

Consultation on scale of audit fees for 2018/19

Opted-in local government and police bodies

December 2017

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

In 2015 the Secretary of State for Communities and Local Government delegated a number of statutory functions (from the Audit Commission Act 1998) to PSAA on a transitional basis by way of a letter of delegation issued under powers contained in the Local Audit and Accountability Act 2014.

As a consequence of these delegations, for 2017/18 the company is responsible under transitional arrangements for appointing auditors to local government and police bodies and for setting audit fees.

In July 2016, the Secretary of State specified PSAA as an appointing person for principal local government authorities 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 scale fees for relevant principal authorities that have chosen to opt into its national scheme. This consultation relates to the first year of these new arrangements.

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Consultation on 2018/19 scale of fees

Introduction

- 1 This consultation document sets out the proposed scale of fees for the work to be undertaken by appointed auditors in respect of the 2018/19 financial statements at authorities that have opted into Public Sector Audit Appointments' (PSAA) national auditor appointment scheme.
- 2 The document also discusses PSAA's intentions, and provides indicative estimates, for scale fees for the five years of the appointing period, from 2018/19 to 2022/23. We plan to review and update our estimates each year during the appointing period, and will consult opted-in bodies and other stakeholders annually, before publishing confirmed scale fees on our website.
- 3 Scale fees are based on the expected work auditors will undertake under the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.
- 4 We hope the information set out in this consultation is helpful to opted-in authorities and other stakeholders in considering our proposals for the 2018/19 scale fees, as well as supporting audited bodies' longer-term financial planning.

Background

- 5 PSAA is specified under the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015 as the appointing person for principal local government bodies in England, including local police bodies.
- 6 PSAA's responsibilities include appointing auditors to opted-in bodies, setting fees, and monitoring the quality of auditors' work. More information about [PSAA](#) is available on our website.
- 7 At the time of issuing this consultation, there are 494 bodies eligible to opt into PSAA's national scheme, of which 484 (98%) have opted in for the current appointing period, covering the accounts for 2018/19 to 2022/23.

2018/19 scale fees

- 8 PSAA's approach to setting scale fees for the duration of the appointing period, and the specific proposals for scale fees for 2018/19, are set out in the remainder of this document.
- 9 PSAA operates on a not-for-profit basis. Fees are therefore set with a view to covering the amounts we need to pay to audit firms, following our auditor procurement exercise, and the expected operating costs of PSAA. Any surplus arising from the scale fees set following consultation will be distributed back to opted-in bodies during the appointing period.

Responding to this consultation

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

workandfeesconsultation@psaa.co.uk

The consultation will close on **Monday 15 January 2018**.

Approach to setting scale fees over the appointing period 2018/19 to 2022/23

10 We propose that scale fees for 2018/19 for all opted-in bodies should be reduced by 23 per cent, compared to the fees applicable for 2017/18. This proposal continues the practice of averaging firms' costs, so that all bodies benefit from the same proportionate savings irrespective of the firm appointed to a particular opted-in body.

11 This reduction is possible as a result of the favourable prices secured from firms in the recent audit services procurement. It follows a period from 2012/13 to 2017/18 in which scale fees reduced in two stages by an aggregate of 55 per cent, in part reflecting reductions in the size and scope of the Audit Commission, for example with the closure of its inspection services.

12 We hope to be able to maintain the reduction of 23 per cent in scale fees for the first three years of the appointing period, based on current assumptions about inflation and the amount of work auditors are required to undertake. We expect to be able to confirm this position when we review and update our assumptions and estimates each year, and consult on scale fees for the following year.

13 We may be able to sustain the 23 per cent reduction for the full five years of the appointing period, but it is not possible to be certain at this early stage. At present we are making cautious assumptions about the likely level of inflation during the appointing period (4 per cent per annum) having regard to the clear uncertainties and potential risks in the longer-term economic outlook.

14 Scale fees must cover both the cost of auditors' work at individual opted-in bodies and PSAA's own costs. PSAA is currently undertaking a significant review of its own costs and staffing structure, and implementing changes that will reduce the cost base for the appointing period.

15 The most significant factors that could have an impact on the level of scale fees required during the appointing period relate to:

- **Inflation:** there is uncertainty about the expected level of inflation but a generally rising trend. The contracts with audit firms include an increase for inflation in the later years of the appointing period.
- **Code of Audit Practice:** the National Audit Office is required to publish a new Code every five years. The next Code will be applicable from 2020/21, the third year of the appointing period. Any changes to the scope of auditors' work, whether this increases or decreases the work required, must be reflected in scale fees.
- **Changes in financial reporting requirements:** current scale fees reflect the audit work needed based on current financial reporting requirements. Changes to these requirements may have an impact on scale fees.

16 Previous consultations have suggested that audited bodies prefer fee stability, finding it helpful to have certainty about fee levels over as long a period as possible. We are making the proposed fee reduction of 23 per cent for 2018/19 with the intention of providing fee stability for subsequent years. We hope to maintain scale fees at this level for the first three

years of the appointing period, and possibly longer, subject to annual review and consultation.

17 We have considered the alternative approach of making a slightly larger one-off reduction in scale fees for 2018/19. This would provide the immediate benefit for opted-in bodies of maximising all the savings achieved in the procurement at the start of the appointing period, but would also involve greater financial risk.

18 A reduction of more than 23 per cent would not be sustainable over the subsequent years of the appointing period, and fee increases would be required each year to cover the costs of the firms and PSAA. We have therefore opted to base the proposed fee strategy for the appointing period on a significant scale fee reduction that provides a good prospect of fee stability over several years.

19 It is not PSAA's intention to generate and retain any surplus from scale fees. If any surplus arises, it will be distributed back to opted-in bodies (a similar distribution is being made in December 2017). The scale of any future distribution is likely to be modest at individual authority level. The company's current financial forecasts suggest that an average annual surplus equivalent to approximately 4 per cent of audit fees may arise and be available for distribution during the five-year appointing period.

20 **We welcome feedback from opted-in bodies in responses to the consultation on the approach we have taken to reducing fees.**

Proposed scale fees for 2018/19

21 The Local Audit (Appointing Person) Regulations 2015 (the Regulations) require PSAA to specify, before the start of the financial year to which the fees relate, the scale of fees for the audit of the accounts of opted-in authorities.

22 The proposed scale of fees for 2018/19 reflects the cost of the expected work programme outlined below, and is based on the scale of fees applicable for 2017/18 with a reduction of 23 per cent. The 2017/18 scale of fees represents the most accurate reflection available of the auditor's assessment of audit risk and complexity for each audited body.

23 The proposed scale fee for each opted-in local government and police audited body is [available on our website](#). Paragraphs 30 to 34 below explain the arrangements that apply to the variation of fees in certain circumstances.

24 The proposed scale audit fees for 2018/19 audits are based on the scale fees applicable for 2017/18, with a reduction of 23 per cent. The scale fees for 2017/18 provide the most accurate reflection available of the auditor's assessment of audit risk and complexity for each audited body.

Work programme

25 Under the provisions of the Local Audit and Accountability Act 2014 (the 2014 Act), the National Audit Office (NAO) is responsible for publishing the statutory [Code of Audit Practice](#) and guidance for auditors. Audits of the accounts for 2018/19 will be undertaken under this Code, on the basis of the scale fees set out in this consultation.

26 The Code requires the auditor to give an opinion on the financial statements of a body subject to audit under the 2014 Act, and a conclusion on the arrangements for value for money. Further information on the Code and guidance is available on the [NAO website](#).

27 Auditors tailor their work to reflect local circumstances and their assessment of audit risk. They do this by assessing the significant financial and operational risks facing an audited body, and the arrangements it has put in place to manage those risks.

28 The scale fees set out in this consultation are based on the assumption of no significant changes in NAO guidance for auditors, professional standards, or CIPFA/LASAAC financial reporting requirements that would affect materially the amount of audit work to be undertaken for 2018/19 audits. A previous example of such a material change in audit work was the implementation of international financial reporting standards (IFRS) for local government bodies for 2010/11.

Audit quality

29 PSAA is very aware of the need to maintain and, where possible, strive for improvements in audit quality. Our responsibilities in this area have been a major driver in our recent audit services procurement and are emphasised in the contracts we have entered into with successful firms. We are also developing new proposals for monitoring and reporting on audit quality once the new audit contracts are fully operational.

Fee variations

30 PSAA has the power to determine the fee above or below the scale fee, where it considers that substantially more or less work was required than envisaged by the scale fee. Scale fees are based on the expectation that audited bodies are able to provide the auditor with complete and materially accurate financial statements, with supporting working papers, within agreed timeframes.

31 Where it becomes clear that audit risk or complexity are significantly different from the level identified and reflected in the previous scale fee, the auditor may request a variation to the scale fee for 2018/19. We would only expect variations from the scale fee to occur for 2018/19 where these factors are significantly different from those identified and reflected in the 2017/18 scale fee.

32 Variation requests must be made to PSAA by the auditor using a standard process and cannot be invoiced to an audited body by the auditor until they have been approved by PSAA.

33 PSAA obtains updated fee information, and explanations for any proposed variations from the scale fee, from appointed auditors on a regular basis. We consider the reasonableness of the explanations provided by auditors, and require the auditor to confirm that they have discussed the reasons for the additional fee with the audited body before we finalise our decision on any variation to the scale fee.

34 PSAA will charge fees for considering objections from the point at which auditors accept an objection as valid, or any special investigations, such as those arising from disclosures under the Public Interest Disclosure Act 1998, as a variation to the scale fee.

Value added tax

35 All the 2018/19 fee scales exclude value added tax (VAT), which will be charged at the prevailing rate of 20 per cent on all work done.

Next steps

36 PSAA has a statutory duty to prescribe a scale of fees for the audit of accounts of bodies that have opted into its national auditor appointment arrangements. Before prescribing scale fees, we are required to consult opted-in authorities, representative associations of relevant authorities and bodies of accountants.

37 We welcome comments from audited bodies and stakeholders on the proposals contained in this document. The consultation will close on **Monday 15 January 2018**.

Please send comments by email to:

workandfeesconsultation@psaa.co.uk

38 Following responses to this consultation, the PSAA Board will approve the final 2018/19 scale of fees for publication in March 2018.

39 If you have comments or complaints about the way this consultation has been conducted, these should be sent by email to generalenquiries@psaa.co.uk.