MERSEYSIDE FIRE AND RESCUE AUTHORITY			
MEETING OF THE:	AUDIT AND SCRUTINY SUB COMMITTEE		
DATE:	15TH SEPTEMBER 2016	REPORT NO:	CFO/071/16
PRESENTING OFFICER	CHIEF FIRE OFFICER		
RESPONSIBLE OFFICER:	IAN CUMMINS, TREASURER	REPORT AUTHOR:	IAN CUMMINS
OFFICERS CONSULTED:	SMG		
TITLE OF REPORT:	ARRANGEMENTS FOR APPOINTING EXTERNAL AUDITORS		

APPENDICES:	

Purpose of Report

1. To seek approval from Members on the preferred option for the appointment of external audit for the financial years 2018/19 onwards.

Recommendation

2. That Members;
   a. note the change to the arrangements for appointing external auditors for financial year 2018/19 onwards; and
   b. note the options considered in relation to the appointment of external auditors from 1st April 2018, and,
   c. agree to sign-up to a sector led arrangement for the appointment of external auditors as advocated by the Local Government Association (LGA), and
   d. agree to sign-up to the LGA's Public Sector Audit Appointments Limited (PSAA) as the Authority's "appointing person" for the external audit appointment for 2018/19 and future years.

Introduction and Background

3. The Local Audit and Accountability Act 2014 abolished the Audit Commission 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 5th October 2015 the Government determined that the transitional arrangements for local government (including fire and rescue authorities) would be extended by one year to also include the audit of the accounts for 2017/18.

4. The Authority's current external auditor is Grant Thornton, this appointment having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the

contract is currently managed by Public Sector Audit Appointments Limited (PSAA), the transitional body set up by the LGA with delegated authority from the Government. Over recent years the Authority has benefited from significant reductions in fees compared with historic levels. This has been the result of a combination of factors including new contracts negotiated nationally with the firms of accountants and savings from closure of the Audit Commission. The Authority's external audit fees for 2015/16 were £32,424.

5. The current transitional arrangements come to an end on 31st March 2018 therefore for the audit of the accounts of the 2018/19 financial year, there must be a local auditor appointed by 31st December 2017. The Authority is be able to appoint its own auditors if it so wishes. There are three options available to local public bodies for appointing an auditor under the Local Audit and Accountability Act 2014. These are to:

    1. undertake an individual auditor procurement and appointment exercise;

    2. undertake a joint audit procurement and appointing exercise with other bodies, those in the same locality for example; or

    3. join a 'sector led body' arrangement where specified appointing person status has been achieved.

Option 1: Make a stand-alone appointment

6. In order to make a stand-alone appointment the Authority will need to set up an Auditor Panel. The panel will be responsible for choosing the auditor and must consist of wholly or a majority of independent members. Independent members for this purpose excludes current and former elected members (or officers) and their close families and friends. Under this option elected members will not have a majority input when assessing bids and choosing which firm of accountants to award a contract for the Authority's external audit.

The main advantage of setting up an auditor panel would be to allow the Authority to take advantage of the new local appointment regime with decision making at the local level. However, the main drawbacks would appear to be:

- The cost and administrative effort of setting up the Panel, i.e. the recruitment of suitable and qualified independent panel members, deciding remuneration etc.

- Servicing the Auditor Panel, running the bidding exercise and negotiating the contract. Estimates produced by the LGA indicate costs of about £15,000 plus on going expenses and allowances.

- The Authority will not be able to take advantage of reduced fees that may be available through joint or national procurement contracts. Note that the current procurement arrangements were very successful at driving down the cost of external audit to the point whereby a number of even the largest firms were priced out of the market. There is a real risk therefore that any individual authority contracts will not benefit from scale economies and audit firms will increase bids accordingly.

Option 2: Set up a Joint Auditor Panel/local joint procurement arrangements

7. The Act enables the Authority to join with other Authorities to establish a joint auditor panel. Again, this will need to consist of wholly or a majority of independent appointees.

Under this option the cost of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of Authorities and there is an opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.

The main drawbacks are:

- Decision-making will be further removed from local input, with potentially only one elected member representing each organisation, depending on the constitution agreed with the other bodies involved.

- The choice of auditor could be complicated where individual organisations have independence issues, i.e. where an auditor is carrying out work such as consultancy or advisory work for the Authority/Council. Where this occurs some auditors may be prevented from being appointed by the terms of their professional standards. There is a risk that if the joint auditor panel choose a firm that is conflicted for this Authority then the Authority may still need to make a separate appointment with all the attendant costs and loss of economies possible through joint procurement.

Option 3: Opt-in to a sector led body

8. The LGA have successfully lobbied for Councils/Fire and Rescue Authorities to be able to 'opt-in' to a Sector Led Body (SLB) when making external audit appointments. An SLB would have the ability to negotiate contracts with audit firms nationally, maximising the opportunities for the most economic and efficient approach to procurement of external audit on behalf of the whole sector.

9. The benefits of opting in are:

- The cost of setting up the appointment arrangements and negotiating fees would be shared across all opt-in Authorities.

- 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 Authority level would be managed by the SLB who would have a number of contracted firms to call upon.

The main drawback of this approach is that it requires the creation of a separate Government approved body to act in the collective interests of the 'opt-in' Authorities. The LGA have set-up the Public Sector Audit Appointments Limited (PSAA) to be such a body, with the PSAA utilising the knowledge and experience acquired from the previous procurement process. In July 2016, the Secretary of State for Communities and Local Government, specified PSAA as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015. This means that PSAA can make auditor appointments for audits of the accounts from 2018/19 of principal Authorities that choose to opt into its arrangements. It is by no means certain that the PSAA will attract sufficient councils that will sign-up at this stage to generate the benefits previously outlined. With this in mind the LGA have recently written to all council chief executives in an attempt to gauge the level of support from councils for a collective sector-wide audit appointment. It is understood they received significant support from the sector. The PSAA is aiming to establish an overall strategy for procurement of external audit by 31st October 2016 and achieve "signup" of scheme members by early January 2017. It then hopes

to invite tenders by eligible audit firms by March 2017 and award contracts by June 2017 with final appointments by 31st December 2017.

10. The scope of the audit will still be specified nationally, the National Audit Office (NAO) is responsible for writing the Code of Audit Practice which all firms appointed to carry out the Authority's audit must follow. 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 has not yet commenced and so the number of firms is not known but it is reasonable to expect that the list of eligible firms may include the top 5 - 12 firms in the country, and is likely to include the Authority's current auditor. It is unlikely that small local independent firms will meet the eligibility criteria.

Conclusion:

11. The Authority will have until December 2017 to make an appointment. In practical terms this means that one of the options outlined above will need to be in place by Spring 2017 in order that the contract negotiation process can be carried out during that year.

12. Given that the LGA have developed a sector led approach, PSAA, then it would seem advantageous for the Authority to opt-in to such arrangements given the significant benefits associated with scale economies. To maximise these benefits and strengthen its negotiating position the LGA are seeking the maximum number of councils acting collectively. At this stage therefore the Treasurer recommends that the Authority should support the LGA approach. The Authority can withdraw from the LGA approach at any point.

13. It is the view of Officers that early consideration of the preferred approach will enable detailed planning to take place so as to achieve successful transition to the new arrangement in a timely and efficient manner. Progress will need to be carefully monitored should the sector led procurement approach not prove feasible so that alternative arrangements can be put in place in a timely manner. .

Equality and Diversity Implications

14. Not applicable.

Staff Implications

15. Not applicable.

Legal Implications

16. The Local Audit and Accountability Act 2014 abolished the Audit Commission and established transitional arrangements for the appointment of external auditors. Additional regulations, the Local Audit (Appointing Person) Regulations 2015 and the Accounts and Audit Regulations 2015 require the Authority to meet various requirements when determining the appointment of the external auditor.

Financial Implications & Value for Money

17. The cost of the current external audit function is £32,424. The audit fees for 2018/19 are unlikely to be finalised until March 2018.

18. If the Authority approves the recommendation to appoint future external auditors via the PSAA route then the PSAA will not charge a membership fee. The audit fees that opted-in bodies will be charged will cover the costs to PSAA.

19. If the Authority went down the audit panel route then it would need to cover the cost of appointing independent members, servicing the Audit Panel, all the costs associated with an appointment of external auditor procurement process and the costs of managing and monitoring the contract. The Authority is also unlikely to benefit from any saving on audit fees that are likely to be delivered via the PSAA being able to negotiate the audit fees for large contracts.

Risk Management, Health & Safety, and Environmental Implications

20. Not applicable.

Contribution to Our Mission: Safer Stronger Communities – Safe Effective Firefighters

21. External audit help ensure the Authority's internal controls and financial management are robust and therefore funds earmarked for fire operational activities remain intact.

BACKGROUND PAPERS

GLOSSARY OF TERMS

LGA	Local Government Association
PSAA	Public Sector Audit Appointments Limited
SLB	Sector Led Body
NAO	National Audit Office