

REPORT TITLE: DECISION TO OPT INTO THE NATIONAL SCHEME FOR
AUDITOR APPOINTMENTS WITH PSAA AS THE "APPOINTING PERSON"

AUDIT COMMITTEE

24 NOVEMBER 2016

PORTFOLIO HOLDER: Cllr Stephen Godfrey

REPORT OF HEAD OF FINANCE

Contact Officer: Simon Little Tel No: 01962 848224

Email slittle@winchester.gov.uk

WARD(S): ALL

PURPOSE

This report sets out the proposals for appointing the external auditor to the Council for the 2018/19 accounts and beyond, as the current arrangements only cover up to and including 2017/18 audits.

RECOMMENDATIONS:

1. The Audit Committee recommends to Full Council, that it accepts Public Sector Audit Appointments (PSAA) invitation to "opt-in" to the sector led option for the appointment of external auditors for five financial years commencing 1 April 2018.

IMPLICATIONS:

1 COMMUNITY STRATEGY OUTCOME

- 1.1 The independent audit of the financial accounts and its delivery of value for money is key to ensuring that Winchester City Council continues to be Effective and Efficient.

2 FINANCIAL IMPLICATIONS

- 2.1 There is a risk that current external fees could increase when the current contract ends in 2018.
- 2.2 Opting into a national scheme provides the maximum opportunity to ensure fees are as low as possible, whilst ensuring the quality of audit is maintained by entering into a large scale collective procurement arrangement.
- 2.3 If the national scheme is not used some additional resource maybe needed to establish an independent auditor panel and conduct local procurement. Until a procurement exercise is completed it is not possible to state what, if any, additional resource maybe required for audit fees for 2018/19.

3 LEGAL AND PROCUREMENT IMPLICATIONS

- 3.1 Section 7 of the Local Audit and Accountability Act 2014 requires a relevant Council to appoint an auditor to audit its accounts for a financial year not later than 31 December in the preceding year (i.e. by 31 Dec 2017 for the audit of the 2018/19 financial year). Section 8 of the Act governs the procedure for the appointment including that the Council must consult and take account of the advice of its auditor panel on the selection and appointment of the auditor. Section 8 provides that where a relevant Council is in an operating executive arrangement, the function of appointing an auditor is not the responsibility of an executive (Cabinet) of the Council under those arrangements.
- 3.2 Section 12 makes provision for the failure to appoint an auditor: the Council must immediately inform the Secretary of State, who may direct the Council to appoint an auditor named in the direction or appoint an auditor on behalf of the Council.
- 3.3 Section 17 gives the Secretary of State the power to make regulations in relation to an "appointing person" specified by the Secretary of State. This power has been exercised in the Local Audit (Appointing Person) Regulations 2015 (SI 192) and this gives the Secretary of State the ability to enable a sector-led body to become the appointing person. In July 2016 the Secretary of State specified PSAA as the appointing person.

4 WORKFORCE IMPLICATIONS

- 4.1 None

5 PROPERTY AND ASSET IMPLICATIONS

5.1 None

6 CONSULTATION AND EQUALITY IMPACT ASSESSMENT

6.1 None

7 RISK MANAGEMENT

Risk	Mitigation	Opportunities
<i>That the Council fails to appoint an auditor in accordance with the new frameworks or does not achieve value for money in the appointment process.</i>	Opting into the sector led approach through the PSAA	
<i>That fees charged by the Auditor will be considerably higher than currently.</i>	Opting into the sector led approach through the PSAA	Driving down the price as a member of a larger grouping of public sector organisations.
<i>Not enough public sector organisations join the PSAA so that it is unable to deliver the efficiencies envisaged.</i>	493 public sector organisations have indicated their preference to join the PSAA.	

8 SUPPORTING INFORMATION:

Purpose and Summary Points

- 8.1 This report sets out the proposals for appointing the external auditor to the Council for the 2018/19 accounts and beyond, as the current arrangements only cover up to and including 2017/18 audits. The auditors are currently working under a contract originally let by the Audit Commission and the contract was novated to Public Sector Audit Appointments (PSAA) following the closure of the Audit Commission.
- 8.2 A sector-wide procurement conducted by PSAA will produce better outcomes and will be less burdensome for the Council than any procurement undertaken locally. More specifically:
- The audit costs are likely to be lower than if the Council sought to appoint locally, as national large-scale contracts are expected to drive keener prices from the audit firms;

- Without the national appointment, the Council would need to establish a separate independent auditor panel, which could be difficult, costly and time-consuming;
- PSAA can ensure the appointed auditor meets and maintains the required quality standards and can manage any potential conflicts of interest much more easily than the Council; and
- Supporting the sector-led body will help to ensure there is a vibrant public audit market for the benefit of the whole sector and this Council going forward into the medium and long term.

8.3 If the Council is to take advantage of the national scheme for appointing auditors to be operated by PSAA for the subsequent years, it needs to take the decision at this meeting to enable it accept the invitation by early March 2017.

Background

8.4 The Local Audit and Accountability Act 2014 (the Act) brought to a close the Audit Commission and established transitional arrangements for the appointment of external auditors and the setting of audit fees for all local government and NHS bodies in England. On 5 October 2015 the Secretary of State for Communities and Local Government (CLG) determined that the transitional arrangements for local government bodies would be extended by one year to also include the audit of the accounts for 2017/18.

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

8.6 In July 2016 PSAA were specified by the Secretary of State as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015. The appointing person is sometimes referred to as the sector-led body and PSAA has wide support across local government. PSAA was originally established to operate the transitional arrangements following the closure of the Audit Commission under powers delegated by the Secretary of State. PSAA is an independent, not-for-profit company limited by guarantee and established by the LGA.

8.7 PSAA is inviting the Council to opt in, along with all other authorities, so that PSAA can enter into a number of contracts with appropriately qualified audit firms and appoint a suitable firm to be the Council's auditor.

8.8 The principal benefits from such an approach are as follows:

- PSAA will ensure the appointment of a suitably qualified and registered auditor and expects to be able to manage the appointments to allow for appropriate groupings and clusters of audits where bodies work together;
- PSAA will monitor contract delivery and ensure compliance with contractual, audit quality and independence requirements;
- Any auditor conflicts at individual authorities would be managed by PSAA who would have a number of contracted firms to call upon;
- It is expected that the large-scale contracts procured through PSAA will bring economies of scale and attract keener prices from the market than a smaller scale competition;
- The overall procurement costs would be lower than an individual smaller scale local procurement;
- The overhead costs for managing the contracts will be minimised through a smaller number of large contracts across the sector;
- There will be no need for the Council to establish alternative appointment processes locally, including the need to set up and manage an 'auditor panel', see below;
- The new regime provides both the perception and reality of independent auditor appointment through a collective approach; and
- A sustainable market for audit provision in the sector will be easier to ensure for the future.

8.9 The Council's current external auditor is Ernst and Young LLP, this appointment having been made under contract let by the Audit Commission. Following closure of the Audit Commission the contract was novated to PSAA, and since this date PSAA has demonstrated its capability in terms of auditor appointment, contract management, and monitoring audit quality. Over recent years authorities have benefited from a reduction in fees in the order of 55% compared with fees in 2012. This has been the result of a combination of factors including new contracts negotiated nationally with the audit firms and savings from closure of the Audit Commission. The Council's current external audit fees are £66,871 per annum.

8.10 The proposed fees for the subsequent years cannot be known until the procurement process has been completed, as the costs will depend on proposals from the audit firms.

- 8.11 The scope of the audit will still be specified nationally; the National Audit Office (NAO) is responsible for writing the Code of Audit Practice which all firms appointed to carry out the Council's audit must follow. Not all audit firms will be eligible to compete for the work; they will need to demonstrate that they have the required skills and experience and be registered with a Registered Supervising Body approved by the Financial Reporting Council.
- 8.12 Currently, there are only nine providers that are eligible to audit local authorities and other relevant bodies, all of these being firms with a national presence. This means that a local procurement exercise, as described immediately below, would seek tenders from these same firms, subject to the need to manage any local independence issues. Local firms could not be invited to bid.

The invitation

- 8.13 PSAA has now formally invited this Council to opt in. Details relating to PSAA's invitation are provided in an Appendix A to this Report.
- 8.14 In summary the national opt-in scheme provides the following:
- The appointment of a suitably qualified audit firm for each of the five financial years commencing 1 April 2018;
 - Appointing the same auditor to other opted-in bodies that are involved in formal collaboration or joint working initiatives to the extent this is possible with other constraints;
 - Managing the procurement process to ensure both quality and price criteria are satisfied. PSAA will seek views from the sector to help inform its detailed procurement strategy;
 - Ensuring suitable independence of the auditors from the bodies they audit and managing any potential conflicts as they arise;
 - Minimising the scheme management costs and returning any surpluses to scheme members;
 - Consulting with authorities on auditor appointments, giving the Council the opportunity to influence which auditor is appointed;
 - Consulting with authorities on the scale of audit fees and ensuring these reflect scale, complexity and audit risk; and
 - Ongoing contract and performance management of the contracts once these have been let.

The way forward

- 8.15 Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt in must be made by a meeting of the Council (meeting as a whole). The Council then needs to formally respond to PSAA's invitation in the form specified by PSAA by early March 2017.
- 8.16 PSAA will commence the formal procurement process after this date. It expects to award contracts in summer 2017 and consult with authorities on the appointment of auditors so that it can make an appointment by the statutory deadline of December 2017.

9 OTHER OPTIONS CONSIDERED AND REJECTED

- 9.1 If the Council did not opt in there would be a need to establish an independent auditor panel. In order to make a stand-alone appointment, the auditor panel would need to be set up by the Council itself. The members of the panel must be wholly or a majority of independent members as defined by the Act. Independent members for this purpose are independent appointees, this excludes current and former elected members (or officers) and their close families and friends. This means that elected members will not have a majority input to assessing bids and choosing which audit firm to award a contract for the Council's external audit.
- 9.2 Alternatively, the Act enables the Council to join with other authorities to establish a joint auditor panel. Again this will need to be constituted of wholly or a majority of independent appointees (members). Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each council under the Act and the Council would need to liaise with other local authorities to assess the appetite for such an arrangement.
- 9.3 Neither of these options are recommended. Both these options would be more resource-intensive processes to implement and, without the bulk buying power of the sector led procurement, would be likely to result in a more costly service. It would also be more difficult to manage quality and independence requirements through a local appointment process.

BACKGROUND DOCUMENTS:-

Previous Committee Reports:-

AUD106 - Local Audit and Accountability Act 2014 – 4 December 2014

AUD158 - Local Appointment of External Auditors – Update – 28 June 2016

Other Background Documents:-

Website for PSAA, includes prospectus on how they will develop the scheme for appointing auditors.

[http://www.psaa.co.uk/supporting-the-transition/appointing-person/.](http://www.psaa.co.uk/supporting-the-transition/appointing-person/)

APPENDICES:

Appendix A – Invitation letter from PSAA

Appendix B – Email invitation from PSAA

Appendix C - Form of notice of acceptance

27 October 2016

Email: appointingperson@psaa.co.uk

Chief Executive
Winchester City Council
City Offices
Colebrook Street
Winchester Hampshire SO23 9LJ

Copied to: Simon Little, Head of Finance, Winchester City Council
Howard Bone, Head of Legal Services, Winchester City Council

Dear Chief Executive

Invitation to opt into the national scheme for auditor appointments

As you know the external auditor for the audit of the accounts for 2018/19 has to be appointed before the end of 2017. That may seem a long way away, but as there is now a choice about how to make that appointment, a decision on your authority's approach will be needed soon.

We are pleased that the Secretary of State has expressed his confidence in us by giving us the role of appointing local auditors under a national scheme. This is one choice open to your authority. We issued a prospectus about the scheme in July 2016, available to download on the [appointing person](#) page of our website, with other information you may find helpful.

The timetable we have outlined for appointing auditors under the scheme means we now need to issue a formal invitation to opt into these arrangements. The covering email provides the formal invitation, along with a form of acceptance of our invitation for you to use if your authority decides to join the national scheme. We believe the case for doing so is compelling. To help with your decision we have prepared the additional information attached to this letter.

I need to highlight two things:

- we need to receive your formal acceptance of this invitation by 9 March 2017; and
- the relevant regulations require that, except for a body that is a corporation sole (a police and crime commissioner), the decision to accept the invitation and to opt in needs to be made by the members of the authority meeting as a whole. We appreciate this will need to be built into your decision making timetable.

If you have any other questions not covered by our information, do not hesitate to contact us by email at appointingperson@psaa.co.uk.

Yours sincerely



Jon Hayes, Chief Officer

Appointing an external auditor

Information on the national scheme

Public Sector Audit Appointments Limited (PSAA)

We are a not-for-profit company established by the Local Government Association (LGA). We administer the current audit contracts, let by the Audit Commission before it closed.

We have the support of the LGA, which has worked to secure the option for principal local government and police bodies to appoint auditors through a dedicated sector-led national procurement body. We have established an advisory panel, drawn from representative groups of local government and police bodies, to give access to your views on the design and operation of the scheme.

The national scheme for appointing local auditors

We have been specified by the Secretary of State for Communities and Local Government as the appointing person for principal local government bodies. This means that we will make auditor appointments to principal local government bodies that choose to opt into the national appointment arrangements we will operate for audits of the accounts from 2018/19. These arrangements are sometimes described as the 'sector-led body' option, and our thinking for this scheme was set out in a prospectus circulated to you in July. The prospectus is available on the [appointing person](#) page of our website.

We will appoint an auditor for all opted-in authorities for each of the five financial years beginning from 1 April 2018, unless the Secretary of State chooses to terminate our role as the appointing person beforehand. He or she may only do so after first consulting opted-in authorities and the LGA.

What the appointing person scheme will offer

We are committed to making sure the national scheme will be an excellent option for auditor appointments for you.

We intend to run the scheme in a way that will save time and resources for local government bodies. We think that a collective procurement, which we will carry out on behalf of all opted-in authorities, will enable us to secure the best prices, keeping the cost of audit as low as possible for the bodies who choose to opt in, without compromising on audit quality.

Our current role means we have a unique experience and understanding of auditor procurement and the local public audit market.

Using the scheme will avoid the need for you to:

- establish an audit panel with independent members;
- manage your own auditor procurement and cover its costs;
- monitor the independence of your appointed auditor for the duration of the appointment;
- deal with the replacement of any auditor if required; and
- manage the contract with your auditor.

Our scheme will endeavour to appoint the same auditors to other opted-in bodies that are involved in formal collaboration or joint working initiatives, if you consider that a common auditor will enhance efficiency and value for money.

We will also try to be flexible about changing your auditor during the five-year appointing period if there is good reason, for example where new joint working arrangements are put in place.

Securing a high level of acceptances to the opt-in invitation will provide the best opportunity for us to achieve the most competitive prices from audit firms. The LGA has previously sought expressions of interest in the appointing person arrangements, and received positive responses from over 270 relevant authorities. We ultimately hope to achieve participation from the vast majority of eligible authorities.

High quality audits

The Local Audit and Accountability Act 2014 provides that firms must be registered as local public auditors with one of the chartered accountancy institutes acting in the capacity of a Recognised Supervisory Body (RSB). The quality of registered firms' work will be subject to scrutiny by both the RSB and the Financial Reporting Council (FRC), under arrangements set out in the Act.

We will:

- only contract with audit firms that have a proven track record in undertaking public audit work;
- include obligations in relation to maintaining and continuously improving quality in our contract terms and in the quality criteria in our tender evaluation;
- ensure that firms maintain the appropriate registration and will liaise closely with RSBs and the FRC to ensure that any quality concerns are detected at an early stage; and
- take a close interest in your feedback and in the rigour and effectiveness of firms' own quality assurance arrangements.

We will also liaise with the National Audit Office to help ensure that guidance to auditors is updated as necessary.

Procurement strategy

In developing our procurement strategy for the contracts with audit firms, we will have input from the advisory panel we have established. The panel will assist PSAA in developing arrangements for the national scheme, provide feedback to us on proposals as they develop, and helping us maintain effective channels of communication. We think it is particularly important to understand your preferences and priorities, to ensure we develop a strategy that reflects your needs within the constraints set out in legislation and in professional requirements.

In order to secure the best prices we are minded to let audit contracts:

- for 5 years;
- in 2 large contract areas nationally, with 3 or 4 contract lots per area, depending on the number of bodies that opt in; and
- to a number of firms in each contract area to help us manage independence issues.

The value of each contract will depend on the prices bid, with the firms offering the best value being awarded larger amounts of work. By having contracts with a number of firms, we will be able to manage issues of independence and avoid dominance of the market by one or two firms. Limiting the national volume of work available to any one firm will encourage competition and ensure the plurality of provision.

Auditor appointments and independence

Auditors must be independent of the bodies they audit, to enable them to carry out their work with objectivity and credibility, and in a way that commands public confidence.

We plan to take great care to ensure that every auditor appointment passes this test. We will also monitor significant proposals for auditors to carry out consultancy or other non-audit work, to protect the independence of auditor appointments.

We will consult you on the appointment of your auditor, most likely from September 2017. To make the most effective allocation of appointments, it will help us to know about:

- any potential constraints on the appointment of your auditor because of a lack of independence, for example as a result of consultancy work awarded to a particular firm;
- any joint working or collaboration arrangements that you think should influence the appointment; and
- other local factors you think are relevant to making the appointment.

We will ask you for this information after you have opted in.

Auditor appointments for the audit of the accounts of the 2018/19 financial year must be made by 31 December 2017.

Fee scales

We will ensure that fee levels are carefully managed by securing competitive prices from firms and by minimising our own costs. Any surplus funds will be returned to scheme members under our articles of association and our memorandum of understanding with the Department for Communities and Local Government and the LGA.

Our costs for setting up and managing the scheme will need to be covered by audit fees. We expect our annual operating costs will be lower than our current costs because we expect to employ a smaller team to manage the scheme. We are intending to fund an element of the costs of establishing the scheme, including the costs of procuring audit contracts, from local government's share of our current deferred income. We think this is appropriate because the new scheme will be available to all relevant principal local government bodies.

PSAA will pool scheme costs and charge fees to audited bodies in accordance with a fair scale of fees which has regard to size, complexity and audit risk, most likely as evidenced by audit fees for 2016/17. Pooling means that everyone in the scheme will benefit from the most competitive prices. Fees will reflect the number of scheme participants – the greater the level of participation, the better the value represented by our scale fees.

Scale fees will be determined by the prices achieved in the auditor procurement that PSAA will need to undertake during the early part of 2017. Contracts are likely to be awarded at the end of June 2017, and at this point the overall cost and therefore the level of fees required will be clear. We expect to consult on the proposed scale of fees in autumn 2017 and to publish the fees applicable for 2018/19 in March 2018.

Opting in

The closing date for opting in is 9 March 2017. We have allowed more than the minimum eight week notice period required, because the formal approval process for most eligible bodies, except police and crime commissioners, is a decision made by the members of an authority meeting as a whole.

We will confirm receipt of all opt-in notices. A full list of authorities who opt in will be published on our website. Once we have received an opt-in notice, we will write to you to request information on any joint working arrangements relevant to your auditor appointment, and any potential independence matters that would prevent us appointing a particular firm.

If you decide not to accept the invitation to opt in by the closing date, you may subsequently make a request to opt in, but only after 1 April 2018. The earliest an auditor appointment can be made for authorities that opt in after the closing date is therefore for the audit of the accounts for 2019/20. We are required to consider such requests, and agree to them unless there are reasonable grounds for their refusal.

Timetable

In summary, we expect the timetable for the new arrangements to be:

- Invitation to opt in issued 27 October 2016
- Closing date for receipt of notices to opt in 9 March 2017
- Contract notice published 20 February 2017
- Award audit contracts By end of June 2017
- Consult on and make auditor appointments By end of December 2017
- Consult on and publish scale fees By end of March 2018

Enquiries

We publish frequently asked questions on our [website](#). We are keen to receive feedback from local bodies on our plans. Please email your feedback or questions to: appointingperson@psaa.co.uk.

If you would like to discuss a particular issue with us, please send an email to the above address, and we will make arrangements either to telephone or meet you.

From: appointingperson@psaa.co.uk
To: [Simon Little](#)
Subject: Winchester City Council - Confirmation of acceptance of electronic communication with PSAA Ltd
Date: 13 October 2016 16:08:10
Importance: High

Confirmation of acceptance of electronic communication with PSAA Ltd The Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015 (the Regulations)

Public Sector Audit Appointments Limited (PSAA), being an appointing person for the purposes of the Regulations, will soon be inviting all principal local government authorities to opt in to the national sector-led arrangements.

In accordance with the Regulations we are seeking confirmation of each authority's willingness to receive notices by means of electronic communication.

To ensure efficient and reliable communication with your authority on opting into the new auditor appointment arrangements, PSAA will assume that your authority confirms its acceptance to receive electronic communications to your email address until notified otherwise. If you do not wish to accept electronic communication or would like us to use another email address, please confirm this by emailing: appointingperson@psaa.co.uk by **Tuesday 25th October 2016**.

We will be contacting authorities through the Chief Executive and Director of Finance towards the end of October/early November to ask for formal confirmation of a decision to opt in. This will include an acceptance pro-forma which your authority will be asked to return by early March 2017, the latest date for return will be stated in the opt in letter.

As you may be aware, the Regulations require this to be a decision made by the authority meeting as a whole, (full council), except where the authority is a corporation sole (such as a police and crime commissioner), where the function must be exercised by the holder of the office. The LGA has developed a template report to support you with this, which can be found on their website.

We have produced a prospectus to explain how we are developing a scheme for local auditor appointment [PSAA prospectus August 2016 \(PDF document\)](#)!. In addition we regularly update our website and FAQs with the latest information. <http://www.psaa.co.uk/supporting-the-transition/appointing-person/>.

Thank you

Jon Hayes
Chief Officer

This email and any files transmitted with it are private and intended solely for the use of the individual or entity to which they are addressed. If you are not the intended recipient the E-mail and any files have been transmitted to you in error and any copying, distribution or other use of the information contained in them is

strictly prohibited.

Nothing in this E-mail message amounts to a contractual or other legal commitment on the part of PSAA unless confirmed by a communication signed on behalf of PSAA. All e-mails to anyone @psaa.co.uk are communications to the company and not private and confidential to any named individual.

PSAA's computer systems and communication may be monitored to secure the effective operation of the system and for other lawful purposes.

Security and reliability of e-mails are not guaranteed. PSAA operate anti-virus programs but you must take full responsibility for virus checking this e-mail (including all attachments). PSAA do not accept any liability in respect of any damage caused by any virus which is not detected.

Form of notice of acceptance of the invitation to opt in

(Please use the details and text below to submit to PSAA your authority's formal notice of acceptance of the invitation to opt into the appointing person arrangements)

To: appointingperson@psaa.co.uk

Subject: Winchester City Council

Notice of acceptance of the invitation to become an opted-in authority

This email is notice of the acceptance of your invitation dated 27 October 2016 to become an opted-in authority for the purposes of the appointment of our auditor under the provisions of the Local Audit and Accountability Act 2014 and the requirements of the Local Audit (Appointing Person) Regulations 2015.

I confirm that Winchester City Council has made the decision to accept your invitation to become an opted-in authority in accordance with the decision making requirements of the Regulations and that I am authorised to sign this notice of acceptance on behalf of the authority.

Name: Simon Little
Title: Head of Finance (authorised officer)
For and on behalf of: Winchester City Council
Date: *To be signed after approval by Full Council*