

Consultation on the 2022/23 audit fee scale

Opted-in local government, fire and police bodies

August 2022

Public Sector Audit Appointments Limited (PSAA) is an independent company limited by guarantee incorporated by the Local Government Association in August 2014.

In July 2016, the Secretary of State specified PSAA as an appointing person for principal local government authorities for audits from 2018/19, under the provisions of the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015.

From 2018/19 PSAA is responsible for appointing an auditor and setting scales of fees for relevant principal authorities that have chosen to opt into its national scheme.

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Summary

- 1 This consultation invites audited bodies and stakeholders to submit views on PSAA's proposals for setting the fee scale for the audit of opted-in bodies' 2022/23 financial statements and value for money arrangements. Audit work under this fee scale will largely be undertaken from autumn 2023 onwards.
- 2 Consultees will be aware that auditors and auditing have been subject to very high levels of scrutiny in recent times following a number of widely reported financial failures in the private sector. These events led the government to commission a series of reviews focusing on audit regulation, the audit market, audit quality and effectiveness, and more specifically the framework for local audit and financial reporting.
- 3 The Department for Levelling Up Housing and Communities (DLUHC) has announced [a range of measures](#) to address the challenges identified in relation to the local audit framework. These measures include arrangements for a 'system leader', a role which is to be located within a new regulator, the Audit Reporting and Governance Authority (ARGA) when it is established. In preparation, the Financial Reporting Council (FRC) will implement shadow arrangements and has appointed the first Director of Local Audit, who will take up a post leading a dedicated local audit unit in September 2022.
- 4 This consultation is therefore taking place in the context of the significant tensions and pressures in the wider audit market and profession, and of evolving arrangements in the local audit system. The issues highlighted in 2020 in the [Redmond review](#) of local audit and financial reporting continue to have a significant impact on audit delivery and have led to increasing delays for auditors in completing some audits.
- 5 The consultation is carried out in accordance with the relevant provisions of the Appointing Person Regulations, which include the requirement to consult on and set the audit fee scale before 1 December of the relevant financial year.
- 6 The consultation explains how PSAA proposes to calculate the audit fees which will make up the 2022/23 fee scale. The proposal involves managing the impact of three key elements:
 - fee variations approved in relation to 2019/20 and 2020/21 audit work which relate to recurrent audit work in subsequent audit years;
 - changes in local audit requirements; and
 - the impact of changes in inflation.
- 7 The 2022/23 audit year is the last in the current five-year appointing period, which covers the audits of the accounts of relevant authorities for 2018/19 to 2022/23.
- 8 New audit contracts will apply for the five audit years from 2023/24, following a PSAA audit procurement exercise during 2022. Any fee implications arising from the results of the procurement will be considered in our consultation on the 2023/24 fee scale in twelve months' time.

Responding to the consultation

We welcome comments on the proposals contained in this document. Please send feedback to:

<https://www.surveymonkey.co.uk/r/LXTQ2MH>

The consultation will close on **Friday 30 September 2022**.

Fee scale 2022/23

Introduction

- 9 As the appointing person for local authorities, fire and police bodies, PSAA is required to undertake consultations before setting audit fee scales. This year's consultation, on the fee scale for the audit of 2022/23 financial statements and value for money arrangements of bodies that have opted into PSAA's national auditor appointment scheme, takes place in the context of continuing significant turbulence and uncertainty in the local audit market.
- 10 The 2020 [Redmond review](#) into local audit and the transparency of local authority financial reporting highlighted a lack of coherence in the current local audit framework, contributing to wider issues including audit delays and market instability. Delays are becoming more prevalent under the pressure of increasing expectations from professional regulators, shortages of experienced auditors, greater complexity of transactions and structures, and the challenges posed by the Covid pandemic.
- 11 The government has announced [a range of measures](#) to strengthen the local audit framework. A 'system leader' role will be discharged by a new regulator, ARGA, when it is established under new legislation. In preparation, the FRC will implement shadow arrangements and has appointed the first Director of Local Audit, who will take up the post of leading a dedicated local audit unit in autumn 2022. In the meantime, DLUHC is acting as interim system leader.
- 12 PSAA is required to set a fee scale under the statutory requirements and timescales set out in the Local Audit Regulations. Changes to the regulations in February 2022 included moving the fee setting deadline from March to November, to provide more scope to set fees based on information from completed audits. The statutory requirement is now that a fee scale must be set before 1 December of the relevant financial year and cannot subsequently be amended.
- 13 This later deadline applies for the first time to the 2022/23 fee scale, the last in the current five-year appointing period. Even with the added time, PSAA must consult on the 2022/23 fee scale before work on the 2021/22 audits is undertaken. The impact of delayed audit completions means that around 40% of 2020/21 audits also remain outstanding. As with the fee scales for the four audit years 2018/19 to 2021/22, this means PSAA is setting the fee scale without the benefit of information on the outcome of audits for the preceding year or years, and without a clear picture of the additional audit work needed.
- 14 Audit requirements have increased in recent years as a result of increased regulatory expectations and changes to the audit work required under the Code of Audit Practice and updated auditing and financial reporting standards. As audit work must be undertaken after the financial year and fee scales have, prior to this year, had to be set before it starts, it has been necessary for PSAA to evaluate the impact on fees of any additional audit requirements through the fee variations process.
- 15 We aim to consolidate fee variations for ongoing additional audit requirements into a future fee scale at the earliest opportunity, removing the need for continued discussion each year between opted-in bodies and auditors about the additional fees for ongoing work. We received generally positive feedback on this approach from opted-in bodies and

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stakeholders in consultations in November 2020 on fee variation arrangements and in 2021 on the 2021/22 fee scale. We propose to continue this approach for the 2022/23 fee scale.

Factors to be considered in setting the 2022/23 fee scale

- 16 PSAA set the most recent fee scale, for the 2021/22 audits, in March 2021. At that time, we were able to consolidate into the fee scale approved 2018/19 fee variations for ongoing audit requirements where these had been submitted for approval.
- 17 The 2021/22 fee scale is the baseline from which we will set the 2022/23 fee scale. We will update the fee scale to take account of more recent approved fee variations for ongoing work. In setting the fee scale, we also need to consider whether we can update it to reflect changes in audit requirements that apply from 2022/23.

Approved fee variations which relate to audit work of an ongoing nature

- 18 Auditors may find it necessary to carry out additional audit work in order to give their audit opinion. This may be because requirements have changed, or it may be due to local circumstances. The regulations allow for additional fees to be payable where significant additional work is required. Additional fees are evaluated under our [fee variations process](#) and are subject to PSAA approval.
- 19 Where the additional audit work is of an ongoing nature, it makes sense to update the relevant scale fee at the earliest opportunity, to reflect the need for that work in future years. In this way we aim to ensure that all fees are systematically updated on a regular basis for any changing audit work requirements. In contrast, non-recurrent additional work continues to be dealt with through one-off fee variations each year.
- 20 In the 2022/23 fee scale we are proposing to consolidate the additional fees needed for ongoing audit work identified in 2019/20 and 2020/21 fee variations, excluding the fees needed for work on the VFM commentary and ISA540. We can do this where audits are complete and fee variations have been submitted to and approved by PSAA.
- 21 Ongoing additional audit work generally falls into the following categories:
 - group accounts;
 - pension valuation;
 - PPE valuation;
 - increased regulatory challenge;
 - public interest entity requirements; and
 - PFI.
- 22 While we do not have complete information yet for all 2019/20 or 2020/21 audits, we do have many audits with agreed and approved fee variations. Where we do not have approved fee variation information for individual bodies, we will need to consolidate those requirements into a future fee scale consultation. When we update the fee scale for recurring 2019/20 and 2020/21 fee variations, we will strip out any elements that have already been baked into scale fees in prior years to ensure we avoid any double counting.

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23 As part of this consultation we will write to all individual opted-in bodies to explain the proposed change to their scale fee for 2022/23. This will ensure that individual bodies have an opportunity to ask questions and, if appropriate, to challenge our proposals. For the avoidance of doubt, we will write to:

- bodies which have been subject to approved fee variations for 2019/20 or 2020/21 that we have assessed as being of an ongoing nature (with the proposed impact on their 2022/23 scale fee);
- bodies for which approved fee variations have not related to work of an ongoing nature, or which have not been subject to approved fee variations (whose 2022/23 scale fees will be unaffected); and
- bodies for which claims for 2019/20 and 2020/21 fee variations remain outstanding (whose scale fees may need to be updated for a future fee scale).

Changes in local audit requirements

24 Where local audit requirements change or are updated, PSAA must consider the potential impact of each development on the fee scale. We need to consider whether additional fees are necessary, whether we can estimate the additional fees based on reliable evidence, and whether it is possible to incorporate the fees into the proposed fee scale in time for the consultation. We take a cautious approach to consolidating fees into the fee scale, to avoid the risk of over-estimating the additional requirement in the longer term.

25 Over the last two years we have commissioned external independent technical research to provide information, analysis and recommendations to support our work on updating the fee scale. This work has also provided helpful input to our fee variations reviews.

26 As we are required to consult on and publish the fee scale before audit work for the relevant year is undertaken, the research has focused on published changes in requirements, such as those set out in the Code of Audit Practice 2020 (the Code) and new or updated auditing and financial reporting standards. It has not included consideration of changes in regulatory expectations, as these typically arise from regulatory reviews carried out after audit work has been completed.

27 From an extensive list of changes and updates to the Code and relevant standards, the research has identified three that will have a significant enough impact to need additional fees for 2022/23 audits:

- the requirement for a VFM commentary, rather than a conclusion, in the Code of Audit Practice 2020, effective from 2020/21 audits;
- additional requirements in ISA (UK) 540 (revised) Auditing Accounting Estimates, effective from 2020/21 audits; and
- additional work needed under ISA (UK) 315 (revised) Identifying and assessing the risks of material misstatements, effective from 2022/23 audits.

28 The research has concluded that the impact on auditors' work of these changes is likely to be variable during the implementation years, depending on the local circumstances and arrangements of individual opted-in bodies. This makes it difficult to estimate a standardised fee with any certainty for all or most bodies.

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- 29 Given the complexity of the new requirements relating to the VFM commentary and ISA 540, we do not propose to consolidate additional fees for this work into the 2022/23 fee scale at this stage. Instead, we plan to use the fee variations process for a second year, for the 2021/22 audits, to evaluate the longer-term additional fees required for consolidation into a future fee scale.
- 30 For the 2020/21 audits, the first year of implementation, we published indicative minimum additional fee ranges to support discussions between opted-in bodies and auditors of the fees needed for this work. The fee ranges are set out below and will apply again for 2021/22 audits. We will consider consolidation into the 2023/24 fee scale when we consult in twelve months' time.

Minimum additional fees: new VFM commentary work for 2020/21 and 2021/22 audits¹

District council	County council	London borough council	Met council	Unitary	Police (PCC + CC combined)	Fire	Other LG bodies
£6,000-£11,000	£10,000-£19,000	£10,000-£19,000	£10,000-£19,000	£10,000-£19,000	£6,000-£11,000	£5,000-£9,000	Variable based on individual characteristics

¹ To be considered on an individual basis, but the general ranges may provide a useful reference

Minimum additional fees: ISA 540 work for 2020/21 and 2021/22 audits

Overall minimum additional fees								
The additional fees below depend on body type and individual circumstances and the fee variation required may be higher than the suggested minimum								
Approximate minimum additional fee by body type:								
District council	County council	London borough council	Met council	Unitary	Police (PCC + CC combined)	Fire	Pension fund	Other LG bodies
£2,500	£3,800	£4,400	£4,400	£4,400	£2,500	£1,900	£600-£1,900	Too variable to estimate

- 31 The revised ISA 315 applies from 2022/23 audits. Our research could not identify a consistent basis for estimating the additional fees needed at this stage. We therefore propose using the fee variations process to establish a realistic fee level for consolidation into a future fee scale.
- 32 There are some other developments which may affect the audit fees needed for 2022/23 audits, but specific requirements have not been confirmed or published yet:
- CIPFA/LASAAC has consulted on a possible approach to the basis for accounting for infrastructure assets, but further information on any changes to requirements was not available at the time of this consultation;
 - the Treasury is undertaking a review of non-investment asset valuation, which is due to report in autumn 2022; and
 - there may be a change in the threshold for Whole of Government Accounts, reducing the audit work required for some local government bodies.

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- 33 PSAA is unable to amend a fee scale once it is set. Therefore, where any changes to local audit requirements are clarified for 2022/23 audits following this consultation, they will need to be considered initially via the local fee variations process.

Inflation

- 34 Our contracts with audit suppliers provide for an increase for inflation for audit years 2021/22 and 2022/23 based on the annual March CPI rate, minus 1%.
- 35 No increase was required for the 2021/22 fee scale given the relatively stable position on inflation in 2021. However, for 2022/23 we need to increase the firms' remuneration by 5.2% based on the March 2022 CPI of 6.2%.
- 36 The total cost of the increase in remuneration for 2022/23 audits is £1.79 million. The options for funding this increase are either to use the surplus funds not required for PSAA's operations, which would otherwise be distributed to opted-in bodies, or to add the required increase to the 2022/23 fee scale.
- 37 We propose to fund the increase from our surplus, rather than making a separate distribution.

Summary of Proposal

- 38 In summary, we propose that the fee scale for 2022/23 will be built up as follows:

2022/23 fee scale: proposed elements
A. The fee scale set for 2021/22
Plus:
B. Fee variations for recurrent requirements in 2019/20 audits
C. Fee variations for recurrent requirements in 2020/21 audits
D. Adjustment for inflation
Additional fees needed for work relating to additional changes in auditing and financial reporting requirements will be determined using the fee variations process and considered for consolidation into a future fee scale

- 39 We will write to opted-in bodies during the consultation period to set out their expected scale fee based on these elements. We have set out below an example of how the scale fee will be made up:

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Example	Body Z
A. The fee scale set for 2021/22 Plus:	£30,000
B. Fee variations for recurrent requirements in 2019/20 audits (where received and approved and where different from the 2018/19 fee variations already consolidated into the 2021/22 fee scale)	£2,000
C. Fee variations for recurrent requirements in 2020/21 audits (where received and approved and where different from those consolidated for previous years)	£3,000
Subtotal	£35,000
D. Adjustment for inflation 5.2% (on scale fee and recurrent fees)	£1,820
Total scale fee for 2022/23	£36,820
PSAA funding of inflation (on scale fee and recurrent fees)	-£1,820
Fee to be paid by the opted-in body to the firm	£35,000

Statement of responsibilities

- 40 The [statement of responsibilities of auditors and audited bodies](#) sets out the expectations on which scale fees are based. The statement effectively represents the terms of engagement between appointed auditors and audited bodies and summarises their respective responsibilities. Scale fees are based on the expectation that audited bodies can provide the auditor with complete and materially accurate financial statements and supporting working papers within agreed timeframes. Local fee variations may be required where a body is unable to fulfil these requirements.
- 41 The statement of responsibilities also applies to auditors. Additional audit costs that arise due to auditors not meeting expectations in relation to their responsibilities are ineligible for a fee variation.

Value added tax

- 42 Individual audit fees under the 2022/23 fee scale do not include value added tax (VAT), which will be charged at the prevailing rate, currently 20 per cent, on all work done.

Next steps

- 43 We welcome comments from audited bodies and stakeholders on the proposals outlined in this document. The closing date for comments is Friday 30 September 2022.
- 44 Please send any questions on this consultation to: workandfeesconsultation@psaa.co.uk.
- 45 We will take account of responses to this consultation in setting the 2022/23 fee scale, for publication by 30 November 2022.
- 46 If you have comments about the way this consultation has been conducted, these should be sent by email to generalenquiries@psaa.co.uk.