

Crawley Borough Council

Report to Audit Committee

14 December 2021

Provision of External Audit Services

Report of the Head of Corporate Finance – FIN/548

1. Purpose

- 1.1 The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 accounts. As agreed in report [FIN/397](#) in November 2016, the Council opted into the 'appointing person' national auditor appointment arrangements established by Public Sector Audit Appointments (PSAA) for the period covering the accounts for 2018/19 to 2022/23.
- 1.2 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. They 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 PSAA. The purpose of this report is to decide whether to opt-in to the PSAA procurement or to procure alone. A decision by Full Council is required before 11 March 2022 if the PSAA route is taken.
- 1.3. The Audit Committee have not been satisfied with the service provided by PSAA and may wish to consider an alternative provision going forward.
- 1.4. The decision whether to opt-in to the PSAA contract or not is very finely balanced. There is no doubt that our future audits will be more expensive than at present whichever route Council chooses. The large audit firms have told us it is likely timeliness will not improve whichever route the Council takes. Procuring alone carries the chance the Council may not find an auditor, or may find one that may not deliver on time. In addition, if we were to procure alone the choice of auditors is limited, with the majority being the same auditors used by PSAA, which could mean we may not be seen as an attractive contract. Going alone also carries the risk that the Council will not be able to appoint an auditor at all and the [Financial Reporting Council](#) will do so on our behalf. Going alone also carries a high administrative burden.
- 1.5. This report concludes that going with the PSAA is unlikely to lead to any improvements based on track record. This is because we are a lower tier authority and therefore a lower priority to the large audit firms.

2. Recommendation

- 2.1. That the Full Council (at its scheduled meeting on 23 February 2022) be recommended to either:
 - a) Continue the status quo and accept the Public Sector Audit Appointments' (PSAA) invitation to opt-in to the sector-led appointment to external auditors for five financial years from 1 April 2023.

OR

- b) Decline the PSAA's invitation, and undertake our own procurement of an external auditor including the requirement to appoint an Independent Panel to oversee the completion of the procurement process by 31 December 2022.

3. Reasons for the Recommendation

- 3.1. The current auditor appointment arrangements cover the period up to and including the audit of the 2022/23 accounts. The Council opted-in to the 'appointing person' national auditor appointment arrangements established by Public Sector Audit Appointments (PSAA) for the period covering the accounts for 2018/19 to 2022/23.
- 3.2. Under the Local Government Audit & Accountability Act 2014 ("the Act"), the Council is required to appoint an auditor to audit its accounts for each financial year. 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).
- 3.3. In order to opt-in to the national scheme, the Council must make this decision at a meeting of the Full Council and inform PSAA by 11 March 2022.

4. Background

- 4.1. As the next scheduled meeting of the Full Council is due to take place the day after this Audit Committee, it is proposed that the Audit Committee's recommendation be put before the Full Council meeting on 23 February 2022 as the decision is not time-critical.
- 4.2. 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 audits irrespective of whether an eligible body decides to opt-in to PSAA's national scheme or chooses to make its own separate arrangements. The requirements are mandatory; they shape the work auditors undertake and have a bearing on the actual fees required.
- 4.3. There are currently nine audit providers eligible to audit local authorities and other relevant bodies under local audit legislation. This means that a local procurement exercise would seek tenders from the same firms as the national procurement exercise, subject to the need to manage any local independence issues. Local firms cannot be invited to bid unless they are on this list. Local procurements must deliver the same audit scope and requirements as a national procurement, reflecting the auditor's statutory responsibilities. The [nine firms included](#) on the list are: BDO, Cardens Accountants (based in Hove), Deloitte, Ernst & Young, Grant Thornton, KPMG, Mazars, PriceWaterhouseCoopers, Azets Audit Services Ltd.
- 4.4. 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. In addition there would be a requirement to have a housing benefits audit/assurance on behalf of the Department of Works and Pensions. 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.

- 4.5. The auditor must act independently from the Council, and the main purpose of the procurement legislation is to ensure that the appointed auditor is sufficiently qualified and independent.
- 4.6. The auditor must be registered to undertake local audits by the Financial Reporting Council and employ authorised Key Audit Partners to oversee the work. As the report sets out below there is a currently a shortage of registered firms and Key Audit Partners.
- 4.7. Auditors are regulated by the Financial Reporting Council, 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.
- 4.8. 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.
- 4.9. The Council may choose to appoint its own external auditor under the Act. To do this the Council would have to:
 - Establish an independent auditor panel to make a stand-alone appointment. This auditor panel would need to be set up by the Council itself, and 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, excluding current and former elected Councillors (or officers) and their close families and friends. This means that elected Councillors will not have a majority input to assessing bids and choosing which audit firm to award a contract to for the Council's external audit.
 - Manage the contract for its duration, overseen by the Auditor Panel.
 - Alternatively, join with other authorities to establish a joint auditor panel, as enabled by the Act. Again, this will need to be constituted wholly of, or a majority of, independent appointees. 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.

4.10. **The National Auditor Appointment Scheme**

PSAA is specified as the 'appointing person' for principal local government under the provisions of the Act and the Local Audit (Appointing Person) Regulations 2015. PSAA procured five-year audit services contracts in 2017 for the first appointing period, covering audits of the accounts from 2018/19 to 2022/23. It is now undertaking the work needed to invite eligible bodies to opt-in for the next appointing period, from the 2023/24 audit onwards, and to complete a procurement for audit services. 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
- on-going contract and performance management of the contracts once these have been let.

4.11. Pressure Experienced by Crawley Borough Council Arising from the Market Issues

4.11.1. Crawley Borough Council's PSAA appointed auditors for the period are Ernst and Young (EY). The Finance team have completed the Council's draft accounts by the due date for all set deadlines to be ready for the audit. However EY audits like other external auditors have failed to meet deadlines throughout the audit. The current audit is still being undertaken. EY delayed Crawley due to the housing rents issue, however the audit was being pushed back significantly prior to them being informed of this issue.

4.11.2. Reasons for delays include lack of staff and instructions from senior management at EY to prioritise County and Unitary authorities. The late audit this year is creating further pressure on the Finance, Property and Benefits teams at the same time as setting the budget, dealing with the housing issue and preparing for benefits annual billing.

4.11.3. A letter was received from the Department for Levelling Up, Housing and Communities (DLUHC) stated that an unprecedented 91% of 2020/21 local audits have missed the statutory deadline for 30 September.

4.12. The Invitation from PSAA

4.12.1. PSAA is now inviting the Council to opt-in for the second appointing period, for 2023/24 to 2027/28, along with all other eligible authorities. Based on the level of opt-ins, it will enter into contracts with appropriately qualified audit firms and appoint a suitable firm to be the Council's auditor. Details relating to PSAA's invitation are provided in Appendix A to this report.

4.12.2. The prices submitted by bidders through the procurement will be the key determinant of the value of audit fees paid by opted-in bodies. PSAA has said it will:

- seek to encourage realistic fee levels and to benefit from the economies of scale associated with procuring on behalf of a significant number of bodies;
- continue to pool scheme costs and charge fees to opted-in bodies in accordance with the published fee scale as amended following consultations with scheme members and other interested parties ("pooling" means that everyone within the scheme will benefit from the prices secured via a competitive procurement process – a key tenet of the national collective scheme);
- continue to minimise its own costs, around 4% of scheme costs and, as a not-for-profit company, will return any surplus funds to scheme members. In 2019 it returned a total of £3.5million to relevant bodies and in 2021 a further £5.6million was returned.

4.12.3. PSAA has said it will seek to encourage market sustainability in its procurement. Firms will be able to bid for a variety of differently sized contracts so that they can match their available resources and risk appetite to the contract for which they bid. They will be required to meet appropriate quality standards and to reflect realistic market prices in their tenders, informed by the scale fees and the supporting information provided about each audit. Where regulatory changes are in train which affect the amount of audit work suppliers must undertake, firms will

be informed as to which developments should be priced into their bids.

5. Changes in the Audit Market Since the Last Audit Contract Was Awarded

- 5.1. 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.
- 5.2. During 2018 a series of financial crises and failures in the private sector 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, 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. Further change will follow as other recommendations are implemented.
- 5.3. The Kingman review has led to an urgent drive for the Financial Reporting Council 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 Financial Reporting Council'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.
- 5.4. 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.
- 5.5. None of these problems are unique to local government audit. Similar challenges have played out in other sectors, where increased fees and disappointing responses to tender invitations have been experienced during the last two years.

6. Options for Procuring External Audit Services

- 6.1. There are three main options for the Audit Committee, and the Full Council, to consider in deciding whether to join the PSAA tender.

Option One – Join the PSAA Tender

For:

- Avoids the need for an independent panel.
- Lowest workload for the Council's officers in letting the contract.
- Administrative costs of running the contract are limited to 4%.

Against:

- Delivery will probably remain variable and put pressure on our Finance service if audits are completed after the 30 September deadline.
- Price will be higher than at present due to the 80/20 quality/price split. It is not clear from consultation whether this will be the best price available but it was in the 2017 contract let.
- Price increases in the contract period are made by the PSAA.

Option Two – Tender Alone

For:

- Crawley Borough Council with its independent panel will decide lot size.
- There is a chance our terms and conditions might lead to delivery on time, although they may not.

Against:

- There is a risk there will be no bids. Our understanding is this leads to an appointment of an auditor by the Financial Reporting Council or its successor body on behalf of the Government.
- The workload for Council officers will be higher than PSAA route but lower than tendering with others.
- Price will be higher than at present, it is not known if this will be cheaper or more expensive than the PSAA route. The PSSA has economies of scale.
- Housing benefit assurance audit would also be required, this may have to be separately procured due to the complexities of the audit and there are efficiencies of scale by using the same auditor.
- Administrative costs of running the contract are unknown.

Option Three – Tender with other Neighbouring Councils

For:

- Crawley Borough Council with its independent panel will decide lot size.
- There is a chance our terms and conditions might lead to delivery on time, although they may not.

Against:

- Further legal advice on the constitution of an independent panel with partners will be needed.
- The workload of the Head of Corporate Finance and Head of Legal, Governance and HR and their staff will be the highest from this option because of the complexity of lots and a wider independent panel.
- There is a risk there will be no bids. Our understanding is this leads to an appointment of an auditor by the Financial Reporting Council or its successor body.
- Price will be higher than the PSAA tender. It seems unlikely there will be much economies of scale over the tender alone route.
- Administrative costs are unknown.

- 6.2. In reality PSAA have a monopoly over the situation as there are currently nine audit providers eligible to audit local authorities and other relevant bodies under local audit legislation which means that even if the Council opted for a local procurement exercise it would be seeking tenders from the same firms as the national procurement exercise undertaken by PSAA.

7. Information & Analysis Supporting Recommendation

- 7.1. The Audit Committee needs to consider this finely balance decision in detail. On reaching a conclusion it must make a recommendation to the Full Council on 23rd February 2022.
- 7.2. If the Council decides not to join PSAA arrangement the Head of Legal, Governance and HR will advertise for people to join the independent panel after the February 2022 full Council, prepare tender documents and advertise in late spring. The appointment of the auditor will be made by the Full Council no later than at its meeting in December 2022.
- 7.3. One of our partners in the shared procurement service is interested in a possible joint procurement so a procurement could be run by the team at the same time.

8. Implications

Financial

- 8.1. Not joining PSAA will lead to more work for Council officers during the tender process and the audits.
- 8.2. The new audit contract will cost more than the current one. This is inevitable due to the changes in the industry. This will appear in the 2023/24 budget.

Legal

- 8.3. Section 7 of the Local Audit and Accountability Act 2014 (“the Act”) requires a relevant Council to appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding year, in this case 31 December 2022.
- 8.4. Section 8 of the Act governs the procedure for appointment including that the Council must consult and take account of the advice of its auditor panel on the selection and appointment of a local auditor. Section 8 provides that, where a relevant Council is a local Council operating executive arrangements, the function of appointing a local auditor to audit its accounts is not the responsibility of an executive of the Council under those arrangements.
- 8.5. Section 12 of the Act makes provision for the failure to appoint a local auditor. In such an event, the Council must immediately inform the Secretary of State, who may direct the Council to appoint the auditor named in the direction or appoint a local auditor on behalf of the Council. This could occur if no listed auditors applied for the work.

9. Background Papers

[Appointment of External Auditor – Report to Audit Committee 29 November 2016 \(FIN/397\)](#)

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