

Agenda Item No:

Report To: **Audit Committee**

Date: **16th June 2016**

Report Title: Procurement and Appointment of External Auditors

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Portfolio Holder Cllr Shorter Portfolio Holder for Finance & Budget, Resource Management and Procurement



Summary: This is the third report to the committee updating them on the emerging picture for the procurement of an external auditor for the 2018/19 financial statements.

This is the first time that the Council has had the ability to appoint its own auditor, although this freedom will be restricted to appointing an auditor that is authorised by the Financial Conduct Authority.

There are three approaches to this procurement that are outlined in the paper and it recommends that the preferred option is to procure through a Sector Led Body.

Key Decision: Yes

Affected Wards: All

Recommendations: ii.

Policy Overview: The Councils contract with its External Auditor is due to expire, and it will need to appoint a new auditor before 31 December 2017. The new auditor will take on responsibility for examining the 2018/19 financial statements and deliver their first opinion in July 2019.

Financial Implications: The Audit contract is a significant contract with audit fees of circa £70,000. The procurement route for a new external auditor will impact upon the ability of this procurement process to extract the best value for this service.

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Report Title: Procurement and Appointment of External Auditors

Purpose of the Report

1. To inform the committee of the options it has for the appointment of the Councils External Auditor.

Issue to be Decided

2. To make a recommendation to Council on the procurement route for the Council's external auditor.

Background

3. At its meeting on the June 2015 the Audit Committee received a report on the future of local public audit. This reported Informed members of the arrangements that had been put in place following the dissolution of the Audit Commission.
4. In December 2015 the committee received a further report informing members of the Department for Communities and Local Government decision to extend the existing audit contracts by 1 year requiring Authorities to have procured and appointed an external auditor by the end of December 2017.

Options

5. Before considering the procurement options it is important to note that suppliers must be authorised by the Financial Conduct Authority to provide public audit services. Currently the following suppliers are so authorised and provide public audit services in local authorities.
 - a. BDO LLP (Currently auditing 39 authorities)
 - b. Ernst & Young LLP (Currently auditing 232 authorities)
 - c. Grant Thornton UK LLP (Currently auditing 265 authorities)
 - d. KPMG LL P (Currently auditing 218 authorities)
 - e. Mazars LLP (Currently auditing 40 authorities)
6. More providers may seek authorisation as procurement decisions move closer although it is unlikely that small local independent firms will be able to meet the criteria, therefore within this process it is important to acknowledge that the Councils choice of Auditor will be limited.

Solo Procurement and Auditor Panels

7. The Council could opt to take the decision to procure a new auditor alone. To do this the Council would have to establish an Auditor Panel as set out in the 2014 Regulations. The Panel must be independently chaired and contain a majority of independent members. The definition of 'independent' is established in regulations however to be independent a person must :
 - a. not be a councillor or officer of the authority or employed by a prospective auditor and has not been so for at least five years.
 - b. not be a relative or close friend of any serving councillor or officer.

8. Should the authority choose this route, the Auditor Panel could be entirely separate from the Council's committee structure or a sub-committee within its existing governance (for example a sub-committee of the audit committee). It must meet the composition requirements of the Regulations, including a majority independent members and chair. An Auditor Panel is an advisory body recommending actions to full Council, however the Council is not bound to follow its recommendation. Beyond the appointment of an auditor, the Auditor Panel should remain as a standing committee as it has other functions, including:
- Reviewing the Council's policy on obtaining non-audit services from the auditor,
 - Maintaining an independent relationship to the auditor,
 - Monitoring the quality and effectiveness of the auditor,
 - Considering any investigation into the circumstances of an auditor's resignation from office or any proposal to remove, and
 - Receiving any Public Interest Reports published by the auditor.
9. A summary of the advantages and disadvantages of the approach is outlined in the table below.

Advantages/Benefits	Disadvantages/Risks
Maximum (though not complete) control over auditor procurement.	Costs of recruiting and maintaining an <i>Auditor Panel</i> .
Ability to shape auditor requirements to local circumstances	May struggle to recruit sufficient independent members.
	Unlikely to achieve economies of scale.

10. This raises a question whether members would be comfortable with a panel of independent members making recommendations on the appointment of an auditor and overseeing some elements of the governance structure. Whilst it may be possible to recruit a panel of independent members this process would be resource intensive.
11. It also needs to be remembered that an Audit Panel would report directly to council and not through the Audit Committee and this could create some governance issues, especially with the overlap in responsibilities between the Panel and committee for the ongoing items that would be the with the Panels remit.
12. In addition to this it is uncertain whether the audit would be of a sufficient scale to achieve a competitive price and therefore this may result in an increase in the audit cost.

Joint Procurement

13. An alternative to the approach outlined above is that authorities can decide to ask the Auditor Panel of another authority to advise them (a joint procurement, but not a joint Panel). Joint panels need not be restricted by geography or sector (for instance, a joint panel with Police or Fire authorities could meet the requirements). However, the Auditor Panel will still require a majority of independent members.
14. A summary of the advantages and disadvantages of the approach is outlined in the table below.

Advantages/Benefits	Disadvantages/Risks
Spreads the cost of procurement	Some loss of local control of process
Potentially easier to recruit independent members	May encounter complexities if participants have differing procurement aims.

15. It is considered that a joint process is more likely to be able to attract independent members for an Audit Panel it does raise the issue that the panel will remain as a standing committee and therefore a third party body will be maintaining the relationship with the auditor and monitoring their performance and potentially be receiving public interest reports issued. This ongoing function may prove difficult to manage and not be attractive to the Council with this key governance function being operated by a third party.
16. The ability of the body to generate a contract of sufficient scale to achieve a competitive price will be dependent on the number of other authorities that can be encouraged to join the procurement process. A Kent wide body has been considered but this is not a preferred option.

Outsourced Procurement (the 'Sector Led Body')

17. The Secretary of State to authorise a Specified Person who would have the authority to make auditor appointment decisions on behalf of those authorities who opt-in to those arrangements. The regulations do not limit this to a single body however currently the Secretary of State has not made any authorisation and so at this time no Specified Person exists.
18. However, the Local Government Association (LGA) has been exploring the possibility of creating a Sector Led Body (SLB) that would seek authorisation to operate as a Specified Person. The LGA's explorations have included seeking initial feedback from authorities on whether they would be interested in making their procurement decision via an SLB. In a brief survey 58% of respondents reported an interest in the *Specified Person* route (the survey had only a 20% response rate).
19. Authorities that choose to procure via a Specified Person **do not** need to create or maintain an Auditor Panel. In this route, once full Council decides to opt-in, the Specified Person would negotiate contracts and make the

appointment on behalf of councils. The Specified Person would also take on all of the existing tasks of an Auditor Panel on behalf of the opted-in councils.

20. Under the 2015 Regulations, the decision of full Council to opt-in (or not) following invitation by a Specified Person is final. The Council will not have the option of waiting to see what deal the Sector Led body is able to achieve before deciding, nor can it leave the arrangement if it does not support the eventual appointment.
21. A summary of the advantages and disadvantages of the approach is outlined in the table below.

Advantages/Benefits	Disadvantages/Risks
Likely to deliver economies of scale.	Loss of local control of process
No requirement to run procurement exercise or create <i>Auditor Panel</i>	

22. Whilst there is some loss of control of the process this needs to be balanced against the reality of the level of choice that the authority would actually have in the appointment of its auditor. This route has the benefit of being a simplified process and one similar to the process that has been followed previously delivering a considerable reduction in the audit fees. We would need to be mindful of how the sector led body were to recover its costs and monitor the quality of the audit.

Equalities Impact Assessment

23. An EIA is not necessary at this stage.

Handling

24. The Audit Committee is asked to recommend to Council that the council's preferred route to procure an external auditor is through a sector led body.
25. Given the importance of this decision it is suggested that the committee put a report to cabinet highlighting the issue and seeking their endorsement of the recommended approach.
26. Officers will monitor any bodies that come forward and make recommendations on which body is the preferred option for the procurement of the Councils external auditor. A timetable is attached at **Appendix A**.

Conclusion

27. There are three possible routes to procure an external auditor for the council with the sector led body model being the preferred option.
28. The Committee will report to Cabinet with its recommendation to Council.
29. Officers will monitor progress on the development of a sector led body and make recommendations to the Council on the most suitable body to procure the external audit contract.

Portfolio Holder's Views

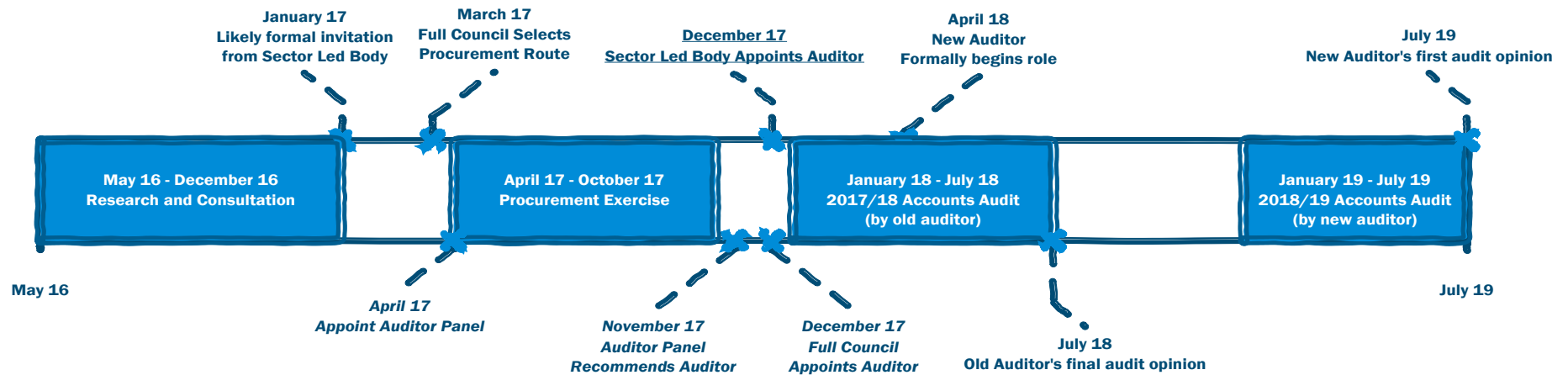
30. To be given at the meeting

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Appendix A - Next Steps

No action is required now. At this stage we ask the Committee to consider the options available and give their views in order to guide the detailed work that officers will then have to undertake. The timeline below sets out a likely way forward from this point.



Italicised events apply only with local procurement
Underlined events apply only with Sector Led Body Procurement