



## **WEST MIDLANDS** COMBINED AUTHORITY

# **Board Meeting**

<b>Date</b>	9 December 2016
<b>Report title</b>	Decision to opt-in to the national scheme for auditor appointments
<b>Portfolio Lead</b>	Councillor Izzi Seccombe – Finance and Investment
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<b>Report to be/has been considered by</b>	WMCA Management Board (10 <sup>th</sup> November 2016)

### **The Combined Authority Board is recommended to:**

1. The Combined Authority Board is requested to agree to opt-in to the sector led option for the appointment of external auditors for the five years commencing 1 April 2018.

## 2. Purpose

1. This report sets out the proposals for appointing the external auditor to the Combined Authority for the 2018/19 accounts and beyond, as the current arrangements only cover up to and including 2017/18 audits. The auditors are currently working under a contract originally let by the Audit Commission which was novated to Public Sector Audit Appointments (PSAA) following the closure of the Audit Commission.
2. The Combined Authority Board will need to consider the options available and put in place new arrangements in time to make a first appointment by 31 December 2017.

## 3. Background

1. The Local Audit and Accountability Act 2014 (the Act) brought to a close 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 5 October 2015 the Secretary of State Communities and Local Government (CLG) 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.
2. The Act also set out the arrangements for the appointment of auditors for subsequent years, with the opportunity for authorities to make their own decisions about how and by whom their auditors are appointed. Regulations made under the Act allow authorities to 'opt in' for their auditor to be appointed by an 'appointing person'.
3. In July 2016 PSAA were specified by the Secretary of State as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015. The appointing person is sometimes referred to as the sector led body and PSAA has wide support across local government. PSAA was originally established to operate the transitional arrangements following the closure of the Audit Commission under powers delegated by the Secretary of State. PSAA is an independent, not-for-profit company limited by guarantee and established by the Local Government Association (LGA).
4. PSAA is inviting the Combined Authority to opt in, along with all other authorities, so that PSAA can enter into a number of contracts with appropriately qualified audit firms and appoint a suitable firm to be the Combined Authority's auditor.
5. The principal benefits from such an approach are as follows:
  - PSAA will ensure the appointment of a suitably qualified and registered auditor and expects to be able to manage the appointments to allow for appropriate groupings and clusters of audits where bodies work together;
  - PSAA will monitor contract delivery and ensure compliance with contractual, audit quality and independence requirements;
  - Any auditor conflicts at individual authorities would be managed by PSAA who would have a number of contracted firms to call upon;
  - It is expected that the large-scale contracts procured through PSAA will bring economies of scale and attract keener prices from the market than a smaller

scale competition;

- The overall procurement costs would be lower than an individual smaller scale local procurement;
  - The overhead costs for managing the contracts will be minimised through a smaller number of large contracts across the sector;
  - There will be no need for the Combined Authority to establish alternative appointment processes locally, including the need to set up and manage an 'auditor panel', see below;
  - The new regime provides both the perception and reality of independent auditor appointment through a collective approach; and
  - A sustainable market for audit provision in the sector will be easier to ensure for the future.
6. The Combined Authority's current external auditor is Grant Thornton UK LLP. Grant Thornton were the auditors to the West Midlands Integrated Transport Authority (ITA) and the West Midlands Passenger Transport Executive (PTE), these appointments having been made under a contract let by the Audit Commission. Following closure of the Audit Commission the contract was novated to PSAA who approved the appointment of Grant Thornton as external auditor to the Combined Authority on 1 September 2016.
  7. PSAA has demonstrated its capability in terms of auditor appointment, contract management, and monitoring audit quality. Over recent years authorities have benefited from a reduction in fees in the order of 50% - 55% compared with fees in 2012. This has been the result of a combination of factors including new contracts negotiated nationally with the audit firms and savings from closure of the Audit Commission. The combined audit fees of the PTE and ITA were £53,000 per annum for 2015/16. The proposed fees from 2018/19 cannot be known until the procurement process has been completed, as the costs will depend on proposals from the audit firms.
  8. 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 Combined 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.
  9. Currently, there are only nine providers that are eligible to audit local authorities and other relevant bodies; all of these being firms with a national presence. This means that a local procurement exercise, as described immediately below, would seek tenders from these same firms, subject to the need to manage any local independence issues. Local firms could not be invited to bid.
  10. Note that all the other Metropolitan districts have also chosen to opt-in to the sector led option.

#### **4. Other options**

1. If the Combined Authority did not opt in there would be a need to establish an independent auditor panel. In order to make a stand-alone appointment the auditor panel would need to be set up by the Combined Authority itself. The members of the panel must be wholly or a majority of independent members as defined by the Act. Independent members for this purpose are independent appointees, this excludes current and former elected members (or officers) and their close families and friends. This means that elected members will not have a majority input to assessing bids and choosing which audit firm to award a contract for the Combined Authority's external audit.
2. Alternatively the Act enables the Combined Authority to join with other authorities to establish a joint auditor panel. Again this will need to be constituted of wholly or a majority of independent appointees (members). Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each Council/Authority under the Act and the Combined Authority would need to liaise with other local authorities to assess the appetite for such an arrangement.
3. Neither of these options are recommended. Both these options would be more resource-intensive processes to implement and without the bulk buying power of the sector led procurement, would be likely to result in a more costly service. It would also be more difficult to manage quality and independence requirements through a local appointment process

#### **5. Next steps**

1. Regulation 19 of the Local Audit (Appointing Person) Regulations 2015 requires that a decision to opt-in must be made by a meeting of the Council/Authority (meeting as a whole). PSAA expects to issue the invitation to 'opt in' to all Councils/Authorities by early November 2016. The Combined Authority then needs to formally respond to PSAA's invitation in the form specified by PSAA by early March 2017.
2. PSAA will commence the formal procurement process after this date. It expects to award contracts in summer 2017 and consult with authorities on the appointment of auditors so that it can make an appointment by the statutory deadline of December 2017.

#### **6. Risk management**

1. The principal risks are that the Combined Authority fails to appoint an auditor in accordance with the new frameworks or does not achieve value for money in the appointment process. These risks are considered best mitigated by opting in to the sector led approach through PSAA.

## **7. Legal implications**

1. Section 7 of the Local Audit and Accountability Act 2014 (the Act) requires a relevant Council/Authority to appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding year. Section 8 governs the procedure for appointment including that the Council/Authority must consult and take account of the advice of its auditor panel on the selection and appointment of a local auditor.
2. Section 8 provides that where a relevant Council/Authority is a local Council/Authority operating executive arrangements, the function of appointing a local auditor to audit its accounts is not the responsibility of an executive of the Council/Authority under those arrangements.
3. Section 12 makes provision for the failure to appoint a local auditor: the Council/Authority must immediately inform the Secretary of State, who may direct the Council/Authority to appoint the auditor named in the direction or appoint a local auditor on behalf of the Council/Authority.
4. Section 17 gives the Secretary of State the power to make regulations in relation to an 'appointing person' specified by the Secretary of State. This power has been exercised in the Local Audit (Appointing Person) Regulations 2015 (SI 192) and gives the Secretary of State the ability to enable a Sector Led Body to become the appointing person. In July 2016 the Secretary of State specified PSAA as the appointing person.

## **8. Financial implications**

1. Current external fees levels are likely to increase when the current contracts end in 2018.
2. Opting-in to a national scheme provides maximum opportunity to ensure fees are as low as possible, whilst ensuring the quality of audit is maintained by entering in to a large scale collective procurement arrangement.
3. If the national scheme is not used some additional resource may be needed to establish an auditor panel and conduct a local procurement. Until a procurement exercise is completed it is not possible to state what, if any, additional resource may be required for audit fees for 2018/19.

## **9. Other implications**

1. There are no other implications arising from this report.

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