

## TRAFFORD COUNCIL

**Report to:** Accounts and Audit Committee  
**Date:** 23 November 2016  
**Report for:** Information / Comments  
**Report of:** Chief Finance Officer

### Report Title

**Options for Appointment of External Auditor**

### Summary

The Local Audit and Accountability Act 2014 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 Trafford Council, the appointment of an auditor must be completed by 31 December 2017 for the audit year 2018/19.

### Recommendation

The Accounts and Audit Committee:

1. Consider the proposal for the establishment of a local joint procurement arrangement with GMCA and other neighbouring authorities for the provision of external audit services from 2017/18 and
2. Delegate to the Chair of the Audit and Accounts Committee, under advice from the Chief Finance Officer, to agree the final recommendation to be made to Full Council before March 2017.

### Contact person for access to background papers and further information:

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### **Background Papers:**

- Local Audit and Accountability Act 2014

## **Options for Appointment of External Auditor**

### **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 Trafford Council 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 Local Government Association (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 Council 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 Council 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 Council's current external auditor. It is unlikely that small local independent firms will meet the required eligibility criteria.
- 1.7 The procurement option chosen must be ratified by Full Council.

### **2. Options for Local Appointment of External Auditors**

- 2.1 There are three broad options open to the Council 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 Council 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 Council 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 Council external audit. A newly established and independent Auditor Panel would be responsible for selecting the auditor.
- 2.3 This option allows the Council 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 ongoing expenses and allowances. In addition the Council 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 Council 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.
- 2.5 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 ten councils, there are likely to be benefits from including all these councils in the 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.
- 2.6 In addition the procurement exercise is proposed to include the GM Combined Authority (“GMCA”) and functions due to be consolidated within the GMCA or the Mayor’s Office from 2017 – Transport of Greater Manchester (“TfGM”), the GM Waste Disposal Authority (“GMWDA”), GM Fire and Rescue Service (“GMFRS”), the GM Police and Crime Commissioner’s Office (“GMPCC”), GM Police and New Economy). There are benefits from appointing a limited number of auditors for this group of bodies, not just in terms of economies of scale but also in enabling the external auditors to obtain a fuller understanding of the audit requirements across GM local authorities.
- 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 council or each GM body would be represented on an independent auditor panel. Individual audit committees would still discharge their functions at council 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, individual elected members in Trafford and across GM will have less opportunity for direct involvement in the appointment process other than through the LGA and/or stakeholder representative groups.
- 2.14 Initial conversations with the PSAAL indicated that this option could result in all the councils, GMCA, TfGM and Chief Constable all having different external auditors. However, GM Treasurers are currently seeking clarity with the LGA as to whether the sector led body approach would allow a limited number of cross-GM appointments, 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 councils.
- 2.15 If the PSAAL could work on behalf of the whole of the GM region then this could result in better value without the need to convene a local panel.
- 2.16 In order to take advantage of this offer all the GM Authorities would have to "opt in" by 9<sup>th</sup> March 2017.

### **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 Council 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
  - 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 additional function that might be helpful.
- 3.3 It is also acknowledged that there should be a relationship between the Auditor Panel and the Audit Committee, who will receive updates and assurances arising from the work of the external auditor; and is 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 Council. It is permissible for Council 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 Council 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 GM 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 and supported by clear panel member role descriptions. The Council and any joint procurement partners will be required to set levels of allowances and expenses.

#### **4. Preferred Approach**

- 4.1 The Chief Finance Officer and her counterparts in the other nine GM Councils, GMCA, TfGM, GMPCC, GMP, GMFRS and GM Waste are supportive of the proposal for a co-ordinated approach at GM level.
- 4.2 Option 2 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 limited pool of firms to be able to discharge external audit functions across Trafford Council, other GM Councils and GM bodies referred to in this report. This will allow the auditors 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.
- 4.4 Option 3 (Sector Led appointment) could still also be considered and could result in further savings without the need to appoint an auditor panel; however, as noted in 2.14 above the PSAAL's ability to act for GM as a whole still needs to be clarified.

## **5. Next Steps**

- 5.1 The Council 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. It should also be noted that any decision to take option 3 needs to be taken by the end of February 2017 in order to meet the PSAAL's timetable.
- 5.2 The Council 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 Committees of each of the GM Councils, the GMCA, OPCC / Chief Constable, TfGM, GMFRS and GM Waste are being asked to comment on the options and to work with Treasurers to propose their preferred procurement option to Full Council by end of February 2017.

## **6. Recommendation**

The Accounts and Audit Committee:

1. Consider the proposal for the establishment of a local joint procurement arrangement with GMCA and other neighbouring authorities for the provision of external audit services from 2017/18 and
2. Delegate to the Chair of the Audit and Accounts Committee, under advice from the Chief Finance Officer, to agree the final recommendation to be made to Full Council before March 2017.