SLOUGH BOROUGH COUNCIL

REPORT TO:	Council
DATE:	10th March 2022
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PART I
FOR DECISION

RECOMMENDATION OF THE AUDIT AND CORPORATE GOVERNANCE COMMITTEE FROM ITS METING HELD ON 9TH DECEMBER 2021 - APPOINTMENT OF EXTERNAL AUDITORS FOR 2023/24 TO 2027/28

1 Purpose of Report

The report outlines the options available in considering future arrangements for the Council in appointing external auditors for the five-year period from 2023/24.

The report was considered by the Audit & Corporate Governance Committee on 9th December 2021 which agreed to make the recommendation set out in Section 2. The Cab

2. Recommendation:

That the Council accepts the Public Sector Audit Appointments' (PSAA) invitation to opt into the sector-led option for the appointment of external auditors for the five-year period from 2023/24.

Comments of the Commissioners:

"The Commissioners support the recommendation to accept the PSAA invitation to opt in to the sector led option for the appointment of SBC external auditors for the five year period from 2023/24."

3. The Slough Joint Wellbeing Strategy, the JSNA and the Five-Year Plan

The actions contained within the attached reports are designed to improve the governance of the organisation and will contribute to all of the emerging Community Strategy Priorities.

3a. Slough Wellbeing Strategy Priorities

The actions contained within the attached reports are designed to improve the governance of the organisation and will contribute to all of the Slough Wellbeing Strategy Priorities.

3b. **Five Year Plan Outcomes**

The actions contained within this report will assist in achieving all of the five-year plan outcomes.

4. **Other Implications**

(a) Financial

The proposed fees cannot be fully known until the procurement process has been completed, as the costs will depend on proposals from the audit firms. Given the widespread prevalence of fee variations, market uncertainty and the revision to an 80% quality weighting within the procurement, it is almost certain that the fee payable by the Council will rise.

If the changes that relate to audit fees, proposed in MHCLG's recent consultation on the Appointing Person Regulations, are ultimately approved and implemented, PSAA will be able to manage the scale of fees and fee variations more flexibly. This will enable scale fees to be determined by taking into account the outcome of more recently completed audits, and fee variations to be managed depending on whether they are driven by national or local factors.

Opting-in to a national scheme provides an opportunity to leverage economies of scale to ensure fees are as low as possible, whilst ensuring the quality of audit is maintained by entering into a large-scale collective procurement arrangement.

If the national scheme is not used some additional resource may be needed to establish an auditor panel and conduct a local procurement. Until a procurement exercise is completed it is not possible to state what, if any, additional resource may be required for audit fees for 2023/24.

(b) Risk Management

Recommendation from section 2 above	**Risks/Threats/ Opportunities**	**Current Controls**	**Using the Risk Management Matrix Score the risk**	**Future Controls**
opt into sector-led option for appointment of external auditors	The key risks are that the Council may fail to appoint an auditor in accordance with the requirements and timing specified in local audit legislation; or the Council is not able achieve value for money in the appointment process	The Council has previously opted in the scheme during the last appointing period to mitigate against these risks	8 (Financial and Regulatory risk – Marginal impact, significant probability)	It is recommended that the Council opt into the sector-led option for this appointing period to mitigate against these risks

(c) Human Rights Act and Other Legal Implications

Section 7 of the Local Audit and Accountability Act 2014 requires a relevant Council 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 Council must consult and take account of the advice of its auditor panel on the selection and appointment of a local auditor. Section 8 provides that where a relevant Council is a local Council operating executive arrangements, the function of appointing a local auditor to audit its accounts is not the responsibility of an executive of the Council under those arrangements.

Section 12 makes provision for the failure to appoint a local auditor: the Council must immediately inform the Secretary of State, who may direct the Council to appoint the auditor named in the direction or appoint a local auditor on behalf of the Council.

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.

Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to accept the formal invitation to opt in to PSAA for the appointment of the Council's external auditors must be made by a meeting of the Council (meeting as a whole).

(d) Equalities Impact Assessment

There are no direct equalities implications in this report.

5. Supporting Information

5.1 Introduction

5.1.1 The Council opted into the national arrangement for the procurement of external audit led by PSAA. The arrangement was for a period of five years starting from 2018/19 and is due to end in 2022/23.

5.1.2 The process for retendering for external audit in local authorities in England, for contracts due to start from 2023/24, is now underway and the Council will need to decide whether to procure its own external auditor or opt into the national procurement framework again.

5.1.3 Legislation requires a resolution of Full Council if a local authority wishes to opt into the national arrangement. The deadline for this decision is 11th of March 2022. If the Council doesn't make such a decision, the legislation assumes that the Council will procure its own external audit, with all the extra work and administration that comes with it.

5.2 Background

5.2.1 The Local Audit and Accountability Act 2014 (the Act) 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 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.

5.2.2 The Act also set out the arrangements for the appointment of auditors for subsequent years, with the opportunity for authorities to make their own decisions about how and by whom their auditors are appointed. Regulations made under the Act allow authorities to 'opt in' for their auditor to be appointed by an 'appointing person'.

5.2.3 In July 2016, Public Sector Audit Appointments Limited (PSAA)[1] were specified by the Secretary of State as an appointing person under Regulation 3 of the Local Audit (Appointing Person) Regulations 2015. The appointing person is sometimes referred to as the sector led body and PSAA has wide support across local government. PSAA was originally established to operate the transitional arrangements following the closure of the Audit Commission under powers delegated by the Secretary of State.

5.2.4 Acting in accordance with this role, PSAA is responsible for appointing auditors and setting scales of fees for relevant principal authorities that have chosen to opt into its national scheme, overseeing issues of auditor independence and monitoring compliance by the auditor with the contracts they enter into with the audit firms.

5.3 Current audit arrangements

5.3.1 In 2017, PSAA invited the Council, along with all other authorities, to opt into the national procurement scheme so that they could enter into contracts with appropriately qualified audit firms and appoint a suitable firm to be the Council's auditor.

5.3.2 The Council, along with 98% of local authorities invited, opted into the national arrangement and Grant Thornton were appointed as the Councils external auditors for the five-year period from 2018/19 to 2022/23.

5.4 Sector issues

5.4.1 Much has changed in the local audit market since audit contracts were last awarded 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.

[1] PSAA is an independent, not-for-profit company limited by guarantee and established by the Local Government Association in August 2014.

5.4.2 Since the contracts were awarded, a series of financial crises and failures in the private sector led to questions about the role of auditors and the focus and value of their work. In rapid succession we have then had the results of four independent reviews commissioned by Government:

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

5.4.3 The four reviews set out more than 170 recommendations which are now in various stages of consideration by Government with the clear implication that a series of significant reforms will follow. Indeed, in some cases where new legislation is not required, significant change is already underway. A particular case in point concerns the FRC, where the Kingman Review has inspired an urgent drive to deliver rapid, measurable improvements in audit quality. This has already created a major pressure for firms and an imperative to ensure full compliance with regulatory requirements and expectations in every audit they undertake.

5.4.4 By the time firms were conducting 2018/19 local audits, the measures which they were putting in place to respond to a more focused regulator, determined to achieve change, were clearly visible. In order to deliver the necessary improvements in audit quality, firms required their audit teams to undertake additional work to gain higher levels of assurance.

5.4.5 However, additional work requires more time, posing a threat to a firms' ability to complete all of their audits by the target date for publication of audited accounts (then 31 July) – a threat exacerbated by growing recruitment and retention challenges, the complexity of local government financial statements and increasing levels of technical challenges as local authorities explored innovative ways of developing new or enhanced income streams to help fund services for taxpayers.

5.4.6 This risk to the delivery of timely audit opinions first emerged in April 2019 when one of PSAA's contracted firms flagged the possible delayed completion of approximately 20 audits. Less than four months later, all firms were reporting similar difficulties, resulting in only 57% of audits being completed by the target date of 31 July 2019.

5.4.7 2019/20 and 2020/21 audits have faced even greater challenges. With Covid-19 also impacting, unprecedented challenges faced by the sector. Only 45% of 2019/20 audits were completed by the target date of 30 November 2020 and 9% of 2020/21 audits completed by the target date of 30 September 2021.

5.4.8 Delayed opinions are not the only consequence of the FRC's drive to improve audit quality. The additional work has resulted in more fee variation claims being received than in previous years and therefore additional costs incurred by individual local authorities. However, regardless of the additional costs incurred by individual local authorities by way of fee variations, the PSAA led scheme has significantly reduced the cost of local audits on a national level.

5.4.9 None of these problems are unique to local government audit. Similar challenges have played out in other sectors, where increased fees and disappointing responses to tender invitations have been experienced during the past two years.

5.5 Options for future audit arrangements

5.5.1 With the current audit arrangements coming to an end, the Council has three options:

i. **Individual procurement** – to undertake a complete procurement process itself and appoint its own auditor, or

ii. **Joint procurement** – undertake a joint procurement with other bodies, or

iii. **National scheme** – to opt into a national collective scheme that PSAA is developing.

Option 1 – Individual procurement

5.5.2 The option to undertake an individual procurement will require the time, effort and skill of having to undertake a procurement and appointment process. It will also involve specifying the service required, inviting tenders, evaluating tenders.

5.5.3 There would also be a need to establish an independent auditor panel. In order to make a stand-alone appointment the auditor panel would need to be set up by the Council itself. The members of the panel must 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 family and friends.

<u>Advantages</u>

- Provides the Council with the independence to select a supplier itself.

<u>Disadvantages</u>

- Will not benefit from the opportunities that may be available through joint or national procurement to significantly influence quality and price

- Elected members will not have a majority input to assessing bids and choosing which audit firm to award a contract for the Council's external audit

- The costs of recruitment and servicing of the Auditor Panel, running the procurement exercise and negotiating and managing the external audit contract would be borne by the Council

- There are only nine accredited local audit firms, so we would be drawing from the same limited supply of audit resources as PSAA's national procurement.

Option 2 – Joint procurement

5.5.4 The Council would be able to join with other authorities to establish a joint Auditor Panel. As stated above, this will need to be constituted of wholly or a majority of independent appointees (members). At this stage it is unclear whether many of our local neighbouring boroughs are likely or not to opt in to the PSAA collective arrangement and would thus be inclined to join a smaller local joint procurement.

<u>Advantages</u>

- The costs of recruitment and servicing of the Auditor Panel, running the procurement exercise and negotiating and managing the external audit contract shared between the participating authorities

- Greater opportunity for achieving economies of scale by being able to offer a larger combined contract value to the firms.

- Would give the authorities a more direct relationship with the audit firm

<u>Disadvantages</u>

- The Panel will be appointed by all partner authorities not just by the Council thus reducing local input.

- Appointing an auditor could be complicated where the preferred auditor has a conflict of interest in relation to one of the appointing councils but not the others.

- There are only nine accredited local audit firms, so we would be drawing from the same limited supply of audit resources as PSAA's national procurement.

Option 3 – National scheme

5.5.5 The Council could opt into the PSAA led national procurement

Advantages

- There will be no need for the Council to establish alternative appointment processes locally, including the need to set up and manage an auditor panel.

- It is expected that the large-scale contracts procured through PSAA will bring economies of scale and attract more competitive prices from the market than a smaller scale procurement, although it is widely expected that audit fees at their current level are not sustainable and therefore will increase.

- The overall procurement costs would be expected to be lower than an individual smaller scale local procurement.

- The overhead costs for managing the contracts will be minimised though a smaller number of large contracts across the sector.

- PSAA will monitor contract delivery and ensure compliance with contractual requirements, audit quality and independence requirements; and

- Any auditor conflicts at individual authorities would be managed by PSAA who would have a number of contracted firms to call upon;

Disadvantages

- Elected members will have little or no opportunity for direct involvement in the appointment process other than through the LGA and the stakeholder representative groups.

- In order for PSAA to be in the strongest possible negotiating position they will need Councils to indicate their intention to opt-in before final contract prices are known

6. Comments of Other Committees

This report was considered by the Audit & Corporate Governance Committee on 9th December 2021 which agreed to make the recommendation as set out in Section 2 of the report.

The report was also considered, for information, at the Cabinet meeting held on 21st February 2022.

7. Conclusion

This report has explored the options available to the Council in appointing an external auditor for the five-year period from 2023/24 and concludes that a sector-wide procurement led by PSAA would produce better outcomes and will be less burdensome for the Council than an individual or joint procurement on the basis that:

- Collective procurement would reduce costs for the sector and for individual Councils compared to smaller local procurements.

- PSAA provides the best opportunity to secure the appointment of a qualified, registered auditor as there are only nine accredited local audit firms, and a local procurement would be drawing from the same limited supply of audit resources as PSAA's national procurement.

8. **Background Papers**

None