duty to appoint an auditor from the register of local public auditors, on the advice of an Independent Auditor Appointment Panel. The Independent Audit Appointment Panel will have an independent chair and a majority of independent members. Where the body already has an independent audit committee, this could be used to meet this requirement.
- Local public bodies will be able to share appointment panels (and therefore independent members) to ease admin burdens and reduce costs.
- Local public bodies will be required to publish details of the auditor appointment on their website within 28 days of making the appointment, together with the Independent Audit Appointment Panel's advice and, if they did not follow that advice, a statement explaining why.
- Government intends to prescribe specific functions to the Independent Audit Appointment Panel limited to the external audit, including advising on auditor appointment, independence, removal and resignation, and in relation to public interest reports.
- Where the local public body is not an elected body, then in most circumstances that appointment should be made directly by the Independent Auditor Appointment Panel (or its equivalent). This is the case for the Fire and Rescue Authority as the members are appointed by the local Councils. There may be circumstances where it is appropriate for a local public body's board to make that appointment on the advice of the Panel. However, where this is the case transparency (i.e. publication of that advice) will be an important part of the appointment process.

4.9 Failure to Appoint an Auditor:

Local public bodies will be required to appoint an auditor by 31 December in the year preceding the financial year to be audited, and notify the Secretary of State if they have not done so. The Secretary of State will be able to direct the local public body to appoint an auditor or make the auditor appointment directly. In addition to meeting the cost of the appointment the local public body could be subject to a sanction for failing to make the appointment.

4.10 Rotation of Audit Firms and Audit Staff:

- Local public bodies will be required to run a procurement competition for its audit services at least every five years.
- Auditors will have to comply with the standards and rules set by the regulator. Applying the current standards means the audit engagement partner will be able to undertake audit for a local public body for an initial five years and be reappointed for a further two years. The audit manager will be able to be appointed for a maximum of ten years. After these periods, these key audit staff will not be able to work with the local public body for a further five years.

4.11 Resignation or Removal of an Auditor:

There will be rigorous, transparent processes for auditor resignation or removal, designed to protect auditor independence, quality of audit, and accountability to the electorate. These broadly mirror those in the Companies Act, but are adapted to reflect the principles of public audit.

4.12 Scope of Local Public Audit and Auditors' Work:

- The scope of local public audit will remain broadly similar. As now, auditors of local public bodies will be required to satisfy themselves that the accounts have been prepared in accordance with the necessary directions, proper practices have been observed in the compilation of the accounts, and the body has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.
- The detail of how auditors should fulfil these requirements will, as now, be set out in a code of audit practice. The value for money component should be more risk based and proportionate based on evidence provided by the local body.
- The duty for auditors of local public bodies to undertake Public Interest Reporting will be retained, as will their ability to charge audited bodies for reasonable work.
- Auditors will be permitted to provide non-audit services to the audited body, subject to adhering to the Auditing Practices Board's ethical standards and the Independent Auditor Appointment Panel's approval.
- The local public auditor and the Independent Auditor Appointment Panel will be defined as designated persons under the Public Interest Disclosure Act [relates to whistleblowing], to enable individuals to make disclosures under the Act.

- The new framework will retain the rights of local electors to make formal objections to the accounts, but give auditors greater discretion regarding whether to pursue an objection.

4.13 Non Audit Functions of Audit Commission:

- Following the Audit Commission's closure, Government considers that for new grants, the grant paying bodies should agree certification arrangements with grant recipients and auditors.
- Government proposes to continue the National Fraud Initiative, and is discussing with partners and the local public sector about how best to achieve this.
- The Government considers that there is scope for rationalisation in the number of these value for money studies compared to the number previously undertaken and would like to see a coherent and complementary programme of offerings across all providers.

5. Implementation and Next Steps

5.1 In progressing the proposals the Government intends to:

- hold further discussions with local authorities, other local public bodies and the audit sector to flesh out the underlying detail of the framework, and how it might be implemented;

An event with the ANEC Leaders was held on 27th January 2012 to seek their views.

- publish a draft Bill for pre-legislative scrutiny in Spring 2012, which allows for examination and amendments to be made before formal introduction to Parliament.

5.2 The Audit Commission is currently in the process of outsourcing all the audit work of its in-house practice. The outsource contracts will start from 2012-13 and are expected to run for three or five years giving local authorities the time to plan for appointing their own auditors. Once the audits have been outsourced the Commission will be radically reduced in size to become a residuary body responsible for overseeing the contracts and making any necessary changes to the individual audit appointments during the life of the contracts.

6. Recommendations

6.1 Members are asked to note the report.

Background Papers

Government response to the future of local audit consultation (DCLG) – January 2012

