

<b>Report title:</b> National scheme for local auditor appointments	
<b>Report to Audit, Governance and Standards Committee</b>	
<b>Report author:</b> Nicole Wood, Executive Director, Corporate Services	
<b>Date of meeting:</b> 13 December 2021	<b>For:</b> Decision
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<b>Divisions affected:</b> All Essex	

## 1. Purpose of report

- 1.1 Public Sector Audit Appointments Limited (PSAA) is the body responsible for appointing an external auditor for each local authority that opts into its national appointing scheme. The PSAA has begun the process of retendering for external auditors for local authorities in England, for contracts due to start from **1 April 2023**. Hence, the purpose of this report is to consider whether the Council should opt into the PSAA's appointing scheme for external audit contracts due to start from **1 April 2023** or seek to procure its own external auditor from this date.

## 2. Recommendations

- 2.1 That the Committee recommends to Full Council that we opt into the PSAA's national procurement arrangement for auditor appointments for contracts due to start from **1 April 2023** and covering the audits of accounts for the financial years 2023/24 to 2027/28.

## 3. Background

- 3.1 The Council is required, in accordance with section 4 of the Local Audit and Accountability Act 2014 (the 2014 Act), to have its annual accounts audited by an auditor appointed in accordance with the provisions of the 2014 Act.
- 3.2 The Council has the option to:
- arrange its own procurement and make an auditor appointment itself or in conjunction with other bodies; or
  - join and take advantage of a national collective scheme for each appointing period.

- 3.3 Public Sector Audit Appointments Limited (PSAA) was designated by the Secretary of State in 2016 as an appointing person for principal local government and police bodies for audits, under the provisions of the 2014 Act and the Local Audit (Appointing Person) Regulations 2015 (the Regulations).
- 3.4 Acting in accordance with the role of appointing person, the PSAA is responsible for appointing an auditor and setting scales of fees for the duration of an appointing period for eligible bodies that choose to opt into its national scheme.
- 3.5 The Regulations require the appointing person to set the duration of each appointing period; the maximum duration is five years. The first appointing period spans the five consecutive financial years commencing 1 April 2018. It covers the audits of accounts for the financial years 2018/19 to 2022/23.
- 3.6 The second appointing period will span the five consecutive financial years commencing 1 April 2023. It will cover the audits of accounts for the financial years 2023/24 to 2027/28.
- 3.7 The PSAA has begun the process of retendering for external auditors for local authorities in England, for contracts due to start from 1 April 2023. The Council will therefore need to decide whether to opt into the PSAA's national procurement arrangement for the second appointing period, or whether to procure its own external auditor from this date.
- 3.8 Legislation requires a resolution of Full Council if the Council wishes to opt into the national procurement arrangement. The deadline for this decision is **11 March 2022**. Failure to make a formal decision by this date is deemed to be a decision by the Council to procure its own external auditor.

#### **4. Procuring our own external auditor**

- 4.1 The Council can decide not to opt into the national procurement arrangement and make its own auditor appointment instead. However, in order for the Council to undertake the appointment of an external auditor, it would need to establish an **independent auditor panel** to advise on the selection and appointment of an auditor.
- 4.2 The auditor panel must be one of the following:
- A panel appointed solely for the Council.
  - A panel set up with other local authorities.
  - An existing committee or sub-committee of the Council which has been determined to be an auditor panel (subject to compliance with the other provisions and regulations related to auditor panels).
  - An auditor panel of another local authority that has agreed to act as an auditor panel for the Council.

The minimum number of members that an auditor panel must have is three.

4.3 Most of the members of the auditor panel, including the Chairperson, must be **independent** of the Council. The main areas through which independence may be impaired are where the panel member:

- Has been a member or officer of the Council, or another local authority connected to the Council, within the last five years.
- Has been an officer or employee of an entity connected with the Council within the last five years.
- Is party to a contract with the Council, either as an individual or through an entity with which the individual has a beneficial interest.
- Has been an auditor or an employee of a prospective auditor of the Council within the last five years.
- Has a relative or close friend of any of the above.

These requirements may, in practice, make it difficult to find people able and willing to serve on an auditor panel.

4.4 The role of an independent auditor panel would be to advise the Council on:

- The selection and appointment of an auditor.
- Whether the Council should adopt a policy on obtaining non-audit services from the auditor, including the contents of such a policy.
- Any proposal by the Council to enter into a liability limitation agreement.
- Maintaining an independent relationship with its auditor.
- The outcome of any investigation of an auditor's resignation from office, if this occurs, or on any proposal to remove a local auditor from office.

4.5 Whilst the appointment of an external auditor would be the Council's responsibility, the Council must take account of the advice of its auditor panel.

4.6 Once the auditor panel has produced its advice on the selection and appointment of an auditor, the Council must publish a notice, within 28 days of the appointment being made, that includes information such as:

- the name of the auditor.
- the length of the appointment.
- the advice, or a summary of the advice, from the auditor panel.
- Where it has not accepted that advice, the reasons why not.

This notice must be published on the Council's website or in another suitable format.

## 5. National procurement arrangement

- 5.1 The local audit market was relatively stable when the PSAA ran the procurement for the first appointing period. **98%** of authorities opted into the national scheme. As a result of competitive bids from audit firms, the PSAA was able to enter into long term contracts with five audit firms, and to make auditor appointments to all opted-in bodies.
- 5.2 The audit landscape has changed significantly since the PSAA awarded these contracts. A drive to deliver improvements in audit quality started to impact on audit firms' ability to complete all their local authority audits for 2018/19 by the target date for publication of audited accounts (**31 July**) - a problem that was exacerbated by growing recruitment and retention challenges and increasing levels of technical challenges as local authorities explored innovative ways of delivering services to achieve savings.
- 5.3 The 2019/20 audits presented greater challenges. Even with the benefit of an extended timeline for publication of audited accounts, only **45%** of audits were completed by the target date of **30 November** (*compared to 57% of 2018/19 audits being completed by the target date for completion of 31 July*). The situation has deteriorated further in 2020/21, with only **9%** of audits being completed by the target publication date of **30 September**.
- 5.4 This paints a picture of an audit industry under enormous pressure, and of a local audit system which is experiencing considerable strain and instability.
- 5.5 The PSAA's national appointing scheme could be the best option to enable the Council to secure audit services in a very challenging market. The PSAA's national scheme offers a range of benefits for its members, including:
- Transparent and independent auditor appointment via a third party, avoiding the necessity for local bodies to establish an auditor panel and undertake an auditor procurement.
  - Ongoing management of any independence issues which may arise.
  - Access to a dedicated team with significant experience of working within the context of the relevant regulations to appoint auditors, managing contracts with audit firms and setting and determining audit fees.
  - Collective savings for the sector through undertaking one major procurement as opposed to a multiplicity of smaller procurements.
  - A sector led collaborative scheme supported by an established advisory panel of sector representatives to help inform the design and operation of the scheme.
  - Concerted efforts to develop a more sustainable local audit market.

- 5.6 The PSAA is staffed by a team with significant experience of working within the context of the regulations to appoint auditors, managing contracts with audit firms and setting and determining audit fees. All of these roles are undertaken with a detailed, ongoing and up to date understanding of the distinctive context and challenges facing the sector.

## 6. Other considerations

- 6.1 The scope of a local audit is fixed. It is determined by the Code of Audit Practice (currently published by the National Audit Office), the format of the financial statements (specified by CIPFA / LASAAC) and the application of auditing standards regulated by the Financial Reporting Council. These factors apply to all local authorities, irrespective of the route chosen for appointing an auditor.
- 6.2 It is also worth noting that, in accordance with the 2014 Act, audit firms must be registered with the Institute of Chartered Accountants in England and Wales (ICAEW), and that there are currently fewer than ten firms registered to carry out local audit work.
- 6.3 This means that the Council would have little or no influence over what it is procuring. Hence, there appear to be no obvious benefits to the Council choosing to make its own separate arrangements for appointing an external auditor.

## 7. Policy context and Outcomes Framework

- 7.1 The external audit of the Council's annual statement of accounts, and of its arrangements to secure value for money in the use of resources, provides assurance that taxpayers' money has been well managed and properly accounted for; this is one of the cornerstones of public accountability.

## 8. Financial Implications

- 8.1 Whichever method of auditor appointment is chosen, the Council will need to pay fees to its appointed auditor.
- 8.2 The annual audit fees currently payable by the Council are as follows:

Annual audit fees	Essex County Council	Essex Pension Fund
<b>PSAA scale fee</b>	£126,265	£24,075
<b>Additional audit fees</b>		
• Audit of valuations (non-current assets and pension liabilities) and group accounts	£8,155	-
• Audit of judgemental components of the Pension Fund	-	£3,925
<b>Sub total</b>	<b>£134,420</b>	<b>£28,000</b>
• New Use of Resources approach	£TBC	-
<b>Total audit fees</b>	<b>£TBC</b>	

In addition, extra fees are charged on an ad-hoc basis, reflecting circumstances specific to particular audits. For example, in relation to the audit of the Pension Fund triennial actuarial data and to reflect the impact of Covid-19 remote working etc.

- 8.3 It is possible that the scale fees payable from 2023/24 will be higher than the current scale fees. Sir Tony Redmond (who was commissioned by the Secretary of State to undertake an independent review into the oversight of local audit and the transparency of local authority financial reporting) has suggested that fee increases of circa **25%** may be required to enable audit firms to meet current quality standards.
- 8.4 Whilst it is possible that, if the Council conducts its own procurement, it may be able to negotiate a lower audit fee than the scale fees determined by the PSAA, these savings may not be sufficient to cover the costs associated with conducting a separate procurement and constituting and maintaining an independent auditor panel.

## **9. Legal Implications**

- 9.1 The Local Audit and Accountability Act 2014 sets the framework for audit of the Council's accounts. This requires the Council to either appoint its own auditor, following the advice of an independent auditor panel, or to opt into a central system where the auditor will be appointed by Public Sector Auditor Appointments Ltd (as the designated 'appointing person').
- 9.2 The Council will need to ensure that an auditor has been appointed by **31 December 2022**. This could be by 'opting in' to the PSAA's national procurement arrangement for auditor appointments or by undertaking its own procurement advised by an independent Auditor Panel.
- 9.3 If the Council accepts the PSAA's invitation, it will become an 'opted in authority' for the period specified in the invitation and it cannot appoint its own auditor during that period, although the central appointing body would be required by law to consult the Council before appointing an auditor.
- 9.4 Audit fees for 'opted in authorities' are calculated using a scale set by the central appointing person after consulting 'opted in authorities' and firms of accountants. Opted in authorities must pay the scale fee, together with any extra charges that apply.
- 9.5 Under regulation 19 of the Local Audit (Appointing Persons) Regulations 2015 the decision to become an opted in authority must be taken at a meeting of the Full Council.

## **10. Staffing and other resource implications**

- 10.1 If the Council decides to conduct its own auditor procurement, then officers will need to:
- Undertake the procurement process and subsequent contract management.
  - Assist with recruitment of independent members to an auditor panel.
  - Organise Panel meetings.
- 10.2 None of this additional capacity will be required if the Council opts into the PSAA national procurement arrangement and does not appoint an auditor panel.

## **11. List of Background Papers**

- 11.1 Email from the Local Government Association dated 23 September 2021 (**appended**).
- 11.2 PSAA Prospectus: The national scheme for local auditor appointments:  
<https://www.psaa.co.uk/wp-content/uploads/2021/11/Prospectus-2023-and-beyond-FINAL.pdf>

## **Appendix - Email from the Local Government Association**

From the Chairman of the Association  
Cllr James Jamieson



**To: Mayors/Leaders/Chief Executives/Chief Finance Officers  
of English Principal Councils**

23 September 2021

Dear Gavin Jones,

### **Retender of External Audit Contracts**

I am writing because your council must shortly make a decision whether to opt into the national arrangement for the procurement of external audit or procure external audit for itself, and to set out the LGA's view on that decision.

In most councils this matter will be considered first in detail by the Audit Committee. You will therefore no doubt wish to pass on a copy of this letter and the more detailed attachment to the colleague who chairs the relevant committee.

Legislation requires a resolution of Full Council if a local authority wishes to opt into the national arrangement. The practical deadline for this decision is 11<sup>th</sup> March 2022. As this is a decision for the Full Council, I wanted to ensure that you had sight of the letter that has been sent to audit and finance colleagues and that you are aware of the crucial issues to be considered.

The way external audit has operated over the last couple of years has been extremely disappointing. This has led to many audits being delayed and dozens of audits remain uncompleted from 2019/20. Dealing with these issues is not a quick or easy fix.

Nevertheless, the LGA's view is that the national framework remains the best option for councils. There are many reasons for favouring the national arrangements and we think those reasons have become more compelling since 2016/17 when councils were last asked to make this choice.

We believe that in a suppliers' market it is imperative that councils act together to have the best chance of influencing the market and for nationally coordinated efforts to improve the supply side of the market to be effective.

The information attached goes into more detail about the background to this decision. My officers will be happy to answer any questions you may have. Please



contact Alan Finch ([alan.finch@local.gov.uk](mailto:alan.finch@local.gov.uk)) if you have any issues you would like to raise.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'James Jamieson', written in a cursive style.

Cllr James Jamieson  
Chairman

cc: Chief Executive  
Chief Finance Officer

## **RETENDER OF EXTERNAL AUDIT CONTRACTS**

### **Information from the LGA for those charged with governance**

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

Legislation requires a resolution of Full Council if a local authority wishes to opt into the national arrangement. The deadline for this decision is the 11<sup>th</sup> 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.

The national framework remains the best option councils can choose. There are many reasons for favouring the national arrangements and we think those reasons have become more compelling since 2016/17 when councils were last asked to make this choice.

The way external audit has operated over the last couple of years has been extremely disappointing. A lack of capacity in the audit market has been exacerbated by increased requirements placed on external auditors by the audit regulator. There is also a limited number of firms in the market and too few qualified auditors employed by those firms. This has led to a situation where many audits have been delayed and dozens of audit opinions remain outstanding from 2019/20 and 2020/21. Auditors have also been asking for additional fees to pay for extra work.

As the client in the contract, a council has little influence over what it is procuring. The nature and scope of the audit is determined by codes of practice and guidance and the regulation of the audit market is undertaken by a third party, currently the Financial Reporting Council. Essentially, councils find themselves operating in what amounts to a suppliers' market and the client's interest is at risk of being ignored unless we act together.

Everyone, even existing suppliers, agrees that the supply side of the market needs to be expanded, which includes encouraging bids from challenger firms. Public Sector Audit Appointments Ltd (PSAA), the body nominated by the Government to run the national arrangements, has suggested various ways this could be done, but these initiatives are much more likely to be successful if a large number councils sign up to the national scheme.

It is therefore vital that councils coordinate their efforts to ensure that the client voice is heard loud and clear. The best way of doing this across the country is to sign up to the national arrangement.

To summarise, the same arguments apply as at the time of the last procurement:

- A council procuring its own auditor or procuring through a joint arrangement means setting up an Audit Panel with an independent chair to oversee the procurement and running of the contract.
- The procurement process is an administrative burden on council staff already struggling for capacity. Contract management is an ongoing burden.
- Procuring through the appointing person (PSAA) makes it easier for councils to demonstrate independence of process.
- Procuring for yourself provides no obvious benefits:
  - The service being procured is defined by statute and by accounting and auditing codes
  - Possible suppliers are limited to the small pool of registered firms with accredited Key Audit Partners (KAP).
  - Since the last procurement it is now more obvious than ever that we are in a 'suppliers' market' in which the audit firms hold most of the levers.
- PSAA has now built up considerable expertise and has been working hard to address the issue that have arisen with the contracts over the last couple of years:
  - PSAA has the experience of the first national contract. The Government's selection of PSAA as the appointing person for a second cycle reflects MHCLG's confidence in them as an organisation.
  - PSAA has commissioned high quality research to understand the nature of the audit market.
  - It has worked very closely with MHCLG to enable the government to consult on changes to the fees setting arrangements to deal better with variations at national and local level, hopefully resulting in more flexible and appropriate Regulations later this year

Councils need to consider their options. we have therefore attached a list of Frequently Asked Questions relating to this issue which we hope will be useful to you in reaching this important decision.

When the LGA set up PSAA in 2015, we did so with the interests of the local government sector in mind. We continue to believe that the national arrangement is the best way for councils to influence a particularly difficult market.

If you have any questions on these issues please contact Alan Finch, Principal Adviser (Finance) ([alan.finch@local.gov.uk](mailto:alan.finch@local.gov.uk)).

## **PROCUREMENT OF EXTERNAL AUDIT from financial year 2023/24**

### **FREQUENTLY ASKED QUESTIONS**

“Were prices set too low in the current contract?”

It is clear that firms did submit bids that reflected what seemed at the time to be very stable market conditions. Unfortunately, a series of financial collapses in the private sector have since created a very different climate and resulted in a whole series of new regulatory pressures. It is very likely that firms thought they could make savings as a result of the new timetable, essentially finishing the accounts audits by the end of July each year. Of course, that is not what has happened.

The Government opened up the market principally on the argument that costs would reduce, and views were mixed in the sector when the first contract was being let. Some councils wanted more savings and some were worried about reduced standards.

“Has the current contract helped cause these issues?”

Since the current contract is based around the Code of Audit Practice and the local government accounting code, this is unlikely. The first year of the new contract coincided with the introduction of new standards and with the emergence of some difficult audit issues such as the [McCloud judgement](#) (a legal case which affected the valuation of pension liabilities). The second year was affected by COVID-19. This laid bare the lack of capacity in the supplier side of the market and led to considerable delays. It is hard to see how the contract could have pre-empted this, but now we are clearer about the level of uncertainty in the system, the next contract can adjust for it.

“If we let our own contract, could we have more influence over auditors?”

No. The auditors are required to be independent and are bound by the Codes and need to deliver to them in line with the regulator’s expectations or face action under the regulatory framework.

As far as delays in audits is concerned, auditors are required to allocate resources according to risk and councils that procure for themselves will find themselves in the same queue as those within the national arrangement.

“If we let our own contract, can we get the auditors to prioritise our audit over others?”

Very unlikely. Auditors are running at full capacity and have to deploy resources according to their assessment of audit risks in accordance with professional standards. It is very unlikely that auditors could give preference to some clients rather than others even if they wanted to.

“Didn’t we used to get more from our auditors?”

Yes we did. For example, auditors were often prepared to provide training to audit committees on a pro-bono basis. The fact that they used to be with us for most of the year meant officers could develop professional working relationships with auditors and they understood us better, within the boundaries required of their independent status. Auditors no longer have the capacity to do extra work and the light shone on

audit independence in other sectors of the economy has reinforced the rules on the way auditors and councils work together.

“Under the national framework we have had to negotiate our own fee variations. Will that continue to be the case?”

Unfortunately, virtually all councils have had to engage in discussions with auditors about fee variations linked to new regulatory requirements and, of course, the challenges of COVID-19. SAA has worked hard with MHCLG to enable the recent consultation on changes to the fee setting regime, and the resulting regulatory change will bring scope for more issues to be settled at a national level in future.

“Can we band together in joint procurements to get most of the benefits of not going it alone?”

We understand that this is lawful. However, joint procurement partners would not be part of PSAA's efforts on behalf of the sector to increase the number of firms competing in the market, which will therefore be less likely to succeed.

At best, joint procurement spreads the pain of procuring over a larger number of councils and at worst it introduces a new layer of bureaucracy, because someone is going to have to take the lead and bring all the members of the consortium along. It's not altogether clear to us why a joint procurement would be better than the national contract, especially as the consortium would then have to manage the contract throughout its life (for example, the implications of changes of audit scope).



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