

Date: 8 October 2015

Item: Effectiveness Review of the External Auditors

This paper will be considered in public

1 Summary

- 1.1 To report to the Committee on external auditor effectiveness.
- 1.2 A more detailed paper is also included on the Part 2 agenda which contains exempt supplemental information, by virtue of paragraph 3 of Schedule 12A of the Local Government Act as it contains information relating to the financial and commercial affairs of TfL.

2 Recommendation

- 2.1 **The Committee is asked to note the paper and the related supplemental information on Part 2 of the agenda.**

3 Background

- 3.1 The Terms of Reference of the Audit and Assurance Committee as set out in the document 'Subordinate Bodies of TfL' require the Committee to review formally the performance of the external auditors at least annually. This review covers the performance of the external auditors of all parts of the TfL Group.
- 3.2 The Terms of Reference do not specify the means by which auditor performance is to be assessed. Other guidance is available, for example in the Institute of Chartered Accountants in England and Wales publication "Guidance for audit committees – Evaluating your auditors". This guidance was published in 2003 and is based on the proposals published by the Smith Committee on Audit Committees and the provisions of the Combined Code on Corporate Governance, but is still relevant. Although this relates to listed companies, the principles are also relevant to entities such as TfL.
- 3.3 The Smith Guidance identifies four criteria in assessing external auditors:
 - (a) qualification;
 - (b) expertise and resources;
 - (c) effectiveness; and
 - (d) independence.
- 3.4 KPMG is a "registered auditor" and required to comply with the Audit Regulations which cover such matters as independence and integrity,

maintaining competence, compliance with technical standards and monitoring compliance with the Regulations. These requirements ensure that the criterion regarding qualification is addressed.

- 3.5 Independence of the external auditors is dealt with through separate reports to the Audit and Assurance Committee on fees for non-audit services and on independence and objectivity – both reported twice a year. The external auditors are appointed by the Audit Commission under a statutory process, and this provides additional safeguards in terms of independence.
- 3.6 This paper deals with assessing the remaining two criteria in the Smith Guidance, namely the effectiveness, and also the expertise and resources of the external auditors.

4 Methodology for Assessing External Auditor Effectiveness and Expertise

- 4.1 A questionnaire was devised and distributed to key finance staff and senior management to obtain their views on the conduct and effectiveness of the external audit, including the expertise and resources of the external auditors.
- 4.2 Responses were sought under four main headings:
 - (a) audit planning and preparation;
 - (b) field work;
 - (c) closing meetings and sign-off; and
 - (d) general.

The questionnaire provided respondents with an opportunity to comment on the specific questions and also respond on more general free-form topics.

- 4.3 Questionnaires were sent out to all parts of the business and all were completed and returned. Some parts of the business consolidated their responses into one return for that business unit. The Finance Shared Services Centre (FSC) and the Group Accounting team were also covered.
- 4.4 Respondents were asked to score responses on a 1 to 3 scale, with 3 being the top score. Average scores were calculated for each part of the questionnaire.

5 Conclusions on External Auditor Effectiveness and Expertise

- 5.1 TfL finance staff were pleased with KPMG's performance as external auditors in this the final year before the hand-over to Ernst & Young (EY). The audit was well managed, and audit work carried out efficiently within a tight timetable. The scores on average were little changed from the prior year and ranged from 2.8-3.0 (2013/14: 2.8-3.0).
- 5.2 The involvement of the KPMG partner (Robert Brent) is always important so that any issues that arise are resolved as quickly as possible. Robert as lead partner was very engaged throughout the audit and the regular progress

updates were extremely helpful in ensuring the timetable was met.

- 5.3 KPMG acted on the prior year's debrief points in all key areas. TfL's incoming auditors, EY, have been made aware of the key observations and these will be taken into account in their planning for the 2015/16 audit:
- 5.4 The questionnaire asked if there were any members of the audit team that TfL staff would single out for their strong personal contribution. Five names were mentioned and these have been fed back to the partners.

List of appendices to this report:

Exempt supplemental information is included in a paper on Part 2 of the agenda.

List of Background Papers:

None

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