

<b>Committee name</b>	Audit Committee
<b>Officer reporting</b>	James Lake, Finance
<b>Papers with report</b>	None
<b>Ward</b>	All

## HEADLINES

### Public Sector Audit Appointments

During Autumn 2021 all local government and police bodies will need to make important decisions about their external audit arrangements for the period commencing from the financial year 2023/24. In relation to appointing auditors, local bodies have options to arrange their own procurement and make the appointment themselves or in conjunction with other bodies, or they can join and take advantage of the national collective scheme administered by Public Sector Audit Appointments (PSAA).

The PSAA issued a draft prospectus which provides an introduction to the PSAA national scheme, and discusses, and invites views and comments from local bodies and other interested parties in relation to the aims of the scheme and how it needs to develop going forward. This process will help the PSAA to shape some of the important features of the scheme ahead of issuing formal invitations to opt-in to all eligible bodies in the Autumn.

The Council has responded to the PSAA consultation and broadly supports the PSAA approach. It will be seeking approval at Full Council to opt into the PSAA procurement service. This paper is provided to update the Audit Committee on the rationale and appointment process.

### EY Partner Update

Suresh Patel will be leaving EY in August 2021 and taking up a new role at Mazars UK. EY have assigned Helen Thompson as Associate Partner for Hillingdon and she will be leading on the 2020/21 audit. Helen will introduce herself and provide her background at the Committee meeting.

### Value For Money (VFM)

For 2020/21 audit firms are required to take a different approach to the VFM audit process. The VFM will now form two stages with part one covering a 'risk assessment' based on the responses provided against a prescribed format of control questions. Part two will be the 'execution and conclusion' where depending on the answers provided in the risk assessment, further testing will

be executed to reach a conclusion. EY are required to produce a separate VFM commentary rather than including their assessment in the audit opinion. The VFM commentary should be produced within three months of the issuance of the audit opinion. EY aim to provide a progress update at the Committee meeting.

## **RECOMMENDATIONS:**

### **That the Committee:**

- 1. Note the rationale, timeline and intention to opt into the Public Sector Audit Appointments procurement scheme.**
- 2. Note appointment of the new EY audit lead**
- 3. Note Value for Money update**
- 4. Note verbal update on audit progress**

## **PSAA SUPPORTING INFORMATION**

Public Sector Audit Appointments Limited (PSAA) is an independent company limited by guarantee incorporated by the Local Government Association in August 2014. In July 2016, the Secretary of State specified PSAA as an appointing person for principal local government and police bodies for audits from 2018/19, under the provisions of the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015. Acting in accordance with this role PSAA is responsible for appointing auditors and setting scales of fees for relevant principal authorities that have chosen to opt into its national scheme, overseeing issues of auditor independence and monitoring compliance by the auditor with the contracts we enter into with the audit firms.

In 2014 when the Local Audit and Accountability Act received Royal Assent the audit market was relatively stable. In 2017 PSAA benefitted from that continuing stability. Their initial procurement on behalf of more than 480 bodies (98% of those eligible to join the national scheme) was very successful, attracting very competitive bids from firms. As a result, the PSAA were able to enter into long-term contracts with five experienced and respected firms and to make auditor appointments to all bodies.

2018 proved to be a very significant turning point for the audit industry. A series of financial crises and failures in the private sector gave rise to questioning about the role of auditors and the focus and value of their work. In rapid succession the PSAA had the results of four independent reviews commissioned by Government:

- Sir John Kingman's review of the Financial Reporting Council (FRC), the audit regulator;
- the Competition and Markets Authority review of the audit market;
- Sir Donald Brydon's review of the quality and effectiveness of audit; and
- Sir Tony Redmond's review of local authority financial reporting and external audit.

In total, the four reviews set out more than 170 recommendations which are now in various stages of consideration by Government with the clear implication that a series of significant reforms will follow. Indeed, in some cases where new legislation is not required, significant change is already underway. A particular case in point concerns the FRC, where the Kingman Review has inspired

an urgent drive to deliver rapid, measurable improvements in audit quality. This has already created a major pressure for firms and an imperative to ensure full compliance with regulatory requirements and expectations in every audit they undertake.

By the time firms were conducting 2018/19 local audits, the measures which they were putting in place to respond to a more focused regulator, determined to achieve change, were clearly visible. To deliver the necessary improvements in audit quality firms were requiring their audit teams to undertake additional work to gain deeper levels of assurance. However, additional work requires more time, posing a threat to firms' ability to complete all of their audits by the target date for publication of audited accounts (then 31 July) – a threat accentuated by growing recruitment and retention challenges, the complexity of local government financial statements and increasing levels of technical challenges as bodies explored innovative ways of developing new or enhanced income streams to help fund services for local people.

This risk to the delivery of timely audit opinions first emerged in April 2019 when one of PSAA's contracted firms flagged the possible delayed completion of approximately 20 audits. Less than four months later, all firms were reporting similar difficulties, resulting in more than 200 delayed audit opinions.

2019/20 audits have presented even greater challenges. With Covid-19 in the mix both finance and audit teams have found themselves in uncharted waters. Even with the benefit of an extended timetable targeting publication of audited accounts by 30 November, more than 260 opinions remained outstanding. The timeliness problem is extremely troubling. It is deep-seated and has a range of causes. There are no easy solutions, and so it is vital that co-ordinated action is taken across the system by all involved in the accounts and audit process to address the current position and achieve sustainable improvement without compromising audit quality. PSAA is fully committed to do all it can to contribute to achieving that goal.

Delayed opinions are not the only consequence of the FRC's drive to improve audit quality. Auditors need to be paid for their additional work. As a result, many more fee variation claims have been received than in prior years. None of these problems are unique to local government audit. Similar challenges have played out throughout other sectors where increased fees and disappointing responses to tender invitations have been experienced during the past two years. All this paints a picture of an audit industry under enormous pressure and of a local audit system which is experiencing its share of the strain and unavoidable instability as impacts cascade down to the frontline of individual audits.

Local government audit will not be immune from these difficulties. The Council believes that opting into PSAA's national scheme will put them in a better position than those which choose to make their own separate arrangements. Firms are more likely to make positive decisions to bid for larger, long term contracts, offering secure income streams, than they are to invest in bidding for a multitude of individual opportunities.

The national scheme already offers a range of benefits for its members:

- transparent and independent auditor appointment via a third party;
- the best opportunity to secure the appointment of a qualified, registered auditor;

- appointment, if possible, of the same auditors to bodies involved in significant collaboration/joint working initiatives, if the parties believe that it will enhance efficiency and value for money;
- on-going 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;
- a value for money offer based on minimising PSAA costs and distribution of any surpluses to scheme members;
- 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;
- avoiding the necessity for local bodies to establish an auditor panel and undertake an auditor procurement, enabling time and resources to be deployed on other pressing priorities;
- providing regular updates to Section 151 officers on a range of local audit related matters and our work, to inform and support effective auditor-audited body relationships; and
- concerted efforts to develop a more sustainable local audit market.

However, the challenge for 2023 and beyond is to develop the scheme further, by listening to the feedback from scheme members, suppliers and other stakeholders and learning from the collective post-2018 experience. This work is already firmly underway. During the past three years the PSAA has taken a number of initiatives to improve the operation of the scheme for the benefit of all parties including:

- proactively and constructively engaging with the numerous high-profile industry reviews, including the significant Redmond Review into Local Authority Financial Reporting and External Audit;
- commissioning an independent review by consultancy firm Touchstone Renard of the sustainability of the local government audit market, which identified a number of distinctive challenges in the current local audit market. PSAA published the report to inform debate and support ongoing work to strengthen the system and help to deliver long term sustainability;
- working with MHCLG to identify ways to address concerns about fees by developing a new approach to fee variations which would seek wherever possible to determine additional fees at a national level where changes in audit work apply to all or most opted-in bodies;
- the establishment of a Local Audit Quality Forum, which is free of charge to opted-in bodies and has to date held five well attended events on relevant topics;
- PSAA attendance at meetings of the various Treasurers' Societies and S151 officers to share updates on our work, discuss audit-related developments, and listen to feedback;
- maintaining contact with those registered audit firms that are not currently contracted with the PSAA, to build relationships and understand their thinking on working within the local audit market;
- undertaking research to enable a better understanding of the outcomes of electors' objections and statements of reasons issued since our establishment in April 2015; and

- sharing PSAA experiences with and learning from other organisations that commission local audit services such as Audit Scotland, the NAO, and Crown Commercial Services.

Importantly, the PSAA is also currently working closely with a range of local audit stakeholders including MHCLG, FRC, NAO, and the LGA to help identify and develop further initiatives to strengthen the local audit. In many cases desirable improvements are not within PSAA's sole gift and accordingly it is essential that this work is undertaken collaboratively with a common aim to ensure that local government continues to be served by an audit market which is able to meet the sector's needs and which is attractive to a range of well-equipped suppliers.

One of PSAA's most important obligations is to make an appropriate auditor appointment to each opted-in body. Prior to making appointments for the second appointing period, commencing on 1 April 2023, the PSAA plan to undertake a major procurement enabling suppliers to enter into new long-term contracts with PSAA. If the procurement fails to attract sufficient capacity to enable auditor appointments to every opted-in body, we have fallback options to extend one or more existing contracts for the period spanning 2023/24 and 2024/25.

With the benefits outlined, the Council has indicated it wishes to opt into the PSAA national scheme and it is expected that in September 2021 eligible bodies will be formally invited to join. Full Council will need to then approve the decision and notify the PSAA by January 2022.

The PSAA procurement exercise will then commence in February 2022. The PSAA timeline shows that it intends to award contracts in June 2022 and confirm 2023/24 auditor appointments in December 2022.

### **Financial Implications**

Costs relating to the PSAA form part of the scale fee payable to the respective auditor.

### **Legal Implications**

Included within the body of this report.