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Future arrangements for Audit

Purpose of report

For discussion and direction.

Summary

This report updates members on the current position with regard to the Government's proposals for the future of local public audit and invites members' views.

The report also updates members on the current procurement process and the option of three or five year contracts.

Julie Carney, Deputy Director, Local Government Policy and Productivity, DCLG will attend the meeting.

Recommendation

Members are invited to comment on the Government's proposals.

Action

Officers to pursue in the light of members' comments.

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Future arrangements for Audit

Background

In 2010 the Secretary of State announced plans to disband the Audit Commission and refocus audit on helping local people hold councils and local public bodies to account for local spending decisions – including giving councils the freedom to appoint their own auditors from a more open and competitive market.

In summary the Audit Commission's responsibilities for overseeing and delivering local audit and inspections will stop; the Commission's research activities will end; audit functions will be moved to the private sector; councils will be free to appoint their own independent external auditors from a more competitive and open market; and there will be a new audit framework for local health bodies.

On 30 March DCLG published a consultation paper on the future of public audit, available to view via:

<http://www.communities.gov.uk/publications/localgovernment/localpublicauditconsult>

The LGA welcomed the proposals to allow councils to appoint their own auditors and whilst acknowledging the need for appropriate safeguards to preserve the independence of audit expressed concern that the new approach should not become over regulated and prescribed. Specifically the proposal for statutory audit committees with a majority of independent members was regarded as both excessive and unnecessary. A summary of the key points of the LGA response is **attached**.

Developing proposals on the future of local public audit:

DCLG has published a response to the responses it received to the consultation. The response sets out the key themes and views expressed during the consultation and what the Government now proposes for the future of local public audit. A copy is here <http://www.communities.gov.uk/news/corporate/2060456>

In summary the DCLG paper confirms that, with regard to Audit:

- Councils will be under a statutory duty to appoint an auditor from the register of local public auditors;
- The appointment must be made by full council on the advice of an Independent Audit Appointment Panel (IAAP);
- The IAAP will be independently chaired with a majority of independent members;

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- The requirements will be framed in a way to allow local public bodies to share appointment panels (and therefore independent members) to ease the administrative burdens and reduce costs;
- The Government will prescribe specific functions to the IAAP around advising on auditor appointment, independence, removal and resignation and in relation to public interest reports – but there will flexibility to expand the remit of Panels to respond to local circumstances;
- Councils will be required to appoint an auditor by 31 December in the preceeding year and to notify the Secretary of State if they have not done so;
- Councils will be required to run a procurement competition for audit services at least every five years;
- There will be rigorous, transparent processes for auditor resignation or removal which broadly mirror those in the Companies Act;
- The current scope of local public audit will be retained – including the current Value for Money component – although the document signals that the Government believes this could be delivered in a more risk based and proportionate way;
- Further consideration will be given to proposals for the future audit of smaller public bodies, which will be set out in Spring 2012.

On grant certification the paper signals that, following the closure of the Audit Commission, grant paying bodies will need to develop new arrangements for certification – which could include self-certification.

As regards national value for money studies the paper indicates the Government's view that there is scope for rationalising the number of studies relating to the local public sector and that it would like to see the development of a coherent programme across providers including NAO, Government, and the LGA.

Comment: Whilst the LGA has welcomed the proposal to allow councils to appoint their own auditors it is clear that this is still some considerable way off and will, in practice, depend on the length of the contracts issued as a result of the current procurement process (see below).

Proposals around the appointment of auditors confirm our earlier concerns that the new approach is in danger of becoming over regulated and unduly prescriptive. However DCLG intend to ensure the new arrangements are flexible enough to allow councils to share appointment panels and undertake joint procurement exercises. DCLG also intend to work closely with the sector to ensure the arrangements are as straightforward as possible.

There also appears to be some prospect of helpful changes on grant certification and value for money – though this too will depend on the detail.

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Next steps: Government intends to publish a draft Bill for pre-legislative scrutiny in Spring 2012. In the meantime DCLG plan to hold further discussions with local public bodies to flesh out the underlying detail of the framework and how it might be implemented. DCLG are currently working with regional LGAs/improvement organisations to arrange some discussions during January – details of which have been circulated separately to Board members.

Audit procurement

Government has decided that the best route for transferring the Audit Commission's audit function to the private sector should be by way of outsourcing the work.

Sir Bob Kerslake wrote to Chief Executives on 28 July explaining that DCLG has been considering how long the outsourced contracts should be - with options ranging from three to five years from 2012/13. Whilst longer contracts might achieve greater value for money they would also delay the point at which councils would be free to appoint their own auditors (if the contracts were for five years then the first year for which councils will have been able to appoint their own auditors will not be until 2017/18).

The Audit Commission has launched the process for outsourcing the work of its Audit Practice. Further details are here <http://www.audit-commission.gov.uk/aboutus/future/pages/timetable-for-outsourcing-process.aspx>

The Commission has invited 13 potential providers who have met the pre qualification requirements to tender (more than twice the number currently in the market). Deadline for tenders was 16 December – following which a decision will need to be taken about whether to go for 3 or 5 year contracts. Formally speaking this is for the AC Board – in discussion with DCLG – but Sir Bob Kerslake's letter indicated that “...we want to talk to the sector about this trade off (*between earlier ability to appoint auditors and potentially lower fees*) once we have a better sense of the difference this makes to audit fees.”

Once the audits have been outsourced the Commission will be further reduced in size to become a small residuary body responsible for overseeing the contracts and making any necessary changes to individual audit appointments during the life of the contracts.

An update on the progress of the procurement process will be provided at the Board meeting.

Recent Audit Commission reports:

Audit Commission report: “Tough Times” This Audit Commission report published on 17 November provides a comprehensive picture of how councils are responding

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to the current financial climate. The report found that despite the challenges most councils were coping well and auditors expected 90% of councils to balance their 2011/12 budget.

<http://www.audit-commission.gov.uk/nationalstudies/localgov/Pages/toughtimes.aspx>

Auditing the Accounts 2010/11 This Audit Commission report published on 15 December found that overall councils maintained their standard of performance on financial reporting for 2010/11 and that this was a notable achievement given that they had to face the challenge of preparing their accounts for the first time in accordance with the International Financial Reporting Standards (IFRS). The audit opinion was issued by 30 September 2011 at 328 out of 356 councils (compared with 329 last year).

<http://www.audit-commission.gov.uk/pressoffice/pressreleases/Pages/auditingtheaccounts1011pr.aspx>

Financial Implications

There are no additional financial implications for the LGA arising as a result of this report.

Annex A

**LGA response to DCLG consultation paper on the future of local public audit -
summary of key points:**

- Future arrangements for the Audit Commission's activities need to be set within the context of the Coalition Government's approach to transparency and stronger local, rather than national, accountability.
- External audit makes an important contribution to the stewardship of public resources, but the current arrangements can be improved.
- Councillors, local people and communities should be the primary audience for audit and a simpler and more easily understandable framework for published accounts is required.
- We welcome the proposal that councils should appoint their auditors.
- We fully acknowledge the need for appropriate safeguards to preserve the independence of audit and ensure public trust in the process and outcomes is not jeopardised. But at the same time we are concerned that the new approach to audit does not become over regulated and prescribed through Government guidance
- Audit Committees - This proposal is both excessive and unnecessary. It is reminiscent of the standards committees which the government recently recognised were overly bureaucratic and runs contrary to the Government's agenda around devolution and localism. Moreover there will still be a regulatory framework including the registration of auditors and monitoring of the quality of audits.
- Procurement: There needs to be sufficient flexibility in the arrangements for procuring audit to enable a number of organisations to work together to jointly procure audit across a local area.
- Scope of Audit: The scope of audit should in future be more tightly focussed around the accuracy of the financial statements and issues of probity (that the authority's financial activities are materially free from fraud and corruption).
- The new arrangements must deliver a competitive market. This is more likely where future arrangements do not dissuade smaller audit firms from entering the market.
- There is a need for greater clarity around the timescales for when councils will be able to appoint their own auditor.