

Date: 11 October 2016

Item: Effectiveness Review of the External Auditors

This paper will be considered in public

1 Summary

- 1.1 To report to the Audit and Assurance 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 this report and the 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 "TfL Committees and Panels" 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 where EY are auditor.
- 3.2 The Terms of Reference do not specify the means by which auditor performance is to be assessed. Other guidance is available, one of the more recent of which is the Financial Reporting Council 2016 publication "Guidance on Audit Committees". This is an update of guidance first published in 2003 and subsequently updated in 2008. It is based on the UK Corporate Governance Code, and although this relates to listed companies, the principles are also relevant to entities such as TfL.
- 3.3 The Guidance identifies four criteria in assessing external auditors:
 - (a) qualification
 - (b) expertise and resources
 - (c) effectiveness
 - (d) independence
- 3.4 EY have taken over from KPMG as auditors of all entities within the TfL group from year ending 31 March 2016 (with the exception of London Transport Museum which was audited by KPMG). Both EY and KPMG are "registered

auditors” 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. It should also be noted that the external auditors are appointed by Public Sector Audit Appointments Limited, the successor body to 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 Guidance, namely the effectiveness, and also the expertise and resources, of EY as external auditors. The Museum is not material to the group as a whole and the effectiveness of the Museum audit was discussed at their own Audit Committee.

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 most were completed and returned. Some parts of the business consolidated their responses into one return for that business unit. The Finance Shared Services Centre 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.

4 Conclusions on External Auditor Effectiveness and Expertise

- 5.1 TfL finance staff were generally satisfied with EY performance as external auditors in this, the first year after the hand-over from KPMG. Given that this was a hand over year the scores on average were lower than the prior year

and ranged from 2.1-3.0 (2014/15: 2.8-3.0).

- 5.2 In some areas of the audit, the work undertaken by EY was more in-depth than in prior years and the overall impression was of a thorough audit.
- 5.3 It was unsurprising that there were some issues arising from lack of knowledge or experience of TfL, given that this was the first audit by EY. There were also areas where it is believed that the efficiency of the audit could be improved. TfL finance staff will work closely with EY in the detailed planning for next year and it is expected that the average scores will improve for the 2016/17 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. Three 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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