

**Agenda Item No:** 8

**Report To:** **AUDIT COMMITTEE**

**Date:** **27 June 2011**

**Report Title:** **Future of local public audit – response to CLG consultation**

**Report Author:** Paul Naylor, Deputy Chief Executive



**Summary:**

Following the Secretary of State for Communities and Local Government's decision to abolish the Audit Commission CLG launched a consultation on future proposals at the end of March. Consultation extends to the end of June. The former Audit Committee was briefed and considered a preliminary response which was then the subject of a briefing with new Audit Committee members earlier this month and with the Parish Forum in April. Following consultation with the Chairman and Vice Chairman of this committee the response attached at **Appendix A** was submitted to the CLG on 21 June. Any amendments from this committee will be submitted to CLG separately. The proposals will allow the council to appoint its own external auditor, which is not contentious, and contains many proposals of a technical and regulatory nature. However, it contains proposals for the structure of Audit Committees which were contentious with Members and implications for parish councils that could give rise to an added cost burden. **Appendix B** is a more recent letter from the CLG Permanent Secretary that explains the determination of government to outsource the Audit Commission by April 2012. There is still some speculation as to when all the new responsibilities for external audit will come into being.

**Key Decision:** No

**Affected Wards:** None specifically

**Recommendations:** **The Audit Committee is asked to consider and endorse the response made to the CLG about the future for local external audit, subject to any amendments from the committee being reported to CLG before the close of the consultation on 30 June.**

**Policy Overview:** Strong and transparent local governance including accountability for financial resources, value for money and probity are fundamental to the proper working of local government. The external audit function acts as a watchdog to provide assurance to Members and residents. The CLG's proposals are founded on design principles that underpin this requirement.

<b>Financial Implications:</b>	None at this stage
<b>Other Material Implications:</b>	Not applicable at this stage
<b>Background Papers:</b>	CLG consultation paper, 'The Future of Local Public Audit' – March 2011 Report to Audit Committee 21 April 2011
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## **Report Title: Future of local public audit – response to CLG consultation**

### **Purpose of Report**

1. To endorse the response, at **Appendix A**, submitted on 21 June 2011 to the Department for Communities and Local Government (CLG) regarding its consultation on the Future of Local Public Audit (external audit).
2. Members should note that the CLG proposals will, if followed through, fundamentally change the composition and role of the Audit Committee from some time either in or after 2013.

### **Decision Required**

3. The Committee is asked to endorse the response made to the CLG about the future for local external audit, subject to any amendments from the committee being reported to CLG before the close of the consultation on 30 June.

### **Background**

4. The Audit Commission (AC) is responsible for conducting the financial audit of local authority accounts and for reviewing a council's value for money arrangements. The AC is the commissioner of all external local authority audits, and undertakes 70% of audits itself. The balance is awarded to the private sector, but tendered and awarded by the AC.
5. The Secretary of State for Communities and Local Government decided in 2010 to abolish the Audit Commission (although it will continue to operate through 2011/12 and possibly up to 2013/14 or beyond) and since the end of March has been consulting on options for future arrangements. This Committee has received briefings from our external auditor about the process.
6. The consultation runs to 54 pages and raises 50 main questions for the consultees to consider. Many are of a technical and regulatory nature, but there are some issues that affect councils more fundamentally; these are highlighted later in this covering report to the response.
7. Please note that at a meeting of the former Audit Committee on 21 April, Members then received a report about the consultation and gave a preliminary view on responses. Since then, the Deputy Chief Executive has written to all parish councils about the proposed responses to those issues that are relevant to parish councils. This followed a briefing to the Parish Forum in April.
8. On 7 June, some members of the new Audit Committee were present at an induction session, when a further briefing about the consultation was provided. It was decided then that subject to further consultation with the Chairman and Vice-Chairman the council's response should be submitted to CLG before this Committee meeting, as the consultation period closes on 30 June. If any changes to the attached response are necessary following this meeting, these will be relayed to CLG before the deadline.

## The main issues

9. To assist Members, the main issues are set out below, and are referenced to the council's response. The consultation paper itself is available through the following link –  
[www.communities.gov.uk/publications/localgovernment/localpublicauditconsult](http://www.communities.gov.uk/publications/localgovernment/localpublicauditconsult)
10. The Secretary of State's main aims are to:
  - Disband the Audit Commission and transfer the work of the Audit Commission's in-house audit service to the private sector (which may include a mutual organisation formed by former Audit Commission staff) – this aim was reaffirmed more recently in a letter to all local authorities from the CLG Permanent Secretary (a copy of the letter is attached as **Appendix B**);
  - Enable local authorities to appoint their own independent external auditors;
  - Provide an alternative for the external audit of smaller public bodies (e.g. parish councils);
  - Make audit committees statutory and create effective independent assurance;
  - Provide new arrangements for the audit of local health bodies (not a significant issue for ABC), and
  - Ensure that all local public bodies are still subject to robust auditing.
11. The underlying approach to the change is to adopt external audit practices to meet the specific requirements of local government, but that follow similar principles to the external audit of the private sector and other parts of the public sector.
12. The consultation covers:
  - Scope and Principles for external audit
  - Regulation of local public audit
  - Commissioning local public audit services
  - Scope of audit and the work of the auditors
  - Arrangements for smaller bodies.
13. The main issues from each of the sections are outlined below.

## Scope and Principles

14. CLG proposes that the National Audit Office should in future be responsible for a Code of Audit Practice that governs the approach taken by the auditors. CLG also propose that registration of audit firms and monitoring and enforcement of audit standards be undertaken by the professional accountancy bodies under the supervision of the Financial Reporting Council.
15. The design principles used by the CLG to develop the new approach are:
  - localism and decentralisation – freeing up local public bodies, subject to appropriate safeguards, to appoint their own independent external auditors from a more competitive and open market, while ensuring a proportionate approach for smaller bodies

- transparency – ensuring that the results of audit work are easily accessible to the public, helping local people to hold councils and other local public bodies to account for local spending decisions
- lower audit fees – achieving a reduction in the overall cost of audit
- high standards of auditing – ensuring that there is effective and transparent regulation of public audit, and conformity to the principles of public audit

16. Our response agrees that the design principles are appropriate, but we make the point that some of the later proposals from CLG are not entirely consistent with some of the principles.

### **Regulation of local public audit**

17. Regulation and supervision of external auditors is necessary and here the CLG main proposals include:

- the National Audit Office being responsible for an external audit Code of Practice and supporting guidance to be used by local public auditors;
- the Financial Reporting Council acts as the regulator for local public audit
- auditors must be members of recognised supervisory bodies (the main accountancy institutes) and eligible for appointment under the rules of that body;
- supervisory bodies will be responsible for monitoring the quality of audit work, investigating complaints and disciplining their members. They could also stop an unsatisfactory firm from being eligible for appointment.

18. In essence, there will be a list of audit firms recognised as being qualified to undertake public audit work.

19. The proposals in this section are supported.

### **Commissioning local public audit services**

20. CLG proposes that external auditors should be appointed by the audited body (the full council in our case) who will receive the advice of an audit committee. It is proposed that residents should have an opportunity to input to the decision-making process.

21. Councils may choose to jointly appoint an auditor if that were their wish. In the event that a council fails to appoint an auditor then the Secretary of State may either have the power to direct the council to appoint an auditor, or may have the power to appoint one himself.

22. Auditors could be appointed for 5 years, with one renewal, but CLG suggest that after 10 years a new firm must be appointed. There are also safeguards in place for the dismissal or resignation of auditors. The first point was not accepted by the former Audit Committee, which suggested that it was more important for an 'audit manager' to be rotated than an audit firm. This point is built into our response.

23. This section of the consultation also sets out the CLG's proposals for the composition of audit committees for local government. This is likely to be the most contentious element for Members and our response makes clear that the council disagrees with the basic proposition.

24. It is proposed that audit committees should be made statutory (this point is supported), but it be made mandatory for committees to include a majority of non-elected members who can only be considered if:
- they have not been a member or an officer of the local authority/public body within five years before the date of the appointment
  - they are not a member or an officer of any other relevant authority
  - they are not a relative or a close friend of a member or an officer of the body/authority
  - they have applied for the appointment
  - their appointment is approved by a majority of the members of the council
  - the position has been properly advertised
25. CLG also proposes that:
- the chair and vice-chair of the authority would be non-elected representatives
  - elected members on the audit committee should be non-cabinet members with at least one (and ideally one third of all members) having recent and relevant financial experience
26. Finally, this section also considers the **role** of an audit committee. Two options are outlined. The first takes a narrow approach and considers the audit committee having one mandatory duty, which is to advise council on the appointment or removal of an auditor.
27. The second option would be a wider and more detailed mandatory role covering:
- providing advice to the full council on the procurement and selection of their external auditor
  - setting a policy on the provision of non-audit work by the statutory auditor
  - overseeing issues around the possible resignation or removal of the auditor
  - seeking assurances that action is being taken on issues identified at audit
  - considering auditors' reports
  - ensuring that there is an effective relationship between internal and external audit
  - reviewing the financial statements, external auditor's opinions/conclusions and reports to members and monitoring management action in response to the issues raised by external audit
  - providing advice to the full council on the quality of service they are receiving
  - reporting annually to the full council on its activities for the previous year
28. Our response based on previous discussions with Members disagrees with the mandation of non-elected representatives on the grounds that such prescription is unnecessary, not consistent with the principles of localism, counter to the role of democratically and accountable elected Members and presumes that Members are unable to act impartially, and a concern that audit committees may become dominated by personalities with professional or personal interests.

## Scope of audit and the work of the auditors

29. This section offers four options for the potential scope of external audit work.

Option 1 (limited scope) - *The auditor would:*

- give an opinion on whether the financial statements (its annual accounts) give a true and fair view of the audited body's financial position and of its income and expenditure
- review, and report on as appropriate, other information published with the financial statements, including the statement on internal control/annual governance statement, the remuneration report and the whole of government accounting summarisation schedules.

This option would reduce the information available to local citizens on how local bodies are spending their money or on whether bodies are securing value for money. However, this option is similar to the practice of external audit for the private sector and would drive the greatest reduction in audit fees.

Option 2 - *This option is the same as option 1, but in addition the auditor would:*

- provide a conclusion as to whether it has the proper arrangements in place to secure value for money (based on locally defined policy priorities) having regard to specified criteria (including financial resilience and regulatory and propriety)

Option 3 - *This option is designed to provide stronger assurances on the way local public bodies spend money and is similar to the current scope. Under this option, the auditor would still give an opinion on the financial statements, but would provide conclusions on:*

- regularity and propriety – a conclusion on compliance with relevant laws and regulations and the audited body's governance and control regime
- financial resilience – a conclusion about the future financial sustainability of the audited body and
- value for money – in addition to proper arrangements in place to secure value for money, a conclusion about the achievement of economy, efficiency and effectiveness within the audited body

Option 4 - *Under this option, all local public bodies would be required to produce an annual report and to publish this report on their website. The report would set out the arrangements the audited body had put in place to secure value for money, whether they had achieved economy, efficiency and effectiveness, regularity and propriety and financial resilience. Auditors, in addition to Option 3 would provide an opinion on the annual report.*

30. Discussion with Members previously indicated a strong preference for Option 2 as a mandatory scope, leaving councils the discretion to widen this if that were their wish.

### **Arrangements for smaller bodies (e.g. parish councils)**

31. The CLG's proposals in this section will affect all parish councils where different arrangements are proposed for local public bodies with income and expenditure of less than £6.5m per annum.
32. The arrangements group local public bodies according to scales of income or expenditure bands.
33. CLG proposes that county councils (either their s151 officer or full council) would appoint an 'independent examiner' (IE) to conduct a more limited audit for each town or parish council in their area. CLG say it would be possible for the IE to be an officer of the county council.
34. District Councils are not given any role in these arrangements. In the case of Kent, the county council could have to appoint circa 300 IEs to the various town and parish councils.
35. Following discussion at our Parish Forum in April and the Member briefing earlier this month there was support for our response suggesting the commissioning role be carried out by Districts, with the ability for Districts internal audit teams to perform a limited external audit for parish councils. Understandably, parish councils were concerned about the potential cost implications of IE if undertaken by private firms. We have copied our draft response to all parish councils in the borough and any comments received will be reported to the committee.

### **Portfolio Holder's Views (Councillor Robert Taylor)**

36. Endorsing the response is a matter for the committee's consideration though I support it in the interests of good local governance. It is good that Members have had an earlier opportunity to consider the consultation and we are consulting our parish councils. The response is consistent with the earlier views of Members and parish council representatives.

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## Ashford Borough Council

## CLG Consultation – ‘Future of local public audit’

## Responses to the detailed ‘50’ questions

Q No.	Issue	Suggested Response
1	<b>Design principles</b>	The principles are sound. However, it is this council’s view that the consultation paper falls short of meeting some of those principles. In particular it is felt the principle of ‘localism’ is compromised by the preferences displayed over the proposals for audit committees and the prescription that non-elected representatives should form most of an audit committee’s members. This is unnecessary and a step too far, a point this response expands on later. The aim that councils and other audit bodies should receive better value for money and audit services at less cost is fully supported. However, neither the council nor our local parish council representatives are confident the proposals will achieve this aim at local level.
2	<b>Probation Trust audits</b>	Yes, the council agrees.
3	<b>Who should produce a Code of Practice?</b>	Yes, the council believes the National Audit Office is the most suitable organisation to produce a Code of Practice.
4	<b>Registration of auditors</b>	Yes
5	<b>Who should maintain register of statutory local public auditors?</b>	The council believes the Financial Reporting Council should maintain and review the register of statutory local public auditors.
6	<b>Balancing audit experience with entry to the audit market</b>	There is an inevitability that local public audit will be dominated by the larger private audit firms. This council hopes the Audit Commission’s proposals for a staff mutual will be supported by Government as it potentially offers an important counterbalance, plus a means of keeping experience of the public sector developed over many years. Any new firms entering the market

		<p>must demonstrate their ability through their track record in other audited sectors and through their structures, qualification and skills of their staff. Firms must also display a sound awareness of the principles of public audit. Local authority audit (even if restricted to audits of the financial statements) can be complex and involve accounting not found in the commercial sector. It is accepted this may count against new and smaller audit firms, but it is assurance and public accountability that matters most.</p>
7	<p><b>Any additional criteria for the appointment of audit firms?</b></p>	<p>Apart from relevant experience and knowledge of the financial frameworks governing local authorities, the council believes that auditors must have a good understanding of the local context of a local public body. This council's audit committee and its members have welcomed auditors' assurances and comments in the knowledge that auditors have full understanding of the local context. We do not believe this requirement would unfairly restrict the market. We believe audit firms must be expected to familiarise themselves with the local context of a prospective client when expressing an interest in contracting for its audit work.</p>
8	<p><b>Public interest entity – definition</b></p>	<p>The council's view is that all principal authorities (districts, counties, unitary councils and metropolitan authorities) should be classed as 'public interest entities', and auditors of those bodies should be regulated by the Financial Reporting Council on the same basis as for public interest entities in the private sector</p>
9	<p><b>PIE – any additional regulation?</b></p>	
10	<p><b>Role of regulator in relation to any local bodies treated as PIEs?</b></p>	
		<p>Additionally, the council suggests that arms length companies where councils have a controlling interest or significant influence should also potentially fall within the public interest entity classification, subject to meeting tests relating to their size and scale of operation.</p> <p>We feel the above will help ensure audit quality and professional standards, which will be vital in any new audit regime.</p>
11	<p><b>Joint procurement of auditors</b></p>	<p>Yes, the council believes the proposals provide enough flexibility in principle for collaboration and joint procurements by local public bodies.</p>
12	<p><b>Criteria for independent members</b></p>	<p>Members view the proposals for compulsory non-elected full members on audit committees as an unnecessary step. The council believes insufficient evidence has been gathered about the role and effectiveness of audit committees currently within local government. However, the council</p>

		<p>supports the notion that non-elected members can bring a measure of independence and experience that elected members may not have. Currently some councils use their discretion to appoint non-elected representatives as either full or co-opted members of audit committees. Our members believe this flexibility should be retained, but given more emphasis in statutory guidance. Elected members are publicly accountable and are concerned that non-elected representatives as full audit committee members inevitably would lack this important characteristic. However, members see strong potential and justification for non-elected representatives to engage in audit committees as co-opted members bringing important experience and independent insight to the work of audit committees. Accordingly, members of this council would prefer the flexibility to appoint a number of co-opted (non-voting) non-elected representatives up to a maximum of one-third of the audit committee full membership (rounded up). It is considered a minimum statutory requirement for at least one non-voting co-opted member should apply. Co-opted non-elected members should be considered for their particular experience in relevant fields of audit work, whether this be financial audit, risk management, procurement etc. To ensure transparency and to increase opportunity for involvement the council would support a requirement for open appointments to co-opted representatives.</p>
<b>13</b>	<b>Skills for independent members</b>	<p>Yes, and building on our response to Question 12 the council believes it is necessary for non-elected representatives serving on audit committees to have relevant expertise (even following the council's preference for co-option). It is most likely this will include financial skills and experience, but could also include other skills and experience relevant to the full scope of an audit committee's work.</p>
<b>14</b>	<b>Will independent member remuneration be needed?</b>	<p>At the numbers implied by the Government's preferred alternative, members feel this could present a big challenge for councils to source enough interest with the skills and experience needed. Again building on the council's response to Questions 12 and 13, and our preference for co-option of non-elected representatives, members feel their preferred option would provide greater prospects for sourcing enough numbers of non-elected representatives. It may not be straightforward however, and financial allowances are likely to be needed. The council believes allowances should be a matter for consideration by councils' Independent Remuneration Panels</p>

15	<b>Audit Committees</b>	<p>As covered in the council's responses to Questions 1 and 12 the council believes the Government's preference for a majority of non-elected members of audit committees is inconsistent with that principle. This is considered a step too far. In members' view the justification lacks any appreciation for the merits and performance of local authorities' audit committees as currently constituted.</p> <p>This council welcomes making audit committees a compulsory requirement for councils, but strongly believes that democratically elected members should form the nucleus of audit committees.</p> <p>Repeating a point made in our response to Question 14 the council suggests co-option for one non-elected representative should be made the statutory minimum requirement with the flexibility to appoint more as councils see fit for their circumstances.</p> <p>As a result, therefore, the council is not able to support the options listed in Paragraph 3.9, though, we repeat, the council agrees with the principle of non-elected member representation on audit committees.</p> <p>The council does not believe that its preference for constituting audit committees will weaken the 'independence' of the relationship between the external auditor and the audited body. That is not our experience so far and we see no reason why this should be affected after decentralising external audit.</p> <p>Even following the council's preference, appointment of the auditor would be achieved through a recommendation of the audit committee (with some non-elected representation) to the Full Council. Both at full council meeting and in the process leading up to the recommendation it should be a requirement that opportunities are created for public involvement and questioning, as well as debate if needed.</p>
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<b>16</b>	<b>Audit Committee roles</b>	The council supports Option 1. We support the ability for councils to use their discretion to widen the role after considering how aspects of assurance work fit with other parts of a council's governance framework (for example the role of overview and scrutiny).
<b>17</b>	<b>Are the roles appropriate?</b>	Yes the roles are appropriate. As stated in our response to Question 16 the council supports Option 1, but that legislation should provide the discretion for councils to widen the role as they think fit.
<b>18</b>	<b>Should Code specify how auditors are appointed?</b>	Yes, and the council believes the NAO should maintain the Code
<b>19</b>	<b>Public involvement in auditor appointment</b>	Yes, the Council supports the proposal for public involvement.
<b>20</b>	<b>Public involvement for other public bodies</b>	Noted
<b>21</b>	<b>Failure to appoint an auditor</b>	Option 2 is supported by the council. The S151 Officer, through an amendment to the Accounts and Audit Regulations, should have the responsibility to ensure the council makes the appointment and that this be made by Full Council and reported accordingly.
<b>22</b>	<b>Duty to inform when auditor appointed</b>	Yes, the council agrees it will be necessary for local public bodies to inform a body of the appointment. If not the Secretary of State's role to step in and appoint an auditor would be impossible to perform. A variation on this would be to place the responsibility to inform Government of a failure to appoint with the Section 151 officer.
<b>23</b>	<b>Who is informed?</b>	Yes, the relevant Government department; CLG in the case of local authorities.
<b>24</b>	<b>Rotation of audit firms</b>	The council has a preference for the ability to maintain a relationship with its external auditor beyond ten years if it is satisfied that the relationship is sound. Therefore Councils should have this discretion, but it is this council's view that rotation of audit managers is a more relevant matter.
<b>25</b>	<b>Are current ethical standards for rotation sufficient?</b>	Yes, the council believes the current ethical standards provide enough safeguards.

26	<b>Requirement to change audit firm after two terms (ten years)</b>	See response to Question 24, where the council does not favour compulsory rotation of audit firms after two terms. Instead the council favours a discretion to do this linked to the compulsory rotation of audit managers within serving audit firms.
27	<b>Resignation and removal of auditors</b>	Yes, the council is satisfied the proposed process is suitable and provides acceptable safeguards for auditors and their clients.
28	<b>Safeguarding against auditors unreasonably limiting their liability</b>	In the absence of a central body providing indemnities to auditors it is right that statutory provisions should seek to prevent auditors from unreasonably limiting their liability to a client. However, we see that auditors' risks will be passed on in extra indirect costs and lead to increases in audit fees generally.
29	<b>Scope of audit work</b>	The council favours Option 2 as members regard with high importance the need for an external audit judgement on value for money. However, this council feels that external auditors should also have a role in advising audited bodies about the effectiveness of their internal audit functions. A narrow audit of financial statements may achieve financial savings, but members are concerned that wider assurance to residents and local taxpayers on matters about value for money and governance may suffer as a result.
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34	<b>Public interest reporting</b>	Yes, the council believes it is necessary to retain the ability for auditors to report in the public interest. The council does not feel an auditor's independence would be compromised as a result; subject to the safeguards referred to elsewhere in the consultation paper.
35	<b>Provision of non-audit services</b>	Yes, the council believes it would be proper for audit committees to consider any proposal to use the auditor for any out-of-audit scope work. Councils should be advised to follow their procurement arrangements and standing orders so as not to limit the ability for other firms to be
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		invited. The Council may choose to limit the volume and value of non-audit services to ensure that this is not seen to impact on the need for independent audit.
37	<b>Public interest disclosure – ‘whistleblowing’</b>	Yes, the council believes that both the audit firm and audit committee should be appointed as ‘prescribed persons’ under the Public Interest Disclosure Act.
38	<b>Transparency – modernising the public’s right to object to the accounts</b>	Yes, the council believes modernising a right first introduced 150 years ago is long overdue. We agree that transparency and the Fol Act provide many opportunities for residents to seek information and raise concerns. It is also reasonable for auditors to be within the scope of the Fol Act, subject to limiting the scope to the audit work for a local public body. However, the council does have some concerns about the implications for audit fees, and whether in practice modernising the ‘right to object’ results in more work for auditors rather than less.
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42	<b>Audit arrangements for smaller public bodies – eg. Parish councils. Which option would the council support?</b>	<p>Parish councils consider the ‘limited audit regime’ carried out by the Audit Commission works well and involves minimal cost. Please note that currently most parish councils in this borough typically incur an audit fee of about £140.</p> <p>The view of the council and of a majority of local parish councils is that independent examination has many merits, but there is a fear this would lead to higher costs. Parish councils, in particular, anticipate substantial percentage increases in audit fee costs, if fee-based independent examination were to become the norm.</p> <p>Ignoring the largest and the smallest parish councils within this borough, the typical average <u>precept</u> for a parish council is about £17,000, with audit fees typically representing about 1% or less of total costs. There is a worry this percentage may rise to 3-4%.</p> <p>It is accepted that full audit for most parish councils is not suitable or needed, but that parish councils should have the discretion to make this decision, however.</p>

		<p>To help reduce unavoidable fee increases the borough council proposes a proportionate system of independent examination that largely follows the current method of limited audit regime undertaken by the Audit Commission. In the same way that limited audit is carried out as a desk-top review by the Audit Commission, a similar approach could be carried out by districts' or county councils' internal audit teams. This arrangement should also permit joint involvement of audit teams.</p> <p>Using internal audit teams would be an alternative to sourcing independent examiners for each parish council audit. Although internal audit teams are small, we consider district and borough council audit teams have the skills, capacity and necessary understanding to cope well with a desk-top review of parish councils' financial statements. The format of material for presentation should be standardised, however.</p> <p>Fees chargeable by internal audit teams could be at marginal additional cost and would be expected to be significantly less than may otherwise be charged if independent examination leads to private sector audit firms being commissioned (even small practices) or fee scales developed for or sought by individuals appointed to carry out the work.</p>
43	<p><b>Should the county council (or unitary) commission independent examiners for small bodies?</b></p>	<p>Ashford Borough Council does not agree that county councils are best placed to perform this role as it could be burdensome role given the numbers of parish councils here in Kent (+300). Borough and District councils should be considered as commissioners given their likely greater contact with and awareness of local parish councils' work and circumstances. Inexplicably this option is not mentioned in the consultation paper.</p> <p>However, the council sees parish councils themselves having involvement with the commissioning process, for parish councils may wish to propose suitable people or firms for consideration. Indeed and in answer to the point raised in Question 45 the council believes it could be appropriate for parish councils who wish to perform the commissioning role to do so and use a district council's audit committee for this purpose.</p>



		<p>The council believes that district and borough councils' section 151 officers could perform the commissioning role acting on advice from their audit committees.</p> <p>Following from the council's response to Question 43 we believe it should be possible for the commissioning body to appoint its own internal audit team (we accept this is an option mentioned in the consultation paper, though this may be referring to county council internal audit). However, commissioning and potential appointment of an internal audit team should follow full consultation with parish councils and be subject to internal audit teams satisfying relevant criteria for appointment.</p>
44	<b>What guidance is required to commissioning bodies for IE appointments</b>	The council believes the NAO should produce and maintain guidance, though much of this is in place as reflected in the consultation paper. The annual return requirements from parish councils could mirror the arrangements currently in place from the Audit Commission.
45	<b>Parish councils appointing an IE</b>	This council believes that parishes that wish to appoint an IE should have the ability to do so, but be expected to use a district council's audit committee to preserve oversight. There are likely to be some smaller parish councils that may not have the capacity or experience to carry out this role and in these cases may look to a district council for advice and to make an appointment on their behalf. The council believes that only some parish councils would have the capacity and scale of work to create and justify an audit committee.
46	<b>Are there other options to ensure independence?</b>	Please refer to our response to Question 42. The council considers its suggestion of a hybrid (adopting the style of the current limited audit regime with aspects of independent examination, possibly then carried out by a district council's internal audit team) is a practical alternative and offers another choice to ensuring independence.
47	<b>Is the four-level approach to IE too complex?</b>	<p>No, it is not too complex. Again the council would suggest that borough and district councils are involved in commissioning rather than county councils in two-tier areas.</p> <p>However, the suggestion that a principal council's officer may act as an IE for say a parish council needs qualifying in our view. Given that many principal councils support local parish councils to</p>

		<p>varying degrees, a position that can only increase under localism, it would be essential for principal councils to display independence if involved in the audit of parish councils' financial statements.</p> <p>Again following from the response to Question 42 the council feels independence by a principal council would be best achieved through using the resources of internal audit teams to conduct an independent examination.</p> <p>For the higher levels of IE the council believes it is necessary for the IE to hold a relevant professional qualification and be experienced in financial or audit work. Internal audit teams would qualify against these criteria.</p>
<b>48</b>	<b>Public interest reporting for smaller bodies</b>	The council believes that matters of public interest about smaller public bodies should be raised with the audited body and a district council's audit committee. The district council's audit committee could decide whether to appoint an auditor to investigate the matter, and have the ability to decide any suitable conditions or sanctions for the smaller local public body.
<b>49</b>	<b>Objections to the accounts of smaller public bodies</b>	Subject to replacing district for county council, this council agrees the proposal is suitable.
<b>50</b>	<b>Regulatory regime for smaller bodies</b>	Subject to replacing district council for county council this council believes it would be appropriate for larger councils to act as the regulatory body for smaller public bodies.

*From the Permanent Secretary*

Local Authority Chief  
Executives

2 June 2011

Dear Local Authority Chief Executives,

#### **UPDATE ON WORK ON THE FUTURE OF LOCAL AUDIT**

In August last year the Secretary of State announced plans to disband the Audit Commission and refocus local public audit. Since then, the feedback from local government has been generally supportive of the decision. We have a shared goal of making progress on a robust new local audit framework, and on shutting down the Commission quickly and efficiently, so that local government can appoint auditors as soon as possible. I want to update you on what we are doing to secure this.

Since the announcement, we have been carefully considering how to deliver the changes as cost effectively and quickly as possible. We are out to consultation on proposals for the new audit framework, and keen to hear your views. The consultation runs until 30 June, and the document is at: <http://www.communities.gov.uk/publications/localgovernment/localpublicauditconsult> We plan to provide a response to the consultation in the autumn, and to publish draft legislation, and then to bring forward primary legislation as soon as Parliamentary time allows.

We have also been looking at how to transfer the audit work from the Commission's in-house audit practice to the private sector. We have taken external advice on how best to achieve this. We need to ensure the public purse is protected, and that you get high quality and value for money audit services until you can start appointing your own auditors.

There are two basic options, either to outsource all the audit work (30% of which is already done by the private sector), or to create an independent company which could be sold. Our initial view, drawing on the work of our external advisers, is that outsourcing could be the better option – potentially quicker, more straightforward and better value for money. We have, therefore, asked the Audit Commission to begin substantive preparatory work for outsourcing the 2012/13 audits. This means we will be able to move quickly if Ministers take a final decision to go down this route. The attached press notice provides more details.

We would ensure that local government is fully engaged in the process of outsourcing and the appointment of auditors. We will ensure that whichever option is chosen provides high quality and value for money. We expect local government to share in the benefit of any savings that are achieved. We are clear that outsourcing would not delay the point at which you are able to appoint your own auditors, compared with the sale option. My department is ready to work closely with local government and the Commission to ensure a smooth transition.

Once Ministers have made a final decision on how best to transfer the in house practice to the private sector, they will inform Parliament in the usual way. I will keep you informed of developments and the programme will be kept under review to ensure the best possible outcome.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Bob Kerlake'. The signature is written in a cursive style with a large initial 'B'.

**SIR BOB KERSLAKE**

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