

Consultation on the 2021/22 audit fee scale

Opted-in local government and police bodies

January 2021

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' 2021/22 financial statements and value for money arrangements.
- 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 have led the Government to commission a series of reviews into:
 - audit regulation (the Kingman Review);
 - the audit market (the Competition & Markets Authority Review);
 - the quality and effectiveness of audit (the Brydon Review);
 - local audit and financial reporting (the Redmond Review).
- 3 This consultation takes place against the backcloth of these reviews and in the context of the significant tensions and pressures currently present within the audit market and profession. It is carried out in accordance with the relevant provisions of the Appointing Person Regulations 2015, including the requirement to consult on and set the fee scale before the commencement of the relevant year. This imposes a very challenging timetable given that a great deal of information which would ideally be available to inform the setting of the scale is simply unavailable at this stage.
- 4 This consultation document explains how PSAA proposes to calculate the fees which will make up the 2021/22 fee scale. Our proposal involves two key variables: the ongoing implications of fee variations approved in relation to 2018/19 audit work, and the implications of further anticipated developments in relation to auditing and financial reporting standards. We explain in this document how we propose to tackle each of these issues and how we plan to communicate the detailed implications of each to individual bodies.
- 5 In theory, a third factor could also apply. Our contracts with audit suppliers include provision for an increase for inflation in relation to their remuneration for 2021/22. However, because the prevailing rate of inflation is currently low, it is unlikely that inflation will impact on 2021/22 fees payable by audited bodies.

Responding to the consultation

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

<https://www.surveymonkey.co.uk/r/X3WKBDH>

The consultation will close on **Friday 19 February 2021**.

Fee scale 2021/22

Background

- 6 As the appointing person for principal local authorities and police bodies, PSAA is required to undertake consultations before setting audit fee scales. This year's consultation, focusing on the fee scale in respect of the audit of 2021/22 financial statements and value for money arrangements, takes place in the context of significant turbulence and uncertainty in the audit market. Key developments include the fact that the future of local audit is in the process of being reshaped following the [Redmond Review](#) and the [Government's recently published policy response](#) to its findings and recommendations.
- 7 A significant proportion of audit work is undertaken after the relevant financial year by necessity. Consulting on changes to the fee scale in advance of the commencement of the relevant year (as the Appointing Person Regulations explicitly require) therefore presents us with significant challenges when audit is subject to as much change as it is currently. Ideally, we would be able to set fees with the benefit of relatively complete information about all preceding years' audits. In practice, we are having to consult on 2021/22 fees with incomplete information in relation to:
 - audits of 2018/19 accounts (a minority of audit opinions remain outstanding);
 - audits of 2019/20 accounts (a significant proportion of opinions remain outstanding)
 - audits of 2020/21 accounts (very limited if any audit work done).
- 8 Our position is therefore in essence comparable to a local body being required to set its budget with incomplete information about spending and revenues in preceding years, and with only theoretical information about the immediate prior year.
- 9 Helpfully the Government's policy response to the Redmond Review includes a commitment to review the Appointing Person Regulations. We are working with MHCLG to review and reform regulations to provide the appointing person with greater flexibility to ensure the recurring costs to audit firms of additional work are built into scale fees in a more timely, flexible and seamless way, subject to consultation. This could include enabling the appointing person to allow a fee scale to be set or changed in-year (subject to consultation with the auditor and the audited body), and/or enabling the appointing person (subject to appropriate consultation) to set additional fees across groupings of audited bodies in-year where there is clear evidence of additional work that affects those groupings. MHCLG has committed to consult in the coming months, with a view to having new regulations in place before summer recess.

Factors to be considered in setting the 2021/22 fee scale

- 10 In the context of the challenge of having incomplete information, we have considered a number of factors which have the potential to impact on 2021/22 audit fees, accepting that some cannot be fully quantified at this stage. They include:
 - i) [Approved fee variations which relate to audit work of an ongoing nature](#)
- 11 Auditors may find it necessary to carry out additional audit work in order to enable a safe audit opinion. The regulations allow for additional fees, calculated via our fee variations

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process, to be payable, subject to PSAA approval. In recent years the number of claims for additional fees has increased significantly, as auditors have needed to meet enhanced regulatory requirements following a number of controversial financial failures in the private sector.

- 12 Sometimes the additional audit work is of an ongoing nature, in which case it makes sense to update the relevant scale fee at the earliest opportunity to reflect the need for the audit work concerned in future years.
 - 13 In the 2021/22 fee scale we are therefore proposing to update as many individual fees as possible to consolidate the ongoing audit work identified in 2018/19 fee variations. We have reviewed all 2018/19 approved fee variations to establish the ongoing ones. These include, for example, ongoing elements of additional work on property valuations, pensions valuations and group accounts.
 - 14 As part of this consultation we will write to all individual opted-in bodies to explain the results of this work and the proposed change to the particular body's scale fee for 2021/22. 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 2018/19 that we have assessed as being of an ongoing nature (with the proposed impact on their 2021/22 scale fee);
 - bodies whose 2018/19 approved fee variations have not related to work of an ongoing nature (whose 2021/22 fees will be unaffected);
 - bodies which have not been subject to approved fee variations in 2018/19 (whose 2021/22 fees will be unaffected);
 - bodies for which claims for 2018/19 fee variations remain outstanding (whose scale fees may need to be updated subsequently).
 - 15 We plan to follow a similar process in respect of 2019/20 fee variations in the 2022/23 scale fees consultation in twelve months' time, or earlier if the Appointing Person Regulations are amended to allow us to update 2021/22 scale fees after the year has started (see paragraphs 3 and 9 above). When we update for 2019/20 fee variations, we will strip out any element which relates to 2018/19 that has already been consolidated – this will avoid any double counting.
 - 16 In this way we hope to ensure that all fees are systematically updated on a regular basis for any changing audit work requirements.
- ii) [Changes in auditing and financial reporting requirements](#)
- 17 We are aware of several scheduled changes to auditing and financial reporting requirements which may impact on the amount of audit work required to enable a safe audit opinion on 2021/22 accounts, and to deliver the requirements on the arrangements for securing value for money. The most significant anticipated developments include:
 - the [Code of Audit Practice](#) applicable from 2020/21, which contains new requirements in relation to reporting on value for money arrangements;

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- ISA 220 (Revised): Quality control of an audit of financial statements (applicable from 2020/21 audits);
 - ISA 540 (Revised): Auditing accounting estimates and related disclosures (applicable from 2020/21 audits);
 - ISA 600 (Revised): Specific considerations – audit of group financial statements (applicable from 2020/21 audits); and
 - IFRS 16 Leases (applicable from 2021/22 audits).
- 18** At this stage we have insufficient information to evaluate the impact of these developments in terms of additional audit work. We therefore propose to deal with these and any other similar developments via PSAA's new approach to fee variations which was subject to a recent separate consultation process.
- 19** The consultation on new fee variations arrangements sought the views of audited bodies and other stakeholders on proposals for PSAA to take a national lead on additional fees for new audit requirements where these are applicable to all or most audited bodies, removing the need for local negotiations. We received a good response to the consultation, with 97% of responses supporting our proposed new approach.
- 20** Under our new approach we intend to assess the additional work and consequent fee requirements for each new standard or requirement, taking account of the differing needs of particular types or groups of body. PSAA will consult on and determine national fee variations or expected fee ranges for different groups of bodies in relation to each relevant change or provide guidance on the factors to be considered. If it is possible to establish the additional costs and consult opted-in bodies on the outcome in time for inclusion in the 2021/22 fee scale, that is before 31 March 2021, PSAA will amend the fee scale accordingly. Where it is not possible to complete the assessment and consultation needed, the additional fees may be the subject of a national fee variation and will be incorporated into the fee scale at a later date.

iii) Inflation

- 21** Our contracts with audit suppliers include provision for an increase in their remuneration for inflation in respect of 2021/22 audits. However, the prevailing rate of inflation is currently low. We will review the position in March, but at this stage do not anticipate the need to adjust the fee scale for inflation as PSAA expects to be able to cover any contractual obligation from existing funds.

Summary of Proposal

- 22** In summary therefore we propose that the fee scale for 2021/22 will be built up as follows:

2020/21 scale fees

plus - relevant adjustments for ongoing additional audit work arising from 2018/19 approved fee variations (paragraphs 11 to 16 above);

plus – any adjustments relating to changes in auditing and financial reporting requirements which are classified as national variations under PSAA's new arrangements for dealing with fee variations and which are determined before 31 March 2021 (paragraphs 17 to 20 above);

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plus - any relevant adjustment for inflation arising from PSAA's contracts with audit suppliers (although at this stage it appears unlikely that the relevant provision will result in additional fees payable by audited bodies in respect of 2021/22) (paragraph 21 above).

Statement of responsibilities

- 23 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.
- 24 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

- 25 Individual audit fees under the 2021/22 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

- 26 We welcome comments from audited bodies and stakeholders on the proposals outlined in this document. The closing date for comments is Friday 19 February 2021.
- 27 Please send any questions on this consultation to: workandfeesconsultation@psaa.co.uk.
- 28 We will take account of responses to this consultation in setting the 2021/22 fee scale, for publication by 31 March 2021.
- 29 If you have comments about the way this consultation has been conducted, these should be sent by email to generalenquiries@psaa.co.uk.