

London Borough of Enfield

Council

24 February 2022

Subject: Retender of External Audit Arrangements - Opting into the National Procurement Arrangements

Cabinet Member: Cllr Mary Maguire

Executive Director: Fay Hammond

Key Decision: Yes

Purpose of Report

1. This report sets out proposals for appointing the external auditor to the Council for the auditing of the Statement of Accounts and Pension Fund Accounts for the five-year period from 2023/24.

Proposal

2. It is proposed that the Council accepts Public Sector Audit Appointments' invitation to opt into the sector-led option for the appointment of external auditors to principal local government for five financial years from 1 April 2023.

Reason for Proposal(s)

3. The purpose of this report is to recommend to Council the preferred option for the external audit arrangements. The General Purposes Committee considered the options and recommendation set out in this report regarding the external audit arrangements on 13 January 2022 at the informally held meeting.

Relevance to the Council's Corporate Plan

4. Sound finances contribute to all of the objectives in the Corporate Plan; external audit provides assurance regarding the financial arrangement of the Council.

Background

5. The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 accounts. Enfield, along with the majority of the public bodies (498 public bodies, 11 with their own arrangements) opted into the national arrangements for the procurement of external auditors via the PSAA

(Private Sector Audit Appointments) for the period covering the accounts for 2018/19 to 2022/23. Enfield were assigned BDO as auditors for five years from 2018/19 to audit the Statement of Accounts and Pension Accounts.

6. PSAA is now undertaking a procurement for the next appointing period, covering audits for 2023/24 to 2027/28. All local government bodies need to make important decisions about their external audit arrangements from 2023/24.
7. As set out in regulations, all relevant authorities listed in schedule 2 of the Local Audit and Accountability Act 2014 (the Act), are required to comply with Part 3 of the Act in relation to the appointment of local auditors. Section 7 of the Act requires a relevant authority to appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding financial year. For the 2023/24 accounts, a local auditor must be appointed by 31 December 2022. The council has three options.
 - To appoint its own auditor, which requires it to follow the procedure set out in the Act.
 - To act jointly with other authorities to procure an auditor following the procedures in the Act.
 - To opt in to the national auditor appointment scheme administered by a body designated by the Secretary of State as the 'appointing person'. The body currently designated for this role is Public Sector Audit Appointments Limited (PSAA).
8. If the Council wishes to take advantage of the national auditor appointment arrangements, it is required under the local audit regulations to make the decision at Council. The opt-in period closes on 11 March 2022.

The Role of the Appointed Auditor

9. The auditor appointed at the end of the procurement process will undertake the statutory audit of accounts and Best Value assessment of the council in each financial year, in accordance with all relevant codes of practice and guidance. The appointed auditor is also responsible for investigating questions raised by electors and has powers and responsibilities in relation to Public Interest Reports and statutory recommendations.
10. The auditor must act independently of the council and the main purpose of the procurement legislation is to ensure that the appointed auditor is sufficiently qualified and independent.
11. The auditor must be registered to undertake local audits by the Financial Reporting Council (FRC) employ authorised Key Audit Partners to oversee the work. As the report below sets out there is a currently a shortage of registered firms and Key Audit Partners.

12. Auditors are regulated by the FRC, which will be replaced by a new body with wider powers, the Audit, Reporting and Governance Authority (ARGA) during the course of the next audit contract.
13. Councils therefore have very limited influence over the nature of the audit services they are procuring, the nature and quality of which are determined or overseen by third parties.

Pressures in the current local audit market and delays in issuing opinions

14. Much has changed in the local audit market since audit contracts were last awarded in 2017. At that time the audit market was relatively stable, there had been few changes in audit requirements, and local audit fees had been reducing over a long period. 98% of those bodies eligible opted into the national scheme and attracted very competitive bids from audit firms. The resulting audit contracts took effect from 1 April 2018.
15. During 2018 a series of financial crises and failures in the private sector year led to questioning about the role of auditors and the focus and value of their work. Four independent reviews were 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. The recommendations are now under consideration by Government, with the clear implication that significant reforms will follow. A new audit regulator (ARGA) is to be established, and arrangements for system leadership in local audit are to be introduced.
16. The Kingman review has led to an urgent drive for the FRC to deliver rapid, measurable improvements in audit quality. This has created a major pressure for audit firms to ensure full compliance with regulatory requirements and expectations in every audit they undertake. By the time firms were conducting 2018/19 local audits during 2019, the measures they were putting in place to respond to a more focused regulator 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 the firms' ability to complete all their audits by the target date for publication of audited accounts. Delayed opinions are not the only consequence of the FRC's drive to improve audit quality. Additional audit work must also be paid for. As a result, many more fee variation claims have been needed than in prior years.
17. This situation has been accentuated by growing auditor recruitment and retention challenges, the complexity of local government financial statements and increasing levels of technical challenges as bodies explore innovative ways of developing new or enhanced income streams to help fund services for local people. These challenges have increased in subsequent audit years,

with Covid-19 creating further significant pressure for finance and audit teams.

Main Considerations for the Council

18. The external audit timeliness and challenges has been in the spotlight nationally with 14 Councils awaiting 2018-19 sign off of accounts, 62 Councils awaiting 2019-20. Only 8% of 2020/21 accounts signed off on time, albeit over 70% of council (including Enfield) published their accounts on time. The challenges of external audit capacity and skills is well documented in the public sector. The ability of the PSAA to influence or impact on this issue appears to be limited in the audit sector beyond reporting and monitoring the challenge. However, should the Council decide to independently appoint an external auditor the process is onerous. This paper briefs members on the options and concludes with a recommendation for Council to join the national arrangements for external audit procurement from 1 April 2023.
19. As background reading, the PSAA has issued a formal invitation for the Council to join the national scheme including their view on the benefits of joining the national framework. The LGA has written to all Local Authorities in support of the PSAA arrangements (Appendix A) which includes a set of Frequently Asked Questions. An overview of the implications of opting in /out is set out below.
20. The Society of London Treasurers is represented on a PSAA working group. The frustration of late audits and the unsatisfactory contract management of these arrangements are shared widely. However, this is weighed against the benefit of the national procurement arrangements and the view is that the majority of councils will continue to join the PSAA contracting arrangements. Anecdotally there are indications that the audit firms are unlikely to bid outside the PSAA arrangements.
21. Broadly the LGA paper recognises the current challenges in the audit arrangements but continues to believe that the PSAA represents the most expedient route. In addition, the LGA's view is that the perceived benefits of following an independent procurement, such as increased control and timeliness of the external audit, are not realisable.
22. A specific consideration for Enfield is the capacity of the Finance Team to support the additional requirements of the independent procurement process. This would divert focus from the Statement of Accounts production and audit cycle which is a key priority.

The national auditor appointment scheme

23. The PSAA is a not-for-profit organisation whose costs are around 4% of the scheme with any surplus distributed back to scheme members. In summary the national opt-in scheme provides the following:

- the appointment of a suitably qualified audit firm to conduct audits for each of the five financial years commencing 1 April 2023.
- 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 has sought 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 during the appointment period.
- minimising the scheme management costs and returning any surpluses to scheme members.
- consulting with authorities on auditor appointments, giving the Council/Authority 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.

Opting into the PSAA Arrangements

24. All bodies who wish to join the scheme must return a Notice of Acceptance Form no later than 11 March 2022.
25. Eligible bodies that have chosen to opt in to the appointing person scheme will have their auditor appointed by PSAA by 31 December 2022, following a consultation about the proposed appointment.
26. The PSAA's procurement process will start in February 2022 on the basis of 80% quality (of which 4% is social value) and 20% price. The intention is to create 7 to 10 contract lots to encourage a wider market engagement (currently the market is dominated by EY and Grant Thornton market share). Quality measures include resourcing, capacity and capability, communication, transition arrangements.
27. If the procurement fails to attract sufficient capacity, there is an option to extend the current contract for a further two years, until 2024/25.

Opting out of the PSAA Arrangements

28. Should the Council decide not to the PSAA framework, there are two options for appointing an external auditor:
 - undertake an individual auditor procurement and appointment exercise; or
 - undertake a joint audit procurement and appointing exercise with other bodies.

29. An independent audit panel must be set up that is responsible for the appointment of the external auditors. This panel (minimum of three) must consist of a majority of independent members (or wholly of independent members) and must be chaired by an independent member. A guide to auditor panels for local government authorities was issued by CIPFA in 2017. This helpfully specifies a framework including protocols for the recruitment of the independent panel members, defining “independent person” (a primary consideration), the function of the Independent Audit Panel and appointment process. <https://www.cipfa.org/policy-and-guidance/publications/g/guide-to-auditor-panels-pdf>
30. Within the period of 28 days beginning with the day on which the auditor appointment is made, section 8 of the Act requires a body that has not opted in to the national appointing person arrangements to publish a notice that:
 - a. states that it has made the appointment.
 - b. identifies the local auditor that has been appointed.
 - c. specifies the period for which the local auditor has been appointed.
 - d. sets out the advice, or a summary of the advice, of its auditor panel about the selection and appointment of a local auditor; and
 - e. if it has not followed that advice, sets out the reasons why it has not done so.

Proposal

31. Following consideration of the options for the external audit contracting arrangements, it is recommended that the Council accept the invitation to join the national procurement arrangements. The sector-wide procurement conducted by PSAA is expected to produce better outcomes and will be less burdensome for the Council/Authority than a procurement undertaken locally because:
 - collective procurement reduces costs for the sector and for individual authorities compared to a multiplicity of smaller local procurements.
 - if the national appointment arrangements are not accessed, the Council/Authority will need to establish its own auditor panel with an independent chair and independent members to oversee a local auditor procurement and ongoing management of an audit contract.
 - it is the best opportunity to secure the appointment of a qualified, registered auditor - there are only nine accredited local audit firms, and a local procurement would be drawing from the same limited supply of auditor resources as PSAA’s national procurement; and
 - supporting the sector-led body offers the best way of to ensuring there is a continuing and sustainable public audit market into the medium and long term.

Safeguarding Implications

32. None arising directly from this report.

Public Health Implications

33. None arising directly from this report.

Equalities Impact of the Proposal

34. None arising directly from this report.

Environmental and Climate Change Considerations

35. None arising directly from this report.

Risks that may arise if the proposed decision and related work is not taken

36. The principal risks are that the Council/Authority are that the council fails to appoint an auditor in accordance with the requirements and timing specified in local audit legislation.

Risks that may arise if the proposed decision is taken and actions that will be taken to manage these risks

37. The principal risks are that the Council/Authority are that the proposed arrangements: do not achieve value for money in the appointment process; or the arrangements fail to drive improvements in the timeliness and capacity in the audit arrangements.

38. The national procurement arrangements competitive tender process measuring price and quality aims to mitigate for these risks.

Financial Implications

39. The external audit fees will need to be funded through the medium-term financial plan. As set out in this report, the audit fees are expected to increase nationally. This additional cost has been recognised by the government with the introduction of a national grant.

40. The PSAA surplus is distributed to Council, this is £3,720 for the Pension Fund and £26,020 for the main audit from the national pot of £5.6m.

Legal Implications

Prepared by CP based on version of Report circulated on 19th December 2021.

The Local Audit and Accountability Act 2014 ('the Act') established arrangements for the audit and accountability of relevant authorities as listed in Schedule 2 of the Act, including local authorities, clinical commissioning groups and police and crime commissioners in England. PSAA is specified as an appointing person under the Act and regulation 3 of the Local Audit (Appointing Person) Regulations 2015. The statutory regime underpinning the appointment of external auditors by local authorities is detailed within this Report.

The Council should satisfy itself that the auditor appointment process carried out by PSAA is compliant with applicable procurement law, and all relevant contract

documentation should be in a form approved by Legal Services on behalf of the Director of Law and Governance.

Workforce Implications

41. None arising directly from this report.

Property Implications

42. None arising directly from the report.

Other Implications

43. None

Options Considered

44. As set out in the report, there are two options for the procurement of external auditors.

Conclusions

45. The options for external audit is to utilise the national contract through the PSAA or for the council to procure directly. The pros and cons of the various options are considered in this report for comments. The timetable for decision is 13 January 2022 GPC and February 2022 Council, in advance of the 11 March 2022 deadline.

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14 February 2022

Appendices

Appendix A – LGA letter to Councils regarding the PSAA

Background Papers

Appendix A

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 Ian Davis,

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 11th 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) if you have any issues you would like to raise.

Yours sincerely



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 11th 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 of 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).

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).