

REPORT TO: Business Efficiency Board

DATE: 21 July 2020

REPORTING OFFICER: Operational Director – Finance

SUBJECT: Review of the External Audit Market and 2020/21 External Audit Fees

PORTFOLIO: Resources

WARD(S): Borough-wide

1.0 PURPOSE OF REPORT

1.1. The report outlines a review of the external audit market commission by Public Sector Audit Appointments Limited (PSAA) and also presents the Council's external audit scale fee for 2020/21.

2.0 RECOMMENDED: That

- 1) The outcomes of the review of the external audit market commissioned by Public Sector Audit Appointments Limited (PSAA), be noted; and**
- 2) The Council's external audit scale fee for 2020/21 of £81,076, be noted.**

3.0 BACKGROUND

3.1 The Local Audit and Accountability Act 2014 abolished the Audit Commission, following which the Council's external audit contract is now procured and managed by Public Sector Audit Appointments Limited (PSAA). PSAA is an independent, not-for-profit company limited by guarantee, established by the Local Government Association to procure and manage external audit contracts for nearly 500 councils.

3.2 The Council's contract with Grant Thornton for the provision of external audit services runs for five years until 31st March 2023.

3.3 Since the new contracts were let in 2018, there have been increasing concerns raised by the nine approved firms regarding the higher assurance levels which they are now required to provide by the audit regulators, compared with the resources they have available to undertake such work based upon the level of fees which can be charged. In addition, the National Audit Office has introduced a new Code of Audit Practice from 2020/21, which will further increase audit assurance requirements.

Review of the Sustainability of the External Audit Market

- 3.4 As a result of these concerns, PSAA commissioned a review of the sustainability of the external audit market and the prospects for any future audit procurement. The report presenting the outcomes of this review is shown in Appendix 1.
- 3.5 The review concluded that almost all of the approved firms have reservations about remaining in the external audit market. The report states that these reservations have arisen because fees have not risen to compensate for the higher risks that the firms perceive they face given higher assurance requirements and because the timing of local audits is now very problematic given the earlier 31 July deadline.
- 3.6 There is also a concern regarding the lack of partners, audit managers and lead auditors with local government experience, due to many having retired or left in recent years and with local external audit not being seen as attractive a career as corporate auditing.
- 3.7 A number of issues and options are identified from the review, for consideration by the PSAA in order to mitigate the risks to the sustainability of the external audit market and any future procurement.

2020/21 Audit Scale Fees

- 3.8 On 30 April 2020 the PSAA wrote to the Chair of the Business Efficiency Board and the Operational Director, Finance, to notify the Council of the 2020/21 external audit scale fees. A copy of the PSAA's letter is presented in Appendix 2.
- 3.9 The letter outlines the challenges facing the external audit market and current developments. It goes on to explain how the PSAA have set the external audit scale fees for 2020/21.
- 3.10 Halton's Scale Fee for 2020/21 will be £81,076 which is the same level as for 2019/20.
- 3.11 The PSAA letter highlights that with so much turbulence currently in the external audit environment, additional fee variations are likely to arise for most if not all audit bodies. Any variations in fees however, will be discussed with the Council at an early stage and are then required to be approved by the PSAA.
- 3.12 As a result of Covid19, MHCLG have acted to ease the pressures upon councils and external auditors, by temporarily revising the Accounts and Audit Regulations to relax the timescales for preparation and audit of the 2019/20 statement of accounts. The 2019/20 audited statement of accounts is now required to be published by 30 November 2020, rather than the previous 31 July 2020.

4.0 FINANCIAL IMPLICATIONS

- 4.1 The scale fee for Halton's external audit in 2020/21 will be £81,076 which is the same level as for 2019/20.

5.0 IMPLICATIONS FOR THE COUNCIL'S PRIORITIES

5.1 Children and Young People in Halton

None.

5.2 Employment, Learning and Skills in Halton

None.

5.3 A Healthy Halton

None.

5.4 A Safer Halton

None.

5.5 Halton's Urban Renewal

None.

6.0 RISK ANALYSIS

6.1 The provision of a robust external audit function is an important aspect of the Council's financial management, as high quality, independent audit is one of the cornerstones of public accountability, providing assurance that taxpayers' money has been well managed and properly expended.

7.0 EQUALITY AND DIVERSITY ISSUES

7.1 None

8.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

Document	Place of Inspection	Contact
Code of Audit Practice 2020	Halton Stadium, Widnes	Merv Murphy

APPENDIX 1

30 April 2020

By email

Email generalenquiries@psaa.co.uk

Dear Section 151 Officer and Audit Committee Chair

Fee Scale for the Audit 2020/21 and update on 2019/20

I am writing to notify you of your 2020/21 audit scale fee. In previous years your auditor has been required to write to you to do this. However, going forward, we have agreed with the audit firms that it is more efficient for PSAA to write out to all bodies directly.

PSAA commissions auditors to provide audits that are compliant with the National Audit Office's Code of Audit Practice ('the Code'). PSAA is required by s16 of the Local Audit (Appointing Person) Regulations 2015 (the Regulations) to set the scale fees by the start of the financial year, and we published the 2020/21 scale fees on our website on 31 March 2020. In addition to notifying you directly of your scale fee, this letter provides you with key updates and information on audit matters in these difficult times.

We wrote to all S151 officers on 12 December 2019 describing that local audit and audit more widely is subject to a great deal of turbulence with significant pressures on fees. These pressures still apply and the key aspects are summarised below;

- It is apparent that the well publicised challenges facing the auditing profession following a number of significant financial failures in the private sector have played a part. As you know, these high profile events have led the Government to commission three separate reviews - Sir John Kingman has reviewed audit regulation, the Competition and Markets Authority has reviewed the audit market, and Sir Donald Brydon has reviewed the audit product.
- It is not yet clear what the long term implications of these reviews will be. However, the immediate impact is clear - significantly greater pressure on firms to deliver higher quality audits by requiring auditors to demonstrate greater professional scepticism when carrying out their work across all sectors – and this includes local audit. This has resulted in auditors needing to exercise greater challenge to the areas where management makes judgements or relies upon advisers, for example, in relation to estimates and related assumptions within the accounts. As a result, audit firms have updated their work programmes and reinforced their internal processes and will continue to do so to enable them to meet the current expectations.

- **How we set your scale fee**

We consulted on the 2020/21 Scale of Fees in early 2020 and received a total of 54 responses. We published the final document on our website ([Scale fee document](#)). In it we explained that although we have set the scale audit fee at the same level as for 2019/20, we do not expect the final audit fee to remain at that level for most if not all bodies because of a variety of change factors, the impact of which cannot be accurately or reliably estimated at this stage.

The impact of these changes is likely to vary between bodies depending on local circumstances, and information to determine that impact with any certainty is not yet available. Our view is that it would also be inappropriate to apply a standard increase to all authorities given the differing impact of these changes between bodies. As the impact of these changes is understood, fee variations will need to be identified and agreed reflecting the impact on each audit

	Scale fee for the audit 2020/21	Scale fee for the audit 2019/20
Halton Borough Council	£81,076	£81,076

As well as the Scale of Fees document, we have also produced a [Q&A](#) which provides detailed responses to the questions raised as part of the consultation. We will update the Q&As periodically to take account of ongoing developments affecting scale fees.

The fee for the audit is based on certain assumptions and expectations which are set out in the [Statement of Responsibilities](#). This statement serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and of the audited body begin and end, and what is to be expected of both in certain areas.

The final fee for the audit will reflect the risk-based approach to audit planning as set out in the Code. Under the Code, auditors tailor their work to reflect local circumstances and their assessment of audit risk. This is achieved by assessing the significant financial and operational risks facing an audited body, and the arrangements it has put in place to manage those risks, as well as considering any changes affecting audit responsibilities or financial reporting standards.

Fee Variations

As noted above, we recognise that with so much turbulence and change in the local audit environment, additional fee variations are likely to arise for most if not all bodies.

The amount of work required on arrangements to secure VFM is a matter of auditor judgement and is based on the requirements set out in the new Code and supporting guidance which will be published later in 2020. Once the Auditor Guidance Notes have been published we will be able to consider the impact of the new requirements in more depth, and may be able to provide indicative ranges in relation to the likely fee implications for different types and classes of body.

Given that local circumstances at each audited body are key to determining the assessment of risk and the audit work required, we would encourage early dialogue with your auditor to determine any related implications for fees. The process for agreeing fee variations begins with local communication, and ideally agreement. We have produced a fee variation process note which is available on our website ([Fee variations process](#)). Please note that all fee variations are required to be approved by PSAA before they can be invoiced.

Quality of Audit Services

- We are committed to do all we can to ensure good quality audits and a high-quality service for the bodies that have opted into our arrangements. The service that you can expect to receive from your auditors is set out in their Method Statement, which is available from your auditors.
- Whilst professional regulation and contractual compliance are important components of the arrangements for a quality audit service, so too is the aspect of relationship management. We recently commissioned a survey via the LGA Research team to obtain audited bodies' views of the audit service provided to them. The themes and improvement areas from the survey will be discussed with firm contact partners for development at a local level. The results from our 2018/19 survey of all opted-in bodies will be available on our website in May and we will notify all S151 officers and Audit Committee Chairs.

Impact of COVID-19 on current 2019/20 audits

The global COVID-19 pandemic has created further turbulence impacting on all aspects of the economy including the public sector. There are potentially significant repercussions for the delivery of audits, audit-related issues and delays to signing audit opinions for 2019/20. MHCLG has acted to ease these pressures by providing more flexibility in the 2019/20 accounts preparation and auditing timetable by temporarily revising the Accounts and Audit Regulations. This has extended the period which an authority has to publish its draft financial statements until 31 August, and importantly there is much greater flexibility for the public inspection period as it is now required to start on or before the first working day of September 2020. The revised date for publishing audited accounts (if available) is 30 November 2020.

We recommend that you discuss with your auditors the use that can be made of this flexibility in meeting mutual governance and assurance responsibilities, noting that in a letter to all local authority Chief Executives on 22 April, MHCLG encouraged approval of pre-audit accounts earlier than 31 August if possible.

We have referred to the importance of audit quality in this letter, and just as important is the quality of the pre-audit financial statements and the working papers that are prepared by bodies. The disruption caused by COVID-19 will impact on areas of judgement and creates uncertainty in preparation of the financial statements, and it is key that bodies ensure there is sufficient focus upon financial reporting and related processes and controls, and that the planned timetable allows for sufficient internal quality assurance and review of financial reporting issues taking into account the wider impact of the pandemic on the officers' time.

Local Audit Quality Forum

Our Local Audit Quality Forum focuses on providing information to support audit committees (or equivalent) in delivering their remit effectively. We are disappointed that we are not able to host our planned event this summer due to the COVID-19 pandemic. However, we plan to host our next event towards the end of the year. It will provide an opportunity to discuss a range of relevant topics and themes. If there are any particular areas you would like to see included on a future agenda, or if you wish to raise any other issues with PSAA, please feel free to contact us at generalenquiries@psaa.co.uk

Your auditor will, of course, be best placed to answer any questions you may have with regard to your audit.

Yours sincerely,

Tony Crawley

Chief Executive