

To: Shareholder and Joint Venture Group
Date: 27 April 2023
Report of: Head of Financial Services
Title of Report: Oxford Direct Services Ltd and Oxford Direct Services Trading Ltd External Auditor Appointment 2022/23

Summary and recommendations	
Purpose of report:	To propose the appointment of Mazars LLP as external auditor for the 2022/23 financial statements.
Recommendation: that the Shareholder and Joint Venture Group resolves to:	
	<ol style="list-style-type: none"> 1. Note the current position in respect of 2021/22, the current state of the audit market, and the increase in audit requirements. 2. Approve the appointment of Mazars LLP as external auditor for the 2022/23 financial statements.

Appendices	
None	

Background

1. The contract for the external audit of the Council's wholly owned group companies plus Barton Oxford LLP is with Mazars LLP up to the conclusion of the 2021/22 audit. The appointment of company auditors is a reserved matter for the shareholder and this report is being brought in order to gain approval from the shareholder for the appointment of Mazars LLP for a further year to enable the delivery of the 2022/23 financial year audit. The intention would be to tender the contract for the audit of the 2023/24 accounts. The contract is arranged by the Council as shareholder of Oxford City Housing Limited, Oxford Direct Services Limited (ODSL), and Oxford Direct Services Trading Limited (ODSTL) and 50% partner in Barton Oxford LLP, however the services are to be provided to the relevant legal entity and the fees are payable by them.
2. The current contract is let to a single auditor for them to provide the audit for all of these companies due to both the complex inter-company relationships which are best dealt with on a consistent basis by one auditor and also to enable Council officers to have one point of contact and one process through which to manage the audit. These requirements continue to be important and as such a report is

being sent to the shareholder meetings of each of the entities to gain the same approval.

The Position in Respect of the 2021/22 Audit

3. The audit is ongoing for ODS 2021/22 due mainly to issues experienced with QL and is unlikely to be concluded until June 2023 at the earliest, at which point the next year's financial year closedown process will be underway. Audit rely on the completion of the prior year accounts for the brought forward figures and the 2021/22 carry forwards will not be available. This therefore means that no reliance can be placed on the balance sheet until the 2021/22 accounts are completed. The issues around systems and the accuracy of financial information within ODSL during 2021/22 and the closedown relating to that year means that any new auditor would not be able to easily place reliance on processes and systems of internal control.

Audit Market Capacity

4. There is a lack of capacity in the audit market for large scale audits such as Councils and Council group companies and auditors are able to choose work that fits their capacity. Increased scrutiny from the Financial Reporting Council (FRC) on the work of audit firms has led to a number of very significant fines of audit firms. Auditors are therefore undertaking more intensive work to cover off the risks. The higher the risk, the less likely an auditor would be to undertake the work. ODSL and ODSTL are currently high risk due to the uncertainty of the 2021/22 financial accounts, the breakdown in financial processes which led to this position and the time it is taking for rectification of the situation to be undertaken.
5. Even if an auditor decided to bid for this work it would invariably be at a very substantial premium. During discussion with the existing auditor, Mazars, they have indicated that if the work were put out to tender then they would not bid for the work because of the risk involved; they have only agreed that they would be willing to undertake the 2022/23 audits after a degree of persuasion.

Auditing Standards

6. Last year saw significant revisions to auditing standards, addressing the audit of accounting estimates and going concern with further revisions to major auditing standards on risk assessment and fraud (revisions to existing International Standards on Auditing (ISAs) (ISA (UK) 315 and ISA (UK) 240)) in the following year. The reason for these changes has been the sudden and high profile failures of major companies and the subsequent scrutiny of the audits of those organisations. As a result, there have been several reviews of the audit market with the aim of improving audit quality. In addition, auditing standards have been updated to keep pace with technology and the way businesses operate today in a digital world. These changes impact on the audits for private and public companies alike, including the Council's group companies. (They also impact on the Council itself since the council operates under the International Financial Reporting Standards and the Council auditors have to comply with ISAs.)
7. ISA (UK) 315, the standard on identifying and assessing the risks of material misstatements has seen a significant expansion. This standard is all about

understanding the entity, its environment, and the applicable financial reporting framework, in order to adequately identify the risks of material misstatement. This standard has specific relevance to ODSL and ODSTL due to the issues that arose in 2021/22 that inevitably then pose an ongoing risk for the 2022/23 audits. Changes to ISA (UK) 315 will likely result in more discussions and requests for information and documentation during the audit planning stage. This will mean the auditor looking more closely at policies, procedures and internal controls than they have done in previous years, and they will focus more heavily on the general IT environment to gather a greater understanding of the potential risks arising from the technology used within the business. The auditor will need to gain a more thorough understanding of the structure of the IT hardware and software and the various layers of the IT system such as security and access rights.

8. Five inherent risk factors have also been introduced to risk assessment: complexity, subjectivity, change, uncertainty and susceptibility to misstatement due to management bias or other fraud risk factors, insofar as they affect inherent risk. New requirements have been added with respect to the entity's control environment, including more evidence/information on controls relevant to the audit and on the design and implementation testing required to be undertaken in all cases.
9. These changes have a direct impact on both the willingness of audit firms to undertake work (especially when combined with increased FCA scrutiny) and the price that needs to be paid for an audit. The latter is impacted both through the increased workload and also the increased risk of undertaking an audit.

Conclusion

10. For all of the reasons included within this report it is considered that appointing Mazars LLP for another year is the best approach for the Council and its group.

Financial implications

11. After discussions with the auditor, the following fees have been proposed for the audit of the 2022/23 financial accounts:

- ODS entities – £70,000 (excluding VAT)

The base fee for 2021/22 was £38,000 with a supplement for the issues around QL that were known at the time of the start of the audit of £12,000 for a total of £50,000. It is likely that the final fees for 2021/22 accounts will be higher than the original estimate due to the additional issues that became apparent after the audit had commenced. The fee increase for 2022/23 is in line with the general additional costs of audit in the market and the increased audit risks.

Legal issues

12. Section 475 of the Companies Act 2006 requires that a company's annual accounts for a financial year must be audited unless the company due to being a small company, a subsidiary of another company or dormant.

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Background Papers:

None
