

North Tyneside Council

Report to Audit Committee

Date: 24 May 2017

ITEM 9

Title: Briefing on new arrangements for appointment of the External (Local) Auditor

Report from Service Area: Finance

Report Author: Allison Mitchell,
Chief Internal Auditor

Tel: (0191) 643 5720

Wards affected: All

PART 1

1.1 Purpose:

This report aims to update Audit Committee on changes regarding the process of appointing the external auditor, and how these changes are being addressed by North Tyneside Council.

The Local Audit and Accountability Act 2014 introduced a new requirement for all local authorities to procure and appoint their own external auditor (known as a 'local auditor') from 2017/18 onwards. North Tyneside Council's current external audit contract with Mazars ends with the audit of the accounts for 2017/18. The Authority, along with all other local authorities, must appoint a local auditor by 31 December 2017 in preparation for the 2018/19 audit year.

In March 2017 Cabinet agreed to a collaborative procurement to appoint a local auditor (working with two neighbouring authorities). This will allow all statutory responsibilities to be fulfilled and is likely to offer optimum value for money at the current time. The procurement process is now underway.

1.2 Recommendation(s):

It is recommended that Audit Committee note the contents of this Report.

1.3 Council Plan and Policy Framework:

The work of the external auditor is based in statute. The external audit responsibilities to audit the published financial statements, and provide a value for money opinion, support all service responsibilities as identified within the Our North Tyneside Plan.

1.4 Information:

1.4.1 Background

All local authorities are required to be externally audited. The requirements of the external audit process have changed over the years, but are codified in a 'Code of Audit

Practice'¹ which explains the duties required of the external auditor. Currently these comprise two main areas:

- **Accounts** – To perform an audit of the Authority's published financial statements; and
- **Value for Money** – To satisfy themselves that the audited body "...has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources".

The external auditor also audits certain grant and subsidy claims.

There are some other responsibilities – such as allowing electors to raise questions about the accounts and issuing reports if required in the 'public interest' or if an item of expenditure has been found to be unlawful. However these latter two reports would not be a usual feature of most local authorities' external audit coverage on an annual basis.

Historically, the Audit Commission appointed external auditors to local authorities, which had no involvement in the choice of appointment or the fees charged. Around two thirds of authorities had their audit provided directly by the Audit Commission and the remaining third had their audit provided by one of the larger accountancy firms (e.g. PwC, Deloitte, Mazars etc.).

The Local Audit and Accountability Act 2014 changed this. This legislation abolished the Audit Commission and introduced a number of other changes to local authorities' corporate governance and external audit arrangements. The duties previously performed by the Audit Commission have been split between the National Audit Office (which previously covered only central government departments) and the Cabinet Office (for matters relating to counter fraud).

The biggest immediate change provided by the Act is that the Authority – along with all other local authorities in England and Wales – must now procure and appoint its own external auditor (known as a 'local auditor') by 31 December 2017. The new auditor will take up their duties from April 2018.

The Act also requires that an Auditor Panel is established. The Authority is required to consult and take into account the advice of the Auditor Panel on the selection and appointment of a local auditor. In addition the Auditor Panel is required to advise the Authority on the maintenance of an independent relationship with the local auditor. Such an Auditor Panel must consist of a majority of independent members (as defined by the Act). An Auditor Panel can be created and act for more than one local authority.

1.4.2 Opportunities and risks associated with the new requirement to procure a 'local' (external) auditor

As the change in the arrangements for external auditor appointments is relatively recent all local authorities are addressing the requirements with a relatively short lead in time. We have been able to consider experiences in the Health sector, where the new arrangements took effect a year earlier (with appointments having to be made by 31 December 2016).

The main opportunities from appointing the Local Auditor are:

¹ National Audit Office, Code of Audit Practice, April 2015

- Local authorities are able to set the specification for the work of their local auditor. The main requirements of the work are clearly set out in the Code of Audit Practice (described above), which cannot be restricted. However there is an opportunity to include specific quality requirements, local aspirations and to define what the Authority expects to be audited for the price to be paid (e.g. group accounts) – so no additional fees occur at a later stage.
- The Council, on the recommendation of the Auditor Panel, decides on the choice of local auditor and the length of that appointment.
- Value for money in the auditor market can be properly tested.
- Local authorities are able to work with others as part of the appointment / procurement process – for example other local authorities (if a collaborative procurement route is chosen) and the independent representatives appointed to the Auditor Panel.

The main risks are:

- anecdotal feedback from the Health Service in their procurements this year is that audit costs may be showing signs of increasing, not decreasing. The accountancy firms in the market for external audit services have commented that the prices which they have levied in the past had been reduced in recognition of substantial market share, which may not be the case under the new arrangements.
- time and costs involved in the specific appointment requirements (e.g. establishing an Auditor Panel).
- attracting sufficient experienced independent members to an Auditor Panel (though our Audit Committee, which already has independent members, has allowed us to access a good source of expertise).
- from collaborative arrangements, ensuring that any appointment fulfils the aspirations of all local authorities involved. However, as the main responsibilities of the external auditor are already set out in the Code of Practice, this would be likely to form the basis of any specification.

1.4.3 Procurement / Appointment Options

The Act includes a number of requirements on how the appointment can be made, with some requirements being dependent upon the procurement route chosen. There are three main procurement avenues that a principal local authority can follow when appointing a 'local auditor' (described below).

- (a) A stand-alone appointment by a local authority, either advertising and procuring directly or via an established external audit framework agreement;
- (b) A collaborative approach, working with one or more local authorities, again procuring as a specific tender for all the authorities involved, or selecting a provider for all collaborating authorities from an external audit framework agreement; and
- (c) Following a 'sector led' approach. The Local Government Association (LGA) has an established company, Public Sector Audit Appointments Ltd, which it has successfully lobbied to be recognised as an 'appointing person' under the Act.

Cabinet have chosen option (b), on the advice of the Chief Finance Officer which is discussed further below. This option requires that an Auditor Panel (as detailed above) must be established. The decision on the choice of local auditor is made by full Council, taking into consideration the recommendation of the Auditor Panel.

One Auditor Panel has therefore been established by the three local authorities to provide the necessary advice and support that each Authority requires in relation to the appointment of the local auditor and the maintenance of the relationship between the Authority and the local auditor. Mr Kevin Robinson, North Tyneside Council's Chair of Audit Committee, has agreed to act as North Tyneside's representative on the Auditor Panel which will meet to consider the bids received during mid May.

1.4.4 Why a collaborative approach?

The potential for a joint procurement and appointment on behalf of three 'north of Tyne' local authorities was discussed between North Tyneside Council, Northumberland County Council and Newcastle City Council. This option was considered to offer the most potential to achieve value for money and ensure that the assurance needs of all three Authorities could be best tailored to their circumstances. This option was therefore recommended to and agreed by Cabinet in March 2017.

Northumberland County Council (which has recent experience of procuring external audit services under the Local Audit and Accountability Act 2014) is leading the procurement exercise, complying with the Contract Standing Orders of that Authority and relevant procurement legislation as well as the requirements of the Act in relation to the suitability of the local auditor.

Together, external audit fees across the three authorities have totalled approximately £2 million over the last three years (North Tyneside's fees accounting for £0.571m of this sum). It is hoped that a contract in such a value range will prove attractive to the market and allow economies of scale and value for money to be achieved.

1.4.5 Current Status

Following Cabinet's decision in March 2017 (and those decisions of the other two Authorities in this procurement), a specification was drafted based on the requirements of the Code of Practice. The opportunity was also taken to incorporate other known assurance requirements (eg the audit of subsidiary entities / group accounts) and audit of subsidy claims requiring external certification.

The contract was advertised on 11 April. Queries from prospective bidders have been received and responded to, and the final date for receipt of completed bids is 12 noon on 16 May 2017.

1.4.6 What will happen next?

The Auditor Panel will consider the bids and evaluate these against the cost and quality criteria which have been established. Once this process is complete and a recommended provider has been identified by the Auditor Panel, a report will be taken to meetings of full Council at each of the three Authorities in this agreement. The report will recommend the choice of provider, which full Council will take into account when making its decision.

Further updates will be brought to future meetings of Audit Committee. Once appointed, the new local auditor will take up their duties from April 2018.

1.5 **Decision options:**

It is recommended that Audit Committee notes the contents of this report. There are no other options available in relation to this report.

1.6 Reasons for recommended option:

This will allow the Audit Committee to be aware of the legislative background to the Local Auditor arrangements, and the decisions taken by Cabinet and rationale for those decisions. It will also allow the Audit Committee to be briefed on the next steps in the Appointment process.

1.7 Appendices:

There are no appendices to this report.

1.8 Contact officers:

Allison Mitchell, Chief Internal Auditor, 0191 643 5720
Kevin McDonald, Group Assurance Manager, 0191 643 5738
Alison Campbell, Senior Business Partner, 0191 643 7038

1.9 Background information:

The following background papers have been used in the compilation of this report and are available at the office of the author.

- Local Audit and Accountability Act 2014
<http://www.legislation.gov.uk/ukpga/2014/2/contents>
- Report to Cabinet 13 March 2017, 'Procurement of Local Auditor by 31 December 2017'
http://www.northtyneside.gov.uk/pls/portal/NTC_PSCM.PSCM_Web.download?p_ID=568463

PART 2 – COMPLIANCE WITH PRINCIPLES OF DECISION MAKING

2.1 Finance and other resources

The Authority has always been required to budget for external audit fees, which are part of the mandatory external audit requirement. It will similarly be a requirement for the Authority to include fees for an auditor procured under the new Local Auditor requirements of the Local Audit and Accountability Act 2014 in its budget and financial plan. Until the market has been approached, it is not known what the fee level will be. During the last three years, annual external audit fees set by the Audit Commission for the Authority (and related advice and non-audit tasks) have ranged between £162k and £207k per annum.

2.2 Legal

The legal implications of the requirements of the Local Audit and Accountability Act 2014 are set out in the report. The procurement and appointment of a local auditor by 31 December 2017 will ensure that the Authority secures compliance with all relevant legal requirements of the Act.

The decision to authorise a procurement process to secure the services of a local auditor and to make arrangements for the creation of and appointment to the Auditor Panel is the responsibility of Cabinet.

The decision to appoint the local auditor is reserved to full Council and will require a report to be presented to a future meeting of full Council. In that report the advice and guidance of the Auditor Panel in relation to who should be appointed as the local auditor will be provided.

2.3 Consultation/community engagement

Internal consultation on this report has been undertaken with the Cabinet Member for Finance and Resources. Consultation has also taken place with the relevant Finance Officers within Newcastle City Council and Northumberland County Council, regarding the potential for a collaborative procurement.

2.4 Human rights

There are no human rights implications arising from this report.

2.5 Equalities and diversity

There are no equalities and diversity implications arising from this report.

2.6 Risk management

A risk register has been developed and all risks will be managed according to North Tyneside Council's agreed risk management procedures.

2.7 Crime and disorder

There are no crime and disorder implications arising directly from this report.

2.8 Environment and sustainability

There are no environment and sustainability implications arising directly from this report.