

REPORT 1

HARBOROUGH DISTRICT COUNCIL

REPORT TO THE AUDIT & STANDARDS COMMITTEE MEETING OF 20 OCTOBER 2021

PUBLIC REPORT: Y

EXEMPT REPORT: N

Report Title	Appointment of External Auditor				
KEY DECISION	No				
Report Author	Clive Mason: Director; Finance, ICT and Assets				
Purpose of Report	The final year of Mazars being our appointed auditors is 2022/23, a new appointment is required for 2023/24. This report will inform members of the committee of the appointment process and make a recommendation for them to propose to Council the preferred option in appointing an external auditor. This decision can only be made by Council but the Committee should consider the options and make its recommendation.				
Reason for Decision	To ensure that the Council appoints its external auditor in an open and transparent way.				
Portfolio (holder)	Cllr James Hallam – Portfolio Holder for Resources				
Corporate Priorities	<table border="1"><tr><td colspan="2">YOUR COUNCIL: creative, proactive, and efficient</td></tr><tr><td>CO 08</td><td>Deliver financial sustainability for the future</td></tr></table>	YOUR COUNCIL: creative, proactive, and efficient		CO 08	Deliver financial sustainability for the future
YOUR COUNCIL: creative, proactive, and efficient					
CO 08	Deliver financial sustainability for the future				
Financial Implications	As set out in the body of the report.				
Risk Management Implications	External Audit supports the Council in mitigating risk by providing the necessary review and commentary on the Councils financial stewardship, governance and achievement of value for money.				
Environmental Implications	There are no direct environment implications arising from this report.				
Legal Implications	As set out in the body of this report				
Equality Implications	There are no direct equality implications arising from this report.				
Data Protection Implications	There are no direct data protection implications arising from this report.				
Consultation	None required.				
Background Papers	None				
Appendices	Advantages (Benefits) and Disadvantages (Risks) of: <ul style="list-style-type: none">• Option 2 (Stand-Alone Auditor Appointment),and• Option 3 (Joint Arrangement Auditor Appointment)				

REPORT 1

Recommendation	To recommend to Council that: <ul style="list-style-type: none"><li data-bbox="683 235 1503 392">i. The Council opts in to the appointing person arrangements made by Public Sector Audit Appointments Ltd (PSAA) for the appointment of external auditors (Option1).<li data-bbox="683 403 1503 517">ii. Delegates authority to the Director; Finance, ICT and Assets to submit the formal notice of acceptance and provision of information to PSAA as required.
-----------------------	---

1 Background

- 1.1 The Local Audit and Accountability Act 2014 brought to a close the Audit Commission and the arrangements for the appointment of external auditors and the setting of audit fees for all local government and NHS bodies in England.
- 1.2 When the last external audit procurement was undertaken, at its meeting of the 23rd January 2017 the Council approved the appointment of PSAA to procure and appoint its external auditor. The last year of the current contract is 2022/23; with new contracts starting from April 2023.
- 1.3 There are 3 options available for local government to appoint its external auditor:

Option 1: to an approved sector led body (SLB) to be specified by the Ministry for Housing, Communities and Local Government (MHCLG) to act as the Appointing Person on behalf of opted-in authorities. The opt-in sector led body approach requires Full Council Approval (Regulation 19, Local Audit (Appointing Person) Regulations 2015). The SLB is Public Sector Audit Appointments Ltd (PSAA), who are a wholly owned company of the Local Government Association.

Option 2: establish its own independent auditor panel (Part 3, section 9 and schedule 4 of the Local Audit and Accountability Act 2014). The panel must be made up of a majority or of wholly independent members and must be chaired by an independent member.

Option 3: establish a joint independent auditor panel to carry out the function on behalf of two or more Councils.

2. Review of Options

Option1- Appointment of PSAA

- 2.1 Our current external audit provider, Mazars LLP, was appointed under the previous PSAA procurement contract arrangement. Current scale fees are based on rates negotiated by PSAA and reflect market share offered in framework contracts. If the Council wishes to remain in the PSAA framework and allow PSAA to continue to manage the appointment of the external auditors, it can do so. PSAA are requesting that all Councils wishing to “opt in” to the new PSAA scheme should ideally notify them by the end of the calendar year. PSAA operates a sector-wide procurement that they argue would produce better outcomes and will be less burdensome for the Council than any procurement undertaken locally (Options 2 and 3). Further, it is expected that the appointed auditor would be for a period of 5-years.
- 2.2 The PSAA have been consulting with local government during 2021 and significant information is provided at their website: www.psa.co.uk/about-us/appointing-person-information/appointing-period-2023-24-2027-28/

2.3 The advantages and disadvantages of **Option 1** are:

2.4 **Advantages (Benefits)**

- i. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities. 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. Any conflicts at individual authorities would be managed by the Sector-led Body who would have a number of contracted firms to call upon. The appointment process would not be ceded to locally appointed independent members. Instead a separate body is set up to act in the collective interests of the 'opt-in' authorities.
- ii. The audit costs are likely to be lower than if the Council/Authority sought to appoint locally, as national large-scale contracts are expected to drive keener prices from the audit firms;
- iii. Without the national appointment, the Council would need to establish a separate independent auditor panel, which could be difficult, costly and time-consuming;
- iv. PSAA can ensure the appointed auditor meets and maintains the required quality standards and can manage any potential conflicts of interest much more easily than the Council/Authority;
- v. Supporting the sector-led body will help to ensure there is a vibrant public audit market for the benefit of the whole sector and this Council/Authority going forward into the medium and long term.
- vi. The scope of local audit is fixed, being defined by statute and by accounting and auditing codes, so it would be the same under a local procurement as under PSAA's procurement.

In respect of PSAA itself:

- vii. PSAA has considerable expertise and experience in the role of appointing person.
- viii. Government confidence having appointed PSAA for a second five-year period – MHCLG's Spring statement refers to our "strong technical expertise and the proactive work we have done to help to identify improvements".
- ix. A dedicated team who are very familiar at working within the context of the relevant regulations to appoint auditors, manage contracts with audit firms, and set and determine audit fees.
- x. A not-for-profit organisation whose costs are around 4% of the scheme with any surplus distributed back to scheme members – so it provides value for public money PSAA is member of new Local Audit Liaison Committee, and regular links with MHCLG and the HO so give feedback and of the sector.

2.5 Disadvantages (Risks)

- i. Individual elected members will have less opportunity for direct involvement in the appointment process other than through the LGA and / or stakeholder representative groups.
- ii. For the Sector-led Body to be viable and to be placed in the strongest possible negotiating position it will need Councils to indicate their intention to opt-in before final contract prices are known.
- iii. There is less control over the contract length and deciding who will be the external auditors appointed.

Option 2 and 3 – Stand Alone or Joint Arrangement Auditor Appointment

2.6 The governance around Option 2 and 3 are similar; the only difference between the two is that:

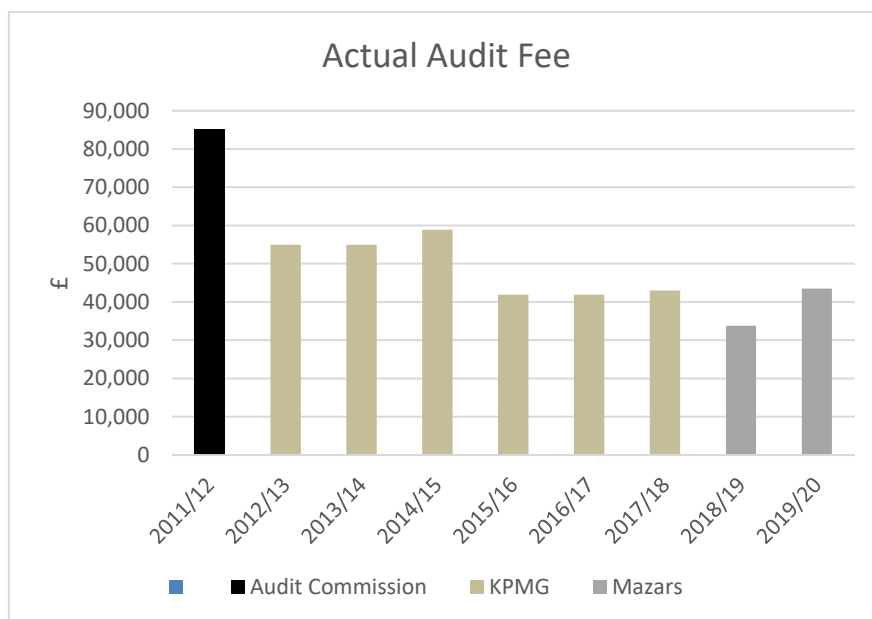
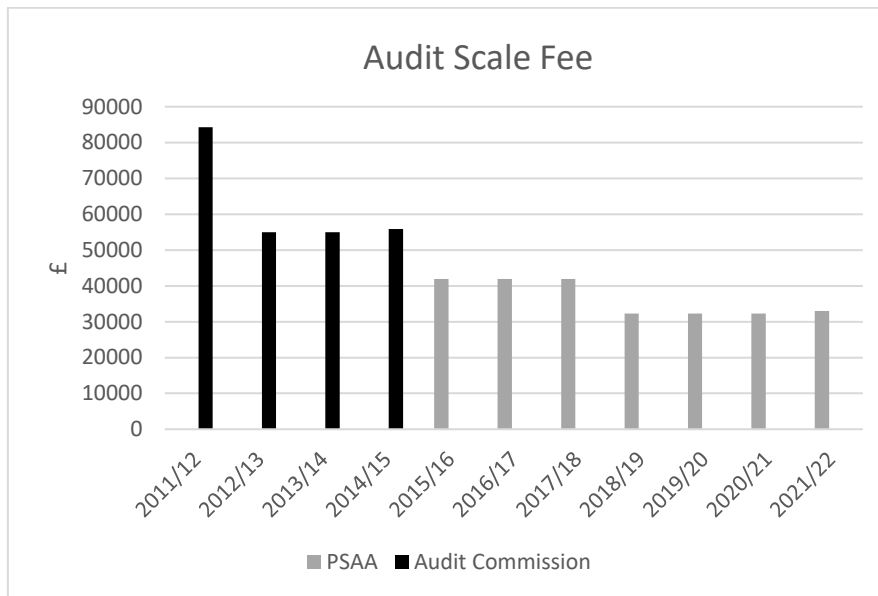
- Option 2 the Council appoints its own external auditor (stand-alone appointment), whereas
- Option 3 the Council appoints along with other Councils (joint arrangement).

2.7 For both Options 2 and 3 the Council will either have to establish its own or participate in a joint auditor panel. Such appointment panels are required to be wholly (or a majority) of 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. This means that elected members will not have a majority input to assessing bids and choosing which firm of accountants to award a contract for the Council's external audit – only the independent auditor panel established by the Council will be responsible for selecting the auditor. The advantages and disadvantages of Option 1 (Stand-Alone) and Option 2 (Joint Arrangement) are shown in the attached **Appendix**.

2.8 The **overriding disadvantage** of Options 2 and 3 when compared to Option 1 is that there are only 8 (in England) qualified, registered auditors who are duly accredited to undertake public audit. It is therefore expected that these auditors will be procured via the PSAA arrangement and thus economies of scale will be lost via Options 2 and 3 because a local arrangement would be "fishing in the same pool" as that of PSAA.

3.0 Future Fee expectation

3.1 The coloured bars in the graphs below show that in respect of both the scale fee (the annual estimated cost of audit) and the actual fee (scale fee + agreed fee variations) are less than the pre-PSAA audit contracts – so on a "simple" cost comparison basis it is shown that PSAA is achieving improved VfM compared to previous suppliers (i.e. cheaper audit conclusion).



3.2 However, it is anticipated that future year’s audit fees, no matter how procured, will cost more than in the past; some of this higher cost was starting to be reflected in the audit requirements of 2019/20. The reasons for this higher cost of audit includes:

- **Limited auditor resource.** This has come about because a lot of the former Audit Commission staff have now exited the audit sector. The firms are now having to invest in their own internal training programmes for a very limited public sector audit market.
- **Higher audit standards.** Because of the audit shortcomings that have been identified following the collapse of Enron, Carillion and other similar high-profile companies, the audit testing regime has been enhanced to

help ensure greater reliance on audit conclusions. There are also planned changes in regulation, through the replacement of the Financial Reporting Council with the new Audit, Reporting and Governance Authority (ARGA)

- **Introduction of new auditing and accounting standards**, requiring additional audit work in a variety of areas, such as accounting estimates, group reporting and leases
- **Introduction of the new Code of Practice**, covering a wider scope on Value for Money and reporting, increasing the volume of work required by experienced staff
- **Increased risk profile and complexity of local authorities**, for example entering new transactions, investments, and new models of delivery, increasing the time input of senior and experienced staff

4.0 Preferred Approach to the Appointment of External Auditor

- 4.1 On balance, considering the various advantages and disadvantages related to each of the options for procuring an external auditor; on balance it is considered that the arrangement offered by PSAA offers best value in respect of audit contract value and the cost of administration. It is therefore recommended that this Committee recommends to Council that:
- i. The Council opts in to the appointing person arrangements made by Public Sector Audit Appointments Ltd (PSAA) for the appointment of external auditors.
 - ii. Delegates authority to the Director; Finance, ICT and Assets to submit the formal notice of acceptance and provision of information to PSAA as required.

Advantages (Benefits) and Disadvantages (Risks) of:

- **Option 2 (Stand-Alone Auditor Appointment),and**
- **Option 3 (Joint Arrangement Auditor Appointment)**

Appendix

Option 2 (Stand-Alone Auditor Appointment)

Advantages / benefits

- Setting up an auditor panel allows the Council to take advantage of the new local appointment regime and have local input to the decision. Also, the Council will have full control over which external audit company will be appointed.

Disadvantages / risks

- 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-£20,000 plus ongoing expenses and allowances.
- The Council will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts compared to trying to make a local appointment.
- The assessment of bids and decision on awarding contracts will be taken by independent appointees and not solely by elected members.
- It is highly unlikely that a lower fee will be obtained than if PSAA were used, and it is likely that little interest will be received from External Auditors not present at other local authorities. This would mean effectively having to use PSAA appointed auditors that had won regional audits in the area as firms would not want to service a small number or cluster of audits unless fees were significantly higher.

Option 3 (Joint Arrangement Auditor Appointment)

Advantages / benefits

- The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities.
- There is a greater opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.

Disadvantages / risks

- The decision-making body will be further removed from local input, with potentially no input from elected members (where a wholly independent auditor panel is used) or possibly only one elected member representing each Council, depending on the constitution agreed with the other bodies involved.

- 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.
- It is highly unlikely that a lower fee will be obtained than if PSAA were used, and we may not get any interest from External Auditors not present at other local authorities. This would mean effectively having to use PSAA appointed auditors that had won regional audits in the area as firms would not want to service a small number or cluster of audits unless fees were significantly higher.