

Consultation questions and proposed responses

1. Have we identified the correct design principles? If not what other principles should be considered? Do the proposals in this document meet these design principles?

Two options have been drafted below as possible responses to this question. Response 1 addresses only the narrow question raised. Response 2 takes a wider view of the role of local authority accounts in local accountability, and the opportunities to take a more fundamental approach. Members' views are sought on the approach they wish to take.

Response 1

The principles of localism and decentralisation, transparency, lower audit fees and high standards of auditing are reasonable design principles, but the consultation paper falls short of meeting them all.

It is a matter of concern that although the paper talks of the need to trust local bodies, that does not extend to the appointment of auditors by elected Members. The proposal for non-elected members on audit committees is in conflict with the principles of localism and the Council considers this a step too far.

If an approved list of audit firms can be established (possibly via the Office for Government Commerce) then the procurement of audit by individual councils will be quick, efficient and competitive (whether by individual councils or jointly) and the professional standards and codes governing the firms will ensure high standards of auditing, particularly as firms will not want to lose their place on the approved list.

Response 2

Local authority accounts are complex to read, expensive to produce and audit, and do not serve the stakeholders well. Indeed, it is no longer apparent who the stakeholders are, since the accounts are not generally read by Members or the public, whose needs are best met by summarised accounts and outturn reports.

The proposals represent a missed opportunity to take a holistic approach to local authority accounts and consider:

- *how local authority accounts should be reformed to:*
 - *provide simple, accessible, relevant and meaningful information to stakeholders*
 - *reduce the costs of production*
 - *reduce the costs of audit*
- *the approach to audit of the accounts*
- *the most appropriate type of organisation to undertake the audit – an audit firm or a reformed Audit Commission.*

Only when these issues have been addressed can the issue of design principles be properly considered.

Nothing in the consultation gives any indication that these issues have been thought through before issuing the consultation, or deciding that a reformed Audit Commission would not be the best vehicle for future local government audit.

Therefore, although the design principles themselves are reasonable, they exist in something of a vacuum and the accounts that councils will continue to publish will not meet local needs or the principles of transparency and low audit fees.

2. Do you agree that the audit probation trusts should fall within the Comptroller and Auditor General's regime?

Yes.

3. Do you think that the National Audit Office would be best placed to produce the Code of audit practice and the supporting guidance?

Yes. Although the NAO may have a conflict of interest in commenting on the DCLG proposals, and in having a role in their implementation.

4. Do you agree that we should replicate the system for approving and controlling statutory auditors under the Companies Act 2006 for statutory local public auditors?

This would appear to be a reasonable approach, but more information is required on how this would work in a public sector context. The private sector approach cannot be regarded as an unqualified success.

For example, the auditors approved and controlled under the Companies Act 2006 were content to sign the accounts of UK and US banks, insurance companies, etc etc when subsequent events would suggest that the auditors either did not understand the risks, or were unwilling to issue qualified opinions..

5. Who should be responsible for maintaining and reviewing the register of statutory local public auditors?

It would be reasonable for the Financial Reporting Council to maintain and review the register. But an OGC managed procurement process could then be undertaken to provide an approved list from which local authorities could draw, without needing to comply with the detailed requirement of EU procurement on an authority by authority basis.

6. How can we ensure that the right balance is struck between requiring audit firms eligible for statutory local public audit to have the right level of experience, while allowing new firms to enter the market?

New firms must be able to demonstrate their awareness of the requirements of public sector audit, including the skills and experience of staff, quality standards and review procedures etc before they can be considered.

If the OGC establishes basic quality thresholds for all firms seeking public audit contracts, whether they are new entrants to the market or not, then the new entrants would only be required to demonstrate these qualities once in order to get onto the approved list.

However, the Council believes that without the Audit Commission, and with a limited supply of experience staff, the market will generally tend to be dominated by the larger national firms with the demonstrable skills and experience, and this may lead to an upward pressure on fees.

7. What additional criteria are required to ensure that auditors have the necessary experience to be able to undertake a robust audit of a local public body, without restricting the market?

Firms would need to demonstrate an understanding of the specific accounting treatments required of the public sector in general and local authorities in particular, the main legislative constraints and requirements applying to local authorities and the governance regimes within which local authorities are required to operate.

8. What should constitute a public interest entity (ie a body for which audits are directly monitored by the overall regulator) for the purposes of local audit regulation? How should these be defined?

Local authorities have little experience of PIE's and the consultation gives no information on the implications of the approaches considered. It is not, therefore, possible to offer responses to questions 8, 9 and 10.

9. There is an argument that by their very nature all local public bodies could be categorised as 'public interest entities.' Does the overall regulator need to undertake any additional regulation or monitoring of these bodies? If so, should these bodies be categorised by the key services they perform, or by their income or expenditure? If the latter, what should the threshold be?

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10. What should the role of the regulator be in relation to any local bodies treated in a manner similar to public interest entities?

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11. Do you think the arrangements we set out are sufficiently flexible to allow councils to cooperate and jointly appoint auditors? If not, how would you make the appointment process more flexible, whilst ensuring independence?

The arrangements are sufficiently flexible to allow for voluntary joint procurement by a number of Councils working together.

However, the Council also understands that the DCLG have considered the idea of letting contracts in geographic bundles (for example all Kent District Councils). This would appear to conflict with the idea of local appointment, and any requirement to get a larger number of Councils working together may bog the process down.

The suggestion at paragraph 3.6 that the electorate can make an input into the appointment of the auditor is also not adequately developed in the consultation. It is not clear if the public are to be allowed to speak, at Council, on the appointment, or if the suggestion is that they participate in the work of the audit committee.

It is also not clear how many members of the public have, in the past, been frustrated in their ambitions to participate in the appointment of the auditors, and disappointing that no evidence is offered, but it is likely to be a very small number. Although the theory sounds plausible, this may have little application in practice.

12. Do you think we have identified the correct criteria to ensure the quality of independent members? If not, what criteria would you suggest?

No. The proposals ensure the independence of the independent members, but do not contain any measures that ensure the quality or skills of the independent members, other than that they must be acceptable to a majority of the council.

The Council believes that the proposal for a majority of the Audit Committee to be independent is unnecessary and takes the proposals too far. No evidence has been brought forward to demonstrate the effectiveness of local authority audit committees.

It may be a good idea to have an independent perspective on work of the Committee, but having a majority of independent members undermines the position of elected members and the principle of localism. The proportion of non-elected members should be a matter for the Council to decide.

13. How do we balance the requirements for independence with the need for skills and experience of independent members? Is it necessary for independent members to have financial expertise?

It is desirable that independent members have financial skills and this should be one of the criteria for their appointment. Indeed, this would be easier to achieve than it would for elected Members where it is not possible to ensure that there are non-executive, non-cabinet Members with relevant financial experience.

14. Do you think that sourcing suitable independent members will be difficult? Will remuneration be necessary and, if so, at what level?

Recruiting sufficient, suitably qualified, independent members who have had no recent roles within local authority and who have no close connections with current officers or Members, but who are interested in serving on a local authority audit committee is likely to be a challenge.

Remuneration will be a matter for the Council's Independent Remuneration Panels, and the levels are likely to be comparable to those set of independent members on Standards Committees.

15. Do you think that our proposals for audit committees provide the necessary safeguards to ensure the independence of the auditor appointment? If so, which of the options described in paragraph 3.9 seems most appropriate and proportionate? If not, how would you ensure independence while also ensuring a decentralised approach?

The Council recognises the potential benefit of one or more suitable qualified independent members of the audit committee. But the precise numbers, and the decision as to whether the Chairman should be independent are matters for the Council, not the DCLG.

The final appointment of the auditor will be a matter for full Council, which will consider the recommendations of the Audit Committee, together with the debate and contributions from other members and possibly the public. Therefore the proposals only safeguard the advice to Council, not the appointment of the auditor.

16. Which option do you consider would strike the best balance between a localist approach and a robust role for the audit committee in ensuring independence of the auditor?

The Council supports Option 1. There should only be one mandatory duty for the Audit Committee. It is quite likely that the Council will choose to add to the Committee's roles and, in practice, the Committee's operation will more closely resemble option 2. But that is a matter for the Council to determine.

17. Are these appropriate roles and responsibilities for the Audit Committee? To what extent should the role be specified in legislation?

It is appropriate that the roles are undertaken by a Committee, and that they are specified in legislation. However, the role of the Audit Committee should be narrowly prescribed, and the additional roles should be discharged as the authority sees fit. It is very likely that the majority of Councils will require the Audit Committee to undertake the roles, and that would be a sensible solution, but the principle of localism requires that this is a decision for the Council.

18. Should the process for the appointment of an auditor be set out in a statutory code of practice or guidance? If the latter, who should produce and maintain this?

Yes. The NAO should maintain it.

19. Is this a proportionate approach to public involvement in the selection and work of auditors?

The approach suggested is proportionate so long as there are reasonable safeguards to deal with repeated or vexatious complaints.

20. How can this process be adapted for bodies without elected members?

As a local authority the Council does not have experience in this area.

21. Which option do you consider provides a sufficient safeguard to ensure that local public bodies appoint an auditor? How would you ensure that the audited body fulfils its duty?

It is not clear what circumstances might give rise to this situation.

If, for example, Councils in more remote areas of the country find that there are no local firms with the necessary skills and expertise available to undertake the work, or no regional/national firms able to undertake the work at a cost that is no more than the former cost of the Audit Commission, the Council may face a significant cost increase in order to comply with the requirement.

Option 1 is the most reasonable response, but presumably the Council will have tried to comply with its statutory requirement, and therefore option 2 would seem to be the inevitable consequence.

22. Should local public bodies be under a duty to inform a body when they have appointed an auditor, or only if they have failed to appoint an auditor by the required date?

It is reasonable that the appointment is notified to the Secretary of State or some other body, in order that the Secretary of State can be certain that all authorities have appointed auditors.

23. If notification of auditor appointment is required, which body should be notified of the auditor appointment/failure to appoint an auditor?

The DCLG.

24. Should any firm's term of appointment be limited to a maximum of two consecutive five-year periods?

Yes. A maximum of ten years is appropriate.

25. Do the ethical standards provide sufficient safeguards for the rotation of the engagement lead and the audit team for local public bodies? If not, what additional safeguards are required?

Yes. The safeguards are sufficient.

26. Do the proposals regarding the reappointment of an audit firm strike the right balance between allowing the auditor and audited body to build a relationship based on trust whilst ensuring the correct degree of independence?

Yes.

27. Do you think this proposed process provides sufficient safeguard to ensure that auditors are not removed, or resign, without serious consideration, and to maintain independence and audit quality? If not, what additional safeguards should be in place?

The safeguards are sufficient. However, the auditor is an individual, not a firm, and that person may resign for many reasons outside of those given in the consultation. Many of them may be personal, such as a change of employer, changing personal circumstances etc.

It is assumed that under these circumstances the audit firm would propose the appointment of a new auditor from their firm, and under these circumstances this would be a relatively smooth process, providing that the individual is acceptable to the local authority.

28. Do you think the new framework should put in place similar provision as that in place in the Companies sector, to prevent auditors from seeking to limit their liability in an unreasonable way?

A framework is required to prevent auditors limiting their liability to an unreasonable extent.

Consideration also needs to be given to the level of materiality employed by the Audit Commission and that which is likely to be employed by audit firms under the new arrangements. Financial/political materiality at a local authority may be at a lower level than it is in the commercial sector.

29. Which option would provide the best balance between costs for local public bodies, a robust assessment of value for money for the local taxpayer and provides sufficient assurance and transparency to the electorate? Are there other options?

There is a danger that, by requiring auditors to form conclusions on a Council's arrangements, an element of the old Use of Resources regime may be retained and this could become too subjective.

Publication of clear, verifiable, non-subjective high level vfm data such as net budget requirement per resident, council tax levels etc, compared to similar authorities within the same "family group" would be a reasonable solution.

The Council considers option 2 to provide the best compromise.

30. Do you think local public bodies should be required to set out their performance and plans in an annual report? If so, why?

It is a matter for elected Members to decide how to explain their authority's plans and performance to the electorate, whether by annual report or other means.

31. Would an annual report be a useful basis for reporting on financial resilience, regularity and propriety, as well as value for money, provided by local public bodies?

It would be reasonable to require authorities to report on financial resilience, regularity and propriety, although it should be possible to do this without also requiring an annual report. For example, a report to the Audit Committee on these matters would be a public report.

32. Should the assurance provided by the auditor on the annual report be 'limited' or 'reasonable'?

It is not accepted that an annual report should be mandatory.

33. What guidance would be required for local public bodies to produce an annual report? Who should produce and maintain the guidance?

It is not accepted that an annual report should be mandatory.

34. Do these safeguards also allow the auditor to carry out a public interest report without his independence or the quality of the public interest report being compromised?

Yes, the ability for auditors to report in the public interest should be retained. Given the proposed safeguards, the Council does not feel the auditor's independence will be compromised.

35. Do you agree that auditors appointed to a local public body should also be able to provide additional audit-related or other services to that body?

Yes, but this should always be reported to the Audit Committee before the work is awarded, and Councils should follow their procurement arrangements and standing orders so other firms can compete for the work.

There should be a cap on the value of such work as a proportion of the value of the audit fees, and also as a proportion of the audit firm's fee income, so that firms are not compromised in their ability/readiness to provide a qualified opinion if circumstances warrant it.

36. Have we identified the correct balance between safeguarding auditor independence and increasing competition? If not, what safeguards do you think would be appropriate?

Yes.

37. Do you agree that it would be sensible for the auditor and the audit committee of the local public body to be designated prescribed persons under the Public Interest Disclosure Act? If not, who do you think would be best placed to undertake this role?

Yes, both the auditor and Audit Committee should be designated 'prescribed persons'.

38. Do you agree that we should modernise the right to object to the accounts? If not, why?

Yes, modernising the right to object to the accounts makes sense. The public have the FOI Act, ombudsman and other routes to seek information or redress.

39. Is the process set out above the most effective way for modernising the procedures for objections to accounts? If not, what system would you introduce?

Yes, except for the FOI proposals.

40. Do you think it is sensible for auditors to be brought within the remit of the Freedom of Information Act to the extent of their functions as public office holders? If not, why?

The Council has concerns that if the auditors are brought within the scope of the FOI Act, then vexatious or frivolous requests could significantly increase the costs to the Council, whilst being outside the Council's control. The volume and cost of FOI work is already a significant concern, and disproportionate to the benefit. It would be a retrograde step to increase the volume and costs.

41. What will be the impact on (i) the auditor/audited body relationship, and (ii) audit fees by bringing auditors within the remit of the Freedom of Information Act (to the extent of their functions as public office holders only)?

For the reasons set out above, the concern is that this will add to the costs of the audit, but will add very little value to the public.

The following questions relate, primarily, to town and parish councils and due to the timescales concerned it will not be possible to seek their views on this section.

42. Which option provides the most proportionate approach for smaller bodies? What could happen to the fees for smaller bodies under our proposals?

Neither approach is satisfactory. The Council believes that the creation of an audit committee is excessive for small bodies, except for those in the £250k - £6.5m range where such an arrangement would be proportionate.

The appointment of an independent examiner should be the role of the next tier above. So it should fall to District or Unitary Councils who will be close to the small bodies, and will have to deal with proportionately smaller numbers.

Fees are likely to increase from their current modest levels.

43. Do you think the county or unitary authority should have the role of commissioner for the independent examiners for smaller bodies in their areas? Should this be the section 151 officer, or the full council having regard to advice provided by the audit committee? What additional costs could this mean for county or unitary authorities?

No. For the reasons set out above, the IE should be appointed by the District or Unitary Council. This should be on the basis of recommendations by the S151 Officer to the District or Unitary Councils Audit Committee who could either be empowered to confirm or reject the proposed appointments, or else required to make their recommendations to full Council for approval.

44. What guidance would be required to enable county/unitary authorities to:

- (a) Appoint independent examiners for the smaller bodies in their areas?
- (b) Outline the annual return requirements for independent examiners?

Who should produce and maintain this guidance?

The guidance and advice should be produced by the NAO.

45. Would option 2 ensure that smaller bodies appoint an external examiner, whilst maintaining independence in the appointment?

Yes, but it would be a disproportionate burden on bodies below £250k.

46. Are there other options given the need to ensure independence in the appointment process? How would this work where the smaller body, e.g. a port health authority, straddles more than one county/unitary authority?

The Council has no other options to propose.

Are there many small port health authorities that straddle more than one county/unitary? If so, make the authority within which most of the port health area rests, the responsible body.

47. Is the four-level approach for the scope of the examination too complex? If so, how would you simplify it? Should the threshold for smaller bodies be not more than £6.5m or £500,000? Are there other ways of dealing with small bodies, eg a narrower scope of audit?

Yes, it is too complex. The consultation identifies a population of 9,900 small bodies. If these are mainly Town and Parish Councils, then relatively few of these fall within London Boroughs and Metropolitan authorities, and Counties and Unitary authorities could be faced with appointing IE's to 200+ small bodies each. It would be surprising if they had any detailed knowledge of the small bodies concerned.

48. Does this provide a proportionate, but appropriate method for addressing issues that give cause for concern in the independent examination of smaller bodies? How would this work where the county council is not the precepting authority?

This is confusing. County Councils do not precept on Town and Parish Councils, and there will be very few, if any, District Councils below the £6.5m threshold.

49. Is the process set out above the most appropriate way to deal with issues raised in relation to accounts for smaller bodies? If not, what system would you propose?

No. The role should rest with the District Council, not the County.

50. Does this provide a proportionate but appropriate system of regulation for smaller bodies? If not, how should the audit for this market be regulated?

No. The role should rest with the District Council, not the County.