EXPLANATORY MEMORANDUM TO

THE LOCAL AUDIT (AUDITOR PANEL INDEPENDENCE) REGULATIONS 2014

2014 No. [XXXX]

1. This explanatory memorandum has been prepared by the Department for Communities and Local Government and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

The Local Audit and Accountability Act 2014 ("the Act") provides that local public bodies will need to appoint their own auditors. Local public bodies must also appoint auditor panels, with a majority of independent members, to advise on the selection and appointment of an auditor. This instrument amends the definition of an independent member as set out in the Act.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 The memorandum by the Department for Communities and Local Government to the Delegated Powers and Regulatory Reform Committee explained that the power under which these regulations are made is necessary to enable provisions around independence to be reviewed and modified quickly to ensure that they are working correctly and strike the right balance. Local government contains an extremely complex set of interrelations and personal interests, and these regulations contain independence definitions which had not been fully developed in time to be included in the draft Bill when the Bill was published for public consultation from 6 July to 31 August 2012. It was important to separately consult on these provisions too, to ensure that they were considered workable and proportionate by the relevant sectors. Though they did not arise from a specific review, these provisions are of the scale of amendment we would expect to emerge from any such review, and have undergone the same level of consideration in their development.

3.2 The regulations have already received a greater degree of parliamentary scrutiny than would normally have been afforded to a statutory instrument before it has been laid: the regulations were shared in draft with the Public Bill Committee (7 November 2013) considering the Local Audit and Accountability Bill, setting out the further disqualifying interests which would render any person holding as not be able to count as an 'independent' member of an auditor panel. The Minister drew the Committee's attention to these draft regulations in debate on the Bill, and made a commitment to publicly consult on them. The powers in the Bill for these regulations to be made were passed without amendment. Following subsequent public consultation on the regulations from 25 November to 20 December 2013 minor changes were made to the regulations, chiefly to include descriptions of functional bodies of

the Greater London Authority, such as the Mayor's Office for Policing and Crime.

4. Legislative Context

The Act makes new provision for the audit of local public bodies ("relevant authorities") once the Audit Commission for Local Authorities and the National Health Service in England and Wales is abolished in 2015. Part 3 of the Act is concerned with the appointment, resignation and removal of local auditors – as defined in section 4 (1) (b) of the Act - to relevant authorities listed in Schedule 2 of the Act. Section 7 provides that a local auditor must be appointed by a relevant authority to audit its accounts for a financial year. Sections 9 and 10 provide that a relevant authority must appoint an auditor panel to advise the authority on appointment of its auditor. Auditor panels, for relevant authorities that are not health service bodies, must have an independent majority in their membership and have an independent chair.

5. Territorial Extent and Application

This instrument applies to England and Wales.

6. European Convention on Human Rights

The Minister for Local Government, Brandon Lewis, has made the following statement regarding Human Rights:

In my view the provisions of the Local Audit (Auditor Panel Independence) Regulations 2014 are compatible with the Convention rights.

7. Policy background

7.1 Auditor panels provide advice to a relevant authority that is not a health service body on the appointment and removal of the authority's local auditor, and on maintaining the independent relationship between the authority and the auditor. Health service bodies subject to the audit requirements of the Act have statutory audit committees, who will advise their governing boards on audit matters.

7.2 The majority of members of an auditor panel, and the chair of the auditor panel, must be independent of the relevant authority, to provide the authority with a genuinely independent perspective on matters related to the appointment of and ongoing relationship with its auditor.

7.3 Paragraph 2 of Schedule 4 to the Act, applying only to non-health service bodies, provides that for the purposes of the auditor panel a person is not independent if they are, or have been within the last five years, a member or officer of the authority, or an officer or employee of an entity connected with the authority. The person is also not independent if they are a relative or

close friend of a current member or officer of the authority or an officer or employee of a connected entity.

7.4 These regulations add to the existing definition of persons who are not independent:

- persons who have commercial links with the relevant authority to be audited; and persons who have links with a prospective or appointed audit firm. This is to avoid any conflict of interest in the deliberations of auditor panellists.

- persons who are, or have been in the last five years, members of an entity connected with the authority to be audited, where the connected entity is also a relevant authority under section 2 of the Act (for example, an Integrated Transport Authority is an entity connected with a Passenger Transport Executive). This is because the connected entity will also have relevance to the accounts of the authorities with which they are connected as the connected entity's accounts are consolidated into them, and as a connected entity which is a relevant authority may have 'members', it is necessary to exclude them as well as officers and employees.

- for the Greater London Authority, persons who are, or have been in the last five years members or officers of a functional body of the Greater London Authority (for example, the London Development Agency, or the London Fire and Emergency Planning Authority). Similarly, for a functional body of the Greater London Authority, persons who are, or have been in the last five years members or officers of the Greater London Authority. This is because these functional bodies have a close relationship with the Greater London Authority.

8. Consultation outcome

8.1 Public consultation, lasting four weeks, from 25th November to 20th December 2013, was undertaken on a draft of these regulations. The consultation paper can be found here:
http://localaudit.readandcomment.com/wp-content/uploads/2013/11/Future_of_Local_Audit_-_Consultation_on_secondary_legislation_.pdf

A summary of consultation response can be found here:
https://www.gov.uk/government/consultations/future-of-local-audit-consultation-on-secondary-legislation

8.2 One respondent argued that 'backbench' councillors should be considered independent; however the Government considers that all members of an authority have responsibility for appointing the auditor therefore they cannot be considered independent. Another respondent recommended a shorter, two year expiry for the period of non-independence due to association with the

bodies specified in the draft regulations; however the Government considers that five years is an appropriate period for the effect of those associations to have expired. There was an appetite for guidance on the application of the independence definitions, which we will consider with the sector.

9. Guidance

The Government will develop guidance in partnership with the sector on the new auditor appointment arrangements, which may include advice on how the definitions of independence should be applied in relevant authorities' appointments to auditor panels.

10. Impact

An Impact Assessment has not been prepared for this instrument, as it will have no impact on charities or the voluntary sector. An individual with commercial links to the authority to be audited will be ineligible to serve as an independent member of the auditor panel, however this will not have an impact on business.

11. Regulating small business

This legislation does not apply directly to small business. As noted above, an individual with commercial links to the authority to be audited will be ineligible to serve on an independent auditor panel, however this will not have an impact on business.

12. Monitoring & review

12.1 As part of the Government's commitment to review the implementation of new legislation within three to five years of receiving Royal Assent, Government has set out some general principles towards developing a possible approach to such a review and assessing the impacts/outcomes associated with the Government's reforms to local audit. An overriding objective for the final approach would be to ensure that any proposed measurement is both proportionate and cost effective.

12.2 The aims and success criteria of the local audit reforms are to:

- Deliver greater localism, decentralisation and transparency;
- Maintain competitive audit fees; and
- Uphold high standards of auditing.

The post implementation review will provide Government, Parliament and the public with the evidence to demonstrate that the local audit framework is achieving its anticipated outcomes

13. Contact

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