

Future of Public Audit Report of the County Treasurer

Please note that the following recommendations are subject to confirmation by the Committee before taking effect.

Recommendation: that Members

- i. Note the proposed appointment of Grant Thornton LLP as External Auditors of Devon County Council from 2012/13
- ii. Note the DCLG proposals for the Future of Public Audit

1 INTRODUCTION

- 1.1 On 13 August 2010, the Secretary of State for Communities and Local Government announced plans to disband the Audit Commission and refocus audit on helping local people hold their councils and other local public bodies to account for local spending decisions.
- 1.2. Following this announcement the Secretary of State proposed that in future local authorities would be able to appoint their own external auditors and in March 2011 launched a consultation document on the Future of Public Audit. However it was recognised that such a framework could not be introduced immediately so the Audit Commission were asked to run a procurement exercise to appoint new external auditors with effect from 2012/13. Following an EU Procurement Exercise a number of private sector providers and the previous in-house Audit Practice were invited to tender for 10 contracts spread over 4 geographical regions.

2 BACKGROUND

- 2.1 Since 1983, the Audit Commission has acted in roles of regulator, commissioner and provider of local public audit services. The current system is governed by the provisions of the Audit Commission Act 1998.
- 2.2 Following the announcement of its decision to abolish the Audit Commission in August 2010, the Government consulted on its proposals for a new local public audit framework from 31 March to 30 June 2011. Those proposals were designed to deliver the Government's objective for a new local public audit framework that places responsibility firmly in the hands of local bodies, giving them the freedom to appoint their own auditors, with appropriate safeguards for auditor independence, from an open and competitive market for local public audit services. They were also designed with the fundamental principle of accountability in mind – providing a system of local public audit that allows local bodies to be held to account for the public money at their disposal, locally to residents and service users, and also as part of a framework of accountability that provides assurance to Parliament about the public money it votes to Government departments and which is in turn devolved to the local level.
- 2.3. The proposals in the consultation paper covered all local public bodies except health bodies and probation trusts.

- 2.4.. Following the end of the Consultation process in June, the Department for Communities and Local Government (DCLG) have been considering the feedback received and have now published their response. A total of 453 responses to the consultation were received, the majority from local government. The Government response sets out the key themes and views which were raised during the consultation and what the Government now proposes for the new arrangements for audit of principal public bodies. This report outlines the key features of the DCLG response and the implications for local authorities,
- 2.5. The Audit Commission has recently announced the results of the process of outsourcing all the audit work of its in-house practice. The outsource contracts that the Commission will put in place will start from 2012-13 and will run for five years giving local councils and other public bodies the time to plan for appointing their own auditors. As a result of the outsourcing, a single provider will be responsible for undertaking the external audit of all public bodies in the south west. Once the audits have been outsourced the Commission will be radically reduced in size to become a small residuary body responsible for overseeing the contracts and making any necessary changes to the individual audit appointments during the life of the contracts.

3. APPOINTMENT OF AUDITOR FOR 2012/13 – 2016/17

- 3.1. As a result of the outsourcing referred to above Grant Thornton LLP have been chosen as the provider of External Audit services to public bodies within the South West region. This includes Devon County Council.
- 3.2. Following the end of the procurement process, there will be a consultation period with audited bodies on the appointment of their new auditors. The appointments will be formally approved by the Commission's Board in July. Appointments for 2012/13 will commence on 1 September, with Audit Commission staff transferring to the new suppliers on 31 October 2012. It is expected that changes to the appointments will only be necessary where there are conflict of interest issues with the proposed appointment such as a firm having a prior or current business relationship with an audited body – such as providing consultancy services directly relevant to auditors' responsibilities (for example in relation to a PFI scheme or the provision of internal audit services) – which would preclude the Commission appointing the firm, or the firm accepting appointment, as the auditor to that body
- 3.3. Where an audited body objects to the proposed appointment, it should set out in writing good reasons why the proposed appointment should not be made. The following grounds may amount to good reasons.
- There is an independence issue, of which the Commission and/or the firm was previously unaware, which would preclude the Commission appointing the firm – or the firm accepting appointment – as the auditor to a particular body.
 - The audited body is involved in formal and on-going joint working arrangements (for example, joint management team or shared back office functions or joint provision of major services with neighbouring bodies), which means it would be more appropriate for those bodies to have the same auditor.
 - There is another specific good reason – for example, a body can demonstrate a history of inadequate services from a particular firm.
- 3.4. The 2012/13 audit fees will be approved by the Commission Board and announced in April 2012. The procurement has been the result of a rigorous assessment of each bidder against published cost and quality criteria, and according to the Audit Commission will mean significant audit fee savings of up to 40% for local councils, NHS trusts and other local bodies. Public bodies are expected to save over £30 million a year for the length of the contracts. Together

with additional savings of £19 million a year achieved through the Commission's own internal efficiencies, the result will be an expected £250 million (or 40 per cent) fall in audit fees for most local public bodies over five years. The Audit Commission have stated that the outcome of the procurement will promote a skilled, well-resourced and diverse public audit market.

- 3.5. As part of the transition arrangements and to support the consultation process, the Audit Commission are arranging a series of introductory meetings in each contract area between 30 April and 16 May. The purpose of these meetings is to give audited bodies in each area an opportunity to meet the new firm proposed as their auditor and its senior partners, and hear how the firm plans to manage its new portfolio and its approach to the audits. The date for the South West region (which includes Avon, Cornwall, Devon, Dorset, Gloucestershire, Somerset and Wiltshire) is expected to be 11th May 2012.

4 KEY ELEMENTS OF THE NEW LOCAL PUBLIC AUDIT FRAMEWORK APRIL 2017 ONWARDS

- 4.1. Following the completion of the outsourced contracts up to 2016/17 financial year, assuming appropriate legislation is in place, the proposed new framework will allow public bodies to appoint their own Auditors. Such appointments would need to be made in December 2016 for the 2017/18 financial year. The design principles of the new framework for local public audit are that it should be localist and transparent, achieve a reduction in the overall cost of audit, and uphold high standards of auditing, ensuring that there is effective and transparent regulation of public audit, and conformity to the principles of public audit. The key elements within the DCLG response are referred to below with references to the detailed document:

REGULATION

- 4.2. The **National Audit Office** will produce the Code of Practice and supporting guidance for audit of local public bodies, subject to Parliamentary approval. The National Audit Office will be required to consult key partners in developing the Code
- 4.4. The **Financial Reporting Council** will be the overall regulator, mirroring its role under the Companies Act 2006. The Financial Reporting Council will be responsible for recognition and supervision of **Recognised Supervisory Bodies** (professional accountancy bodies responsible for supervising the work of auditors, and for putting rules and arrangements in place which their members must fulfil before they can be registered auditors) and for **Recognised Qualifying Bodies** (professional accountancy bodies responsible for awarding audit qualifications).
- 4.5. Mirroring the Companies Act 2006, Recognised Supervisory Bodies will have the roles of registration, monitoring and discipline for local public audit, put in place rules and practices covering eligibility of firms to undertake local public audit; and keep a register of firms eligible to undertake local public audit. As under the Companies Act 2006, Recognised Supervisory Bodies will monitor the quality of audits undertaken by their member firms, and investigate complaints, disciplinary cases and issues identified during the monitoring of firms on the register of local public auditors.

COMMISSIONING LOCAL PUBLIC AUDIT SERVICES

Auditor Appointment

- 4.6. Local public bodies will have a duty to appoint an auditor from the register of local public auditors, on the advice of an Independent Auditor Appointment Panel. The Independent Audit

Appointment Panel will have an independent chair and a majority of independent members. Local public bodies will be able to share appointment panels (and therefore independent members) to ease admin burdens and reduce costs.

- 4.7. The appointment process will be transparent. Local public bodies will be required to publish details of the auditor appointment on their website within 28 days of making the appointment, together with the Independent Audit Appointment Panel's advice and, if they did not follow that advice, a statement explaining why.

Role of Independent Auditor Appointment Panels

- 4.8. Government intends to prescribe specific functions to the Independent Audit Appointment Panel limited to the external audit, including advising on auditor appointment, independence, removal and resignation, and in relation to public interest reports. The arrangements will allow local public bodies to share Independent Audit Appointment Panels, and to expand on the remit of their Panel if they wish, choosing a model which best suits their circumstances. The Government will work with the public sector to produce guidance as to how the responsibilities of the Independent Auditor Appointment Panels might interface with those of the traditional Audit Committee.

Failure to Appoint an Auditor

- 4.9. Local public bodies will be required to appoint an auditor by 31 December in the year preceding the financial year to be audited, and notify the Secretary of State if they have not done so. The Secretary of State will be able to direct the local public body to appoint an auditor or make the auditor appointment directly. In addition to meeting the cost of the appointment the local public body could be subject to a sanction for failing to make the appointment.

Rotation of Audit firms and Audit staff

- 4.10. Local public bodies will be required to run a procurement competition for its audit services at least every five years. Auditors will have to comply with the standards and rules set by the regulator. Applying the current standards means the audit engagement partner will be able to undertake audit for a local public body for an initial five years and be reappointed for a further two years. The audit manager will be able to be appointed for a maximum of ten years. After these periods, these key audit staff will not be able to work with the local public body for a further five years.

Resignation or Removal of an Auditor

- 4.11. There will be rigorous, transparent processes for auditor resignation or removal, designed to protect auditor independence, quality of audit, and accountability to the electorate. These broadly mirror those in the Companies Act, but are adapted to reflect the principles of public audit.

Auditor liability

- 4.12. Auditor liability should be an issue to be dealt with in the contractual negotiations between the auditor and audited body.

Scope of Local Public Audit and Auditors' work

- 4.13. The scope of local public audit will remain broadly similar. As now, auditors of local public bodies will be required to satisfy themselves that the accounts have been prepared in

accordance with the necessary directions; proper practices have been observed in the compilation of the accounts; and the body has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The detail of how auditors should fulfil these requirements will, as now, be set out in a code of audit practice. The value for money component should be more risk based and proportionate, with auditors basing their assessment of risk on evidence of the local public body's arrangements for securing value for money provided by the local public body, possibly in the Annual Governance Statement and other documents.

- 4.14. The duty for auditors of local public bodies to undertake Public Interest Reporting will be retained, as will their ability to charge audited bodies for reasonable work.. A new duty will be placed on audited bodies to publish the Public Interest Report.
- 4.15. Auditors will be permitted to provide non-audit services to the audited body, subject to adhering to the Auditing Practices Board's ethical standards and the Independent Auditor Appointment Panel's approval.
- 4.16.. The local public auditor and the Independent Auditor Appointment Panel will be defined as designated persons under the Public Interest Disclosure Act, to enable individuals to make disclosures under the Act.
- 4.17.. The new framework will retain the rights of local electors to make formal objections to the accounts, but give auditors greater discretion regarding whether to pursue an objection.

5. IMPLEMENTATION AND NEXT STEPS

- 5.1. The Government plans do some further work with smaller bodies and their representatives on regarding audit arrangements for smaller bodies, to explore options for these bodies before firming up proposals, and setting out a preferred approach in Spring 2012;
- 5.2. The Government will hold further discussions with local authorities, other local public bodies and the audit sector to flesh out the underlying detail of the framework, and how it might be implemented;
- 5.3. The Government intends to publish a draft Bill for pre-legislative scrutiny in Spring 2012, which allows for examination and amendments to be made before formal introduction to Parliament; and in advance of introduction of an Audit Bill as soon as Parliamentary time allows.

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Electoral Divisions: All

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Background Paper: None