

# AUDIT AND RISK COMMITTEE

8 May 2012

## The Future of Local External Audit

### Report of the Strategic Director for Resources

STRATEGIC AIM:	All
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#### 1. PURPOSE OF THE REPORT

1.1 The Committee will be aware that following the announcement of its decision to abolish the Audit Commission in August 2010, the Government consulted on proposals for a new local public external audit framework. This report seeks to update the Committee on the response to the consultation, the current position and the arrangements for external audit over the next 5 years.

#### 2. RECOMMENDATIONS

2.1 That the Committee notes the contents of this report.

#### 3. REASONS FOR THE RECOMMENDATIONS

3.1 To ensure that the Committee is aware of the changes to the Council's external audit arrangements and the national developments.

#### 4. BACKGROUND

4.1 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 external audit framework.

4.2 The Government said that the 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 (such as the Council), giving them 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 part of a framework of accountability that provides assurance to Parliament about the public money allocated to Government departments which is in turn devolved to the local level.

4.3 The Government's response to the consultation sets out the key themes and views raised during the consultation and what is now proposed for the new arrangements for audit of principal public bodies.

- 4.4 The Government's 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.
- 4.5 The new contracts will not take effect until April 2017 at the earliest.

## 5. KEY ELEMENTS OF THE ARRANGEMENTS POST APRIL 2017

- 5.1 **Regulation** – there should be a consistent regulatory regime for audit, covering the private sector and local public bodies. The National Audit Office is considered best placed to produce the Code of Practice and supporting guidance for audit of local public bodies. The Financial Reporting Council will be the overall regulator, mirroring its role under the Companies Act 2006. It will be responsible for recognition and supervision of Recognised Supervisory Bodies (professional accounting bodies responsible for supervising the work of auditors) and for Recognised Qualifying Bodies (professional accounting bodies responsible for awarding audit qualifications).
- 5.2 **Appointment of Auditors** – the Full Council will appoint an external auditor from the register of local public auditors on the advice of an Independent Auditor Appointment Panel, and following an EU compliant competitive procurement process (if the relevant threshold is met). This process could be undertaken by the Council on its own or as a shared procurement with other councils. The auditor would usually be appointed for 5 years. This will be a major change for the Council as the Audit Commission currently appoints the auditor.
- 5.3 The Appointment Panel will have an independent chair and a majority of independent members. Any existing committee that meets the independence requirement and has the necessary skills could potentially be used. The Government intends to allow local public bodies to share appointment panels (and therefore independent members) to ease administrative burdens and reduce costs. The Council will be required to publish details of the auditor appointment, together with the Independent Audit Appointment Panel's advice. If the Council does not follow that advice, it will have to state why not.
- 5.4 **Rotation of Audit Firms and Audit Staff** – 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, the key audit staff will not be able to work with the Council for a further five years, although the audit firm itself could be reappointed following the five yearly competitive procurement process.
- 5.5 **Scope of external audit work** – the scope of local public audit will remain broadly similar. As now, auditors 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 Council 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 be set out in a code of audit practice. The duty for auditors to undertake Public Interest Reporting will be retained, as will their ability to charge for reasonable work. Local electors will retain the right to make formal objections to the accounts, but auditors will have greater discretion regarding whether to pursue an objection, to avoid time and cost being spent on vexatious or frivolous objections.

**5.6 Other duties of the Audit Commission** – following the Commission's closure, Government considers that for new grants to the Council, the grant paying body should agree certification arrangements with recipients and auditors. The Government proposes to continue the National Fraud Initiative and intends to rationalise the number of value for money studies.

## **6. DEVELOPING THE DETAILS AND THE LEGISLATION**

**6.1** Further discussions will be held 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. At the current time it appears that there are still many details to be resolved.

**6.2** A draft Bill for pre-legislative scrutiny is planned for spring 2012 which allows for examination and amendments to be made before formal introduction to Parliament eventually leading to a new Act.

## **7. AUDIT ARRANGEMENTS FOR THE NEXT 5 YEARS**

**7.1** The Council is currently audited by the Audit Commission's in house practice, as decided by the Audit Commission.

**7.2** The Commission has recently completed the process of outsourcing all Audit Commission work with outsourced contracts taking effect from 2012/13 for a five year period. This will allow councils and other public bodies time to plan for appointing their own auditors.

**7.3** Contracts have been awarded regionally, with the successful supplier for the East Midlands being KPMG LLP.

**7.4** Audit Commission staff will transfer to the firms that have been awarded the contracts on 31 October 2012. Most 2011/12 audits should be completed by then, but a few may not be either because there has been a problem with the accounts or because of an outstanding objection. The Commission will require the new auditor to complete any outstanding work for 2011/12 or prior years. The new auditor will be expected to place maximum reliance on the work of the current auditor. The Commission is aware of the disruption and additional work that can be caused by the change of auditor.

**7.5** Once the audits transfer to the firms the Commission will radically reduce in size. It will become a small residuary body responsible for overseeing the initial five year contracts and making changes to the individual audit appointments during the life of those contracts.

## **8. IMPLICATIONS FOR RUTLAND COUNTY COUNCIL**

**8.1** The Council's current external audit team will retain a watching brief from April 2012 until KPMG takes up their appointment on 1 September, whilst completing the audit of the 2011/12 accounts.

**8.2** In terms of delivery of audit services, we are not anticipating any major changes immediately after the new appointments. The Strategic Director for Resources is

attending an introductory meeting with KPMG on 10 May 2012 which should help us to gain a clearer picture on this.

**8.3** The main audit fee for 2012/13 has been confirmed and is considerably lower than we had anticipated. Further information will be provided as part of the Quarterly Financial Management reporting.

**8.4** We have planned well and are carefully monitoring our 2011/12 accounts closedown process to enable the Audit Commission to issue their opinion by the statutory deadline of 30 September, thereby ensuring a smooth transition to the new contract.

## **9. RISK MANAGEMENT**

<b>RISK</b>	<b>IMPACT</b>	<b>COMMENTS</b>
Time	Low	National timescales have been set out and the Council is working with the current audit team to ensure as smooth a transition as possible.
Viability	Low	There are no direct implications within this report
Finance	Low	Overall audit costs are expected to reduce as a result of the changes outlined in this report.
Profile	Low	There has been little public interest in the changes to the audit arrangements.
Equality and Diversity	Low	Equality Impact Assessment completed, there are no particular issues from this report.

### **Background Papers**

Government response to the future of local audit consultation  
January 2012.

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