

LANCASHIRE COMBINED FIRE AUTHORITY  
Meeting to be held on 20 February 2017

**APPOINTMENT OF EXTERNAL AUDITORS  
(Appendices 1 and 2 refer)**

Contact for further information:  
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**Executive Summary**

The current external audit appointment ends following the conclusion of the 2017/18 audits. As such the Authority will need to make alternative arrangements for appointing an auditor.

In order to do so the Authority has 3 options:

- Follow a sector led body;
- Set up an Audit Panel, undertake a procurement process and make a stand-alone appointment;
- Set up a Joint Auditor Panel, undertake a joint procurement panel and make a joint appointment.

**Decision Required**

The Authority is asked to approve to opt-in to the national procurement being undertaken by Public Sector Audit Appointments.

**Information**

In March 2016 a report was presented to the Audit Committee looking at options for the future appointment of external auditors:-

- Follow a sector led body;
- To make a stand-alone appointment;
- Set up a Joint Auditor Panel/local joint procurement arrangements.

A copy of the report is attached as appendix 1. Members agreed that following a sector led body was the best option to pursue at the time, minimising procurement costs and resource, maximising buying power and hence was likely to result in the lowest fees. Hence it was resolved “That the Committee agree to support the Local Government Association in setting up a national Sector Led Body by indicating an intention to opt-in.” (Resolution 22/15 refers.)

Further details relating to the sector led approach were presented to the Audit Committee in January, and a copy of that report is attached as appendix 2. Members expressed concerns that the audit fees would only be consulted on in the autumn, after the contracts had been awarded and asked for a more comprehensive report to be presented to the Authority in February.

The current situation remains as set out in these reports, namely that the current contract expires and that a new contract must be in place by December 2017. The Authority cannot have a period where it does not have an appointed external auditor.

Options for appointing an auditor remain as:-

- Follow a sector led body;
- Set up an Audit Panel, undertake a procurement process and make a stand-alone appointment;
- Set up a Joint Auditor Panel, undertake a joint procurement panel and make a joint appointment.

### **Follow a sector led body**

The Secretary of State appointed Public Sector Audit Appointments (PSAA) to appoint local auditors under a national scheme. PSAA is an independent, not-for-profit company limited by guarantee and established by the LGA.

PSAA is inviting the Authority to opt in, along with all other authorities, so that it can undertake a procurement exercise to award a number of contracts with appropriately qualified audit firms, and ultimately to appoint a suitable firm to be the Authority's auditor.

It is worth noting that in order for the Sector Led Body approach to be viable and to be placed in the strongest possible negotiating position then authorities need to commit to this approach before final contract prices are known.

PSAA have already issued an OJEU Contract Notice in February 2017. Eligible bodies must notify PSAA of a decision to opt-in by 9<sup>th</sup> March 2017; anyone not opting in by that date will be unable to opt-in until the following year, and hence will need to appoint their own external auditors by the end of December 2017.

The tender evaluation process is based 50% on cost and 50% on quality, and will complete in June 2017 when the PSAA Board approves the award of contracts.

PSAA will pool scheme costs and charge fees to audited bodies in accordance with a fair scale of fees which has regard to size, complexity and audit risk, most likely as evidenced by audit fees for 2016/17. This means that everyone in the scheme will benefit from the most competitive prices.

The actual audit fees charged to individual authorities will be determined by the prices achieved in the procurement process. Once contracts are awarded the overall cost and therefore the level of fees required will be clear, following which PSAA will undertake a consultation exercise on audit fees in the autumn 2017 and will publish the fees applicable for 2018/19 in March 2018.

This approach is consistent with the procurement exercise that the Audit Commission undertook in 2011/12, and with the principle of a consultation on proposed fees taking place each year, which has happened for many years. It is also

worth noting that prior to the Audit Commission procurement exercise, and based on audit requirements at that time, the audit fee was £68k; it currently stands at £31k, a reduction of over 50%.

#### Advantages/benefit

- 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 (by way of example if all bodies opted in to the national process the annual fee value is in excess of £35m, whereas our individual fee is £31k) ;
- 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 Authority to establish alternative appointment processes locally, including the need to set up and manage an 'auditor panel';
- A sustainable market for audit provision in the sector will be easier to ensure for the future.

#### Disadvantages/risks

- Individual elected members will have no direct involvement in the appointment process, as this will be undertaken by PSAA, however PSAA have been appointed to work in the interests of all authorities;

#### **Set up an Audit Panel, undertake a procurement process and make a stand-alone appointment**

In order to make a stand-alone appointment the Authority will need to set up an Auditor Panel. The members of the panel must be wholly or a majority 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 firm of accountants to award a contract for the Authority's external audit.

Once established the audit panel would then need to undertake a procurement exercise to award a contract for the provision of external audit services. As with all procurement exercises the final price will not be known until such time as a procurement exercise is completed, by which time it is too late to opt in to the national exercise, or to undertake a further procurement exercise.

It is worth noting that currently there are only nine providers that are eligible to audit local authorities and other relevant bodies, all of whom have a national presence, and will be included in the national sector led approach.

#### Advantages/benefit

- Setting up an auditor panel allows the Authority to take maximum advantage of the new local appointment regime and have local input to the decision.

#### Disadvantages/risks

- 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 £15k 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;
- The assessment of bids and decision on awarding contracts will be taken by independent appointees and not solely by elected members;
- Given the relatively low value of our external audit service (current cost is £31k) there may be a limited number of interested bidders who meet the required standards,

### **Set up a Joint Auditor Panel, undertake a joint procurement panel and make a joint appointment**

The Act enables the Authority to join with other authorities to establish a joint auditor panel, who will need to be constituted of wholly or a majority of independent appointees (members). This joint panel would then undertake a procurement exercise, and again the cost of the audit will not be known until such time as a procurement exercise is completed, by which time it is too late to opt in to the national exercise, or to undertake a further procurement exercise

Further legal advice will be required on the exact constitution of such a panel having regard to the obligations of each Authority under the Act and the Authority need to liaise with other local authorities to assess the appetite for such an arrangement. Informal enquiries have not identified any Authorities who wish to be involved in a joint exercise.

#### Advantages/benefits

- The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities;
- There is greater opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.

#### Disadvantages/risks

- The decision making body will be further removed from local input, with potentially no input from elected members where a wholly independent auditor panel is used or possible only one elected member representing each Authority, depending on the constitution agreed with the other bodies involved;
- The choice of auditor could be complicated where individual Authorities have independence issues. An independence issue occurs where the auditor has

recently or is currently carrying out work such as consultancy or advisory work for the Authority. 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;

- Compared with the national contract this would still be likely to be a low value contract and again there may be a limited number of interested bidders who meet the required standards.

## **Recommendation**

At the date of writing the report 287 Authorities (which is more than 60% of all authorities) had opted in to the national sector led solution via Public Sector Audit Appointments. The Treasurer is not aware of any other Lancashire based Authority or any other Fire Authority that is pursuing a different option.

The concerns expressed by the Audit Committee revolved around the cost of the audit not being known until the Autumn consultation, after the contract has been awarded, and a question as to whether undertaking our own exercise would deliver a better value solution.

As highlighted earlier the contract award criteria is split 50% on price and 50% on quality, hence it is clear that achieving a competitive price remains at the forefront of the exercise.

PSAAs letter inviting the Authority to opt-in states:-

- *We will ensure that fee levels are carefully managed by securing competitive prices from firms and by minimising our own costs. Any surplus funds will be returned to scheme members under our articles of association and our memorandum of understanding with the Department for Communities and Local Government and the LGA.*
- *Our costs for setting up and managing the scheme will need to be covered by audit fees. We expect our annual operating costs will be lower than our current costs because we expect to employ a smaller team to manage the scheme. We are intending to fund an element of the costs of establishing the scheme, including the costs of procuring audit contracts, from local government's share of our current deferred income. We think this is appropriate because the new scheme will be available to all relevant principal local government bodies.*
- *PSAA will pool scheme costs and charge fees to audited bodies in accordance with a fair scale of fees which has regard to size, complexity and audit risk, most likely as evidenced by audit fees for 2016/17. Pooling means that everyone in the scheme will benefit from the most competitive prices. Fees will reflect the number of scheme participants – the greater the level of participation, the better the value represented by our scale fees.*
- *Scale fees will be determined by the prices achieved in the auditor procurement that PSAA will need to undertake during the early part of 2017. Contracts are likely to be awarded at the end of June 2017, and at this point*

*the overall cost and therefore the level of fees required will be clear. We expect to consult on the proposed scale of fees in autumn 2017 and to publish the fees applicable for 2018/19 in March 2018.*

A national procurement exercise must provide greater buying power, clearly minimises individual authorities procurement costs, especially any costs associated with establishing and servicing an independent auditor appointment panel, and hence should deliver the greatest value for money. As such this is still seen as the best option to pursue.

### **Financial Implications**

Opting-in to a national Sector Led Body is anticipated to result in the most competitive audit fees, and will remove the costs of establishing an auditor panel. However, it must be acknowledged that until any procurement exercise, either national or local is completed the impact on existing fees cannot be determined.

### **Human Resource Implications**

None

### **Equality and Diversity Implications**

None

### **Business Risk Implications**

There is no immediate risk to the Authority, however the Local Audit and Accountability Act 2014 (the Act) requires a relevant authority to appoint a local auditor to audit its accounts for a financial year not later than 31 December in the preceding year.

### **Environmental Impact**

None

### **Local Government (Access to Information) Act 1985**

### **List of Background Papers**

Paper	Date	Contact
None		
Reason for inclusion in Part II, if appropriate:		