GMCA Audit Committee

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Appointment of External Auditors

Report Of
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PURPOSE OF REPORT
This report summarises the changes to the arrangements for appointing External Auditors.

The Local Audit and Accountability Act 2014 (the Act) at Section 7 states that a “relevant authority must appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding financial year.” Current auditor contracts have been extended for 12 months, therefore for the GMCA the appointment of an auditor must be completed by 31 December 2017 for the audit year 2018/19.

RECOMMENDATION
Audit Committee consider the proposal for the establishment of a local joint procurement arrangement with neighbouring authorities for the provision of external audit services from 2017/18 and approve the GMCA Treasurer to progress actions necessary to develop the procurement process.

PRIORITY
This report is produced to support Audit Committee oversight of risk and assurance across GMCA and AGMA.
RISKS/IMPLICATIONS

Financial: Cost of Internal Audit and Risk Services within GMCA budget.

Staffing: No impact

Policy: No impact

Equal Opportunities – Has a Diversity Impact Assessment been conducted? No

TRACKING/PROCESS

Does this report relate to a Key Decision, as set out in the GMCA Constitution or in the process agreed by the AGMA Executive Board? No

EXEMPTION FROM CALL IN

Are there any aspects in this report which means it should be considered to be exempt from call in by the AGMA Scrutiny Pool on the grounds of urgency? No

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<th>AGMA Commission</th>
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1 Introduction

1.1 The Local Audit and Accountability Act 2014 brought the Audit Commission to a close, and established transitional arrangements for the appointment of external auditors and the setting of audit fees for all local government and NHS bodies in England. On 5 October 2015 the Secretary of State for Communities and Local Government determined that the transitional arrangements for local government bodies would be extended by one year to also include the audit of the accounts for 2017/18.

1.2 The current external auditor for the GMCA and TfGM is Grant Thornton, this appointment having been made under a contract which was originally let by the Audit Commission.

1.3 Following closure of the Audit Commission the contract is currently managed by Public Sector Audit Appointments Limited (PSAAL), the transitional body set up by the LGA with delegated authority from the Secretary of State for Communities and Local Government. When the current transitional arrangements come to an end on 31 March 2018 the GMCA will be able to move to a local appointment of its auditor. There are a number of routes by which this can be achieved, each with varying risks and opportunities.

1.4 Current audit fees are based on discounted rates offered by the firms in return for a substantial market share. When the contracts were last negotiated nationally by the Audit Commission they covered NHS and local government bodies and offered maximum economies of scale.

1.5 The scope of the audit will still be specified nationally by the National Audit Office (NAO) which is responsible for writing the Code of Audit Practice. All firms appointed to carry out the GMCA audit must follow these requirements.

1.6 Not all accounting firms will be eligible to compete for the work, they will need to demonstrate that they have the required skills and experience and be registered with a Registered Supervising Body approved by the Financial Reporting Council. The registration process is in progress and so the number of eligible and interested firms is not known at this stage but it is reasonable to expect that the list may include the top 10 or 12 firms in the country, including the current GMCA external auditor. It is unlikely that small local independent firms will meet the required eligibility criteria.

2 Options for Local Appointment of External Auditors

2.1 There are three broad options open to the GMCA under the Act and new appointments for auditors need to be made by December 2017 regardless of which option is chosen.

Option 1: Make a stand-alone appointment

2.2 To make a stand-alone appointment, the GMCA will need to establish an independent Auditor Panel. The Panel must be made up of a majority of independent members as defined by the Act. Independent members for this purpose are independent appointees – for the GMCA this excludes all current and former elected members (or officers) and their close families and friends. This means that elected members will not have a majority input into the process for the assessment and appointment of the firm of accountants to provide the GMCA external audit. A newly established and independent Auditor Panel would be responsible for selecting the auditor..
2.3 This option allows the GMCA to take maximum advantage of the new local appointment regime and have local input to the decision; however, recruitment and servicing of the Auditor Panel, running the bidding exercise and negotiating the contract is estimated by the LGA to cost in the order of £15,000 plus on going expenses and allowances. In addition the GMCA would not benefit from reduced fees that may be available through joint or national procurement contracts.

**Option 2: Local joint procurement arrangements**

2.4 The Act enables the GMCA to join with other authorities to establish a joint independent Auditor Panel which would need to be constituted and made up of a majority, or of wholly independent members. Further advice will be required on the exact constitution of such a Panel having regard to the obligations of each body under the Act and as such the GMCA will need to liaise with other authorities to assess the appetite for this arrangement.

2.5 The Joint procurement exercise could involve the GMCA and the functions due to be transferred into the GMCA or the Mayor's Office from 2017. This would include: TfGM, the GM Waste Disposal Authority, GM Fire and Rescue Service, the GM Police and Crime Commissioner’s Office, GM Police and New Economy. There are benefits from appointing the same auditor for this group of bodies, not just in terms of economies of scale but also in enabling the external auditor to obtain a fuller understanding of the audit requirements across these GM level functions.

2.6 In addition to GM level local authority bodies, the proposal could also include GM districts. At present, eight of the ten GM Councils are audited by Grant Thornton and two are audited by KPMG. Given the level of collaboration, joint working and similar core functions across the bodies, there are likely to be benefits from including the ten districts in this procurement. In addition to this, an option could be extended to include health bodies at a later date, although it should be noted that they are currently working to a different timetable for appointments.

2.7 Other advantages of this approach are that the costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities and therefore greater opportunity for negotiating economies of scale by being able to offer a larger combined contract value to the firms.

2.8 This option is not without risk. The decision making body will be further removed from local input. It is unlikely that elected members from each district or each GM Body would be represented on an independent auditor panel. Individual Audit Committees would still discharge their functions at district and GM levels; for example considering their own auditor reports; the statement and accounts; and governance arrangements.

2.9 There is a risk that accountancy and audit firms may decline to bid for a package of GM external audit work due to independence issues. A successful firm would be unable to undertake substantial values of advisory work, as to do so would be in contravention of professional standards, independence safeguards and terms of appointment established by the PSAA. Initial soft market testing has been undertaken and whilst some of the top tier firms have confirmed that this issue would likely preclude them from bidding, other firms have expressed interest in this procurement approach.
Option 3: Opt-in to a sector led body

2.10 In response to the consultation on the new arrangement the LGA successfully lobbied for Councils to be able to ‘opt-in’ to a Sector Led Body (SLB) appointed by the Secretary of State under the Act. This body had been confirmed as Public Sector Audit Appointments Limited (PSAAL). PSAAL will have the ability to negotiate contracts with the firms nationally, maximising the opportunities for the most economic and efficient approach to procurement of external audit on behalf of the whole sector.

2.11 Under this approach, the costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities and by offering large contract values the firms would be able to offer better rates and lower fees than are likely to result from local negotiation. Any conflicts at individual authorities would be managed by PSAAL who would have a number of contracted firms to call upon.

2.12 The appointment process would not be ceded to locally appointed independent members but by a separate body set up to act in the collective interests of the ‘opt-in’ authorities.

2.13 Under this option, the GMCA Members and individual elected members across GM will have less opportunity for direct involvement in the appointment process other than through the LGA and/or stakeholder representative groups. This option could result in the GMCA, TfGM, GMP and the Districts all having different external auditors.

2.14 The GMCA Treasurer asked the LGA to clarify whether the sector led body approach would allow a cross-GM appointment given the developments around devolution, the extension of the role of the elected Mayor / Combined Authority and the general increased collaborative working across GMCA and the ten districts. The LGA were unable to commit to this as an option that GM could pursue.

3 Auditor Panel

3.1 Unless opting into the Sector led body approach (option 3), there will be a requirement to establish an independent Auditor Panel, either specifically for the GMCA or in collaboration with partners. The Auditor Panel role is different to that of the Audit Committee. Its functions are to advise the Authority on:

- selection and appointment of the auditor;
- resignation or proposals to remove the auditor;
- adoption of a policy on non audit services;
- maintenance of independent relationship with the auditor; and
- any proposals to enter into limited liability agreements

3.2 There is no specific reference in the Act of the Auditor Panel for carrying out a contract oversight role but guidance from CIPFA does indicate this is a possible addition function that might be helpful.
3.3 It is anticipated that the Panel will benefit from support specifically from the Head of Paid Service, Treasurer / Section 151 Officer, Head of Internal Audit and Head of Procurement. It also acknowledged that there should be a relationship between the Panel and the Audit Committee, who will receive updates and assurances arising from the work of the external auditor; and are also well placed to comment on the quality and performance of services provided through the contract. The Act does allow for the Audit Committee to discharge the duties of the Auditor Panel but only if it meets the criteria set out below and that its role when acting as the Auditor Panel is clearly distinct from its role as the Audit Committee.

3.4 A key challenge for the Auditor Panel is to ensure appropriate appointments that meet the requirements of the Act. It is required that the Panel have at least three members but the majority, including the Chair, should be independent of the GMCA. It is permissible for GMCA elected members to be represented on the panel, but the majority of members and Chair are required to be independent. The definition of independence in the Act and supporting CIPFA guidance is explicit and allows little option other than through the advertisement and appointment of specific, external, independent members. Panel members will also be required to have the requisite skills and experience, which may not be readily identifiable or available given the specialist nature of the external audit contract and procurement processes.

3.5 If the GMCA progresses a single body appointment, it will be required to identify and appoint independent members for this process. The same principle will apply with a joint procurement but the collaborative option means that across the various GM level authorities, only one group of independent members would be required and this increases the likelihood of successfully identifying suitably skilled and experienced independent persons to sit on the panel. These are required to be identified through advertisement arrangements and supported by clear panel member role descriptions. The GMCA and any joint procurement partners will be required to set levels of allowances and expenses.

4 Preferred option

4.1 The GMCA Treasurer and counterparts in TfGM, GMPCC, GMP, GMFRS and GM Waste, as well as across GM local government are supportive of the proposal for a GM level procurement.

4.2 This option allows for economies of scale, given the 2015/16 combined external audit and grant certification fees of these bodies was £1.8m, whilst also enabling a single firm to be able to discharge external audit functions across GMCA, GM Mayor and District functions. This will allow the auditor to take a more strategic approach and should facilitate greater added value in supporting the audited bodies on complex accounting and audit matters.

4.3 A joint procurement is also likely to minimise the time and cost of separate procurements across GM and will also aid the identification and appointment of an appropriate, effective Auditor Panel which it is proposed comprises elected members representing the audited bodies as well as a majority of independent members and independent Chair secured following an open process of advertisement and recruitment.
5 Next Steps

5.1 The GMCA has until December 2017 to make an appointment. In practical terms this means one of the options outlined in this report will need to be in place by Spring 2017 in order that the contract negotiation process can be carried out during 2017.

5.2 The GMCA will need to take action to implement new arrangements for the appointment of external auditors from April 2018. In order that more detailed proposals can be developed and actions progressed the Audit Committee is asked to comment on the options and direct the GMCA Treasurer to take forward a preferred option. This will then enable an action plan and detailed proposals to be developed in terms of the procurement approach; composition of the Auditor Panel; scope of audit work and services required; and engagement approach for working with GM bodies and districts.

6 Recommendations

6.1 Members are requested to confirm a preferred option and approve the GMCA Treasurer to take the appropriate actions to progress a commissioning and procurement process, in proposals for the establishment of an Auditor Panel, in consultation with GMPCC, GMP, GMFRS, TfGM, New Economy, GMWDA and GM District Treasurers.

6.2 Members are asked to receive updates at future Audit Committee meetings.