

Date: **21 January 2022**

Subject: **Options for appointment of external auditor from 2023/24**

Report of: **Steve Wilson, Treasurer of the GMCA**

Purpose of Report

The purpose of this report is to present the options available for appointment of external auditors for Greater Manchester Combined Authority to take effect from 2023/24 and provide information on the process for retendering of external audit contracts.

Recommendations:

The Audit Committee is requested to:

1. Note the recommendation for GMCA and GMP to opt-in to the Public Sector Audit Appointment (PSAA) body for appointment of external auditors;
2. Note the proposal to continue with local joint procurement arrangements for the provision of external audit services with TfGM and other Greater Manchester authorities.
3. Delegate to the GMCA Treasurer, in consultation with the Chair of the Audit Committee, to agree the final recommended option to be made to GMCA and Police and Crime Panel.

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Equalities Impact, Carbon and Sustainability Assessment:

N/A

Risk Management

Considered within the body of the report.

Legal Considerations

N/A

Financial Consequences – Revenue

Financial revenue consequences are discussed within the body of the report.

Financial Consequences – Capital

N/A

Number of attachments to the report: None

Comments/recommendations from Overview & Scrutiny Committee

N/A

Background Papers

N/A

Tracking/ Process

Does this report relate to a major strategic decision, as set out in the GMCA Constitution?

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 relevant Scrutiny Committee on the grounds of urgency? No

GM Transport Committee

N/A

Overview and Scrutiny Committee

N/A

1. INTRODUCTION AND PURPOSE OF REPORT

- 1.1 The purpose of this report is to present the options available for appointment of external auditors for Greater Manchester Combined Authority (GMCA) to take effect from 2023/24 and provide information on the process for retendering of external audit contracts.

2. RETENDER OF EXTERNAL AUDIT CONTRACTS

Information from the Local Government Association for those charged with governance

- 2.1 The process for retendering for external audit in local authorities in England, for contracts due to start from 2023/24, is now underway and shortly GMCA will need to decide whether to procure its own external auditor or opt into the national procurement framework.
- 2.2 Legislation requires a resolution of GMCA if a local authority wishes to opt into the national arrangement. The deadline for this decision is the 11th March 2022. If the GMCA does not make such a decision, the legislation assumes that the authority will procure its own external audit, with all the extra work and administration that comes with it.
- 2.3 The national framework is considered the best option authorities can choose. There are many reasons for favouring the national arrangements and those reasons have become more compelling since 2016/17 when local authorities and public bodies were last asked to make this choice.
- 2.4 The way external audit has operated over this period has changed considerably. A lack of capacity in the audit market has been exacerbated by increased requirements placed on external auditors by the audit regulator. There is also a limited number of firms in the market and too few qualified auditors employed by those firms. This has led to a situation around the country where audits have been delayed and audit opinions remain outstanding from 2019/20 and 2020/21. Auditors have also been asking for additional fees to pay for extra work.
- 2.5 As the client in the contract, an authority has little influence over what it is procuring. The nature and scope of the audit is determined by codes of practice and guidance and the regulation of the audit market is undertaken by a third party, currently the Financial Reporting Council. Essentially authorities find themselves operating in what amounts to a suppliers' market and the client's interest is at risk of being ignored unless we act together.
- 2.6 It is widely acknowledged that supply side of the market needs to be expanded, which includes encouraging bids from challenger firms. Public Sector Audit Appointments Ltd (PSAA), the body nominated by the Government to run the national arrangements, has suggested various ways this could be done, but these initiatives are much more likely to be successful if a large number councils sign up to the national scheme.
- 2.7 It is therefore vital that local authorities and partner public bodies coordinate their efforts to ensure that the client voice is heard loud and clear. The best way of doing this across the country is to sign up to the national arrangement.
- 2.8 To summarise, the same issues apply as at the time of the last procurement:

- A body procuring its own auditor or procuring through a joint arrangement means setting up an Audit Panel with an independent chair to oversee the procurement and running of the contract.
- The procurement process and contract management capacity within the authority would be required.
- Procuring through the appointing person (PSAA) gives greater independence in the process for authorities in appointing its auditors.
- Procurement as an individual authority provides no additional benefit:
 - The service being procured is defined by statute and by accounting and auditing codes
 - Possible suppliers are limited to the small pool of registered firms with accredited Key Audit Partners (KAP).
 - Since the last procurement it is now more obvious than ever that we are in a 'suppliers' market' in which the audit firms hold most of the levers.
- PSAA has now built up considerable expertise and has been working hard to address the issue that have arisen with the contracts over the last couple of years:
 - PSAA has the experience of the first national contract. The Government's selection of PSAA as the appointing person for a second cycle reflects MHCLG's confidence in them as an organisation.
 - PSAA has commissioned high quality research to understand the nature of the audit market.
 - It has worked very closely with MHCLG to enable the government to consult on changes to the fees setting arrangements to deal better with variations at national and local level, hopefully resulting in more flexible and appropriate Regulations later this year.

3. OPTIONS FOR LOCAL APPOINTMENT OF AN EXTERNAL AUDITOR

- 3.1 There are three broad options open to the authority under the Act and new appointments for auditors need to be made by 11th March 2022 regardless of which option is chosen.

Option 1: Make a stand-alone appointment

- 3.2 To make a stand-alone appointment, 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/GMP external audit. A newly established and independent Auditor Panel would be responsible for selecting the auditor.
- 3.3 This option allows 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, GMCA would not benefit from reduced fees that may be available through joint or national procurement contracts.

Option 2: Local joint procurement arrangements

- 3.4 The Act enables the authority 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 GMCA will need to liaise with other authorities to assess the appetite for this arrangement.
- 3.5 At present, the ten Greater Manchester district councils, GMCA, GMP and TfGM are audited by Mazars under the local joint procurement arrangement. Given the level of collaboration and joint working, there have been benefits in this procurement approach. 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.
- 3.6 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.
- 3.7 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.
- 3.8 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

- 3.9 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 (PSAA). PSAA is now well established and has 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.

- 3.10 Under this approach, the costs of setting up the appointment arrangements and negotiating fees are shared across all opt-in authorities and by offering large contract values the firms are able to offer competitive rates and fees than are likely to result from local negotiation. Any conflicts at individual authorities are managed by PSAA who have a number of contracted firms to call upon.
- 3.11 The appointment process would not be ceded to locally appointed independent members but by a separate body that acts in the collective interests of the 'opt-in' authorities.
- 3.12 Under this option, individual elected members 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 all the districts, GMCA, TfGM and Chief Constable all having different external auditors.
- 3.13 In order to pursue this option the authority would have to "opt in" by 11th March 2021.

4. AUDITOR PANEL

- 4.1 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; and
- any proposals to enter into limited liability agreements (auditor panels have a statutory duty to give advice to the authority if the authority proposes to enter into a liability limitation agreement. If panel members lack knowledge or experience in this area, it is recommended that training is sought that may assist them in this duty).

- 4.2 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.
- 4.3 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.
- 4.4 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 authority. 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.
- 4.5 If the authority 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 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.

5 RECOMMENDED OPTIONS

- 5.1 The recommended option is for an opt in to the sector-led body - PSAA (option 3) which is consistent with counterparts in the ten GM Councils and TfGM.
- 5.2 This option is likely to minimise the time and cost of separate procurements across GM and will also negate the need for an additional Auditor Panel.
- 5.3 It is also proposed to continue with local joint procurement arrangements for the provision of external audit services with TfGM and other Greater Manchester authorities.

6. NEXT STEPS

- 6.1 GMCA will need to take action to implement new arrangements for the appointment of external auditors from April 2023. A decision on the options outlined in this report should be made by 11th March 2022 in order that the contract negotiation process can be carried out during 2022 to meet the statutory deadline for award of contracts by 31st December 2022. The closing date to opt in to the PSAA arrangement is 28th February 2022.

7. RECOMMENDATIONS

- 7.1 Recommendations are set out at the front of the report.