

Audit Scotland's fee setting strategy for public sector external audit in Scotland



Information paper for Comhairle Nan Eilean Siar's Audit & Scrutiny Committee 8
February 2024

Purpose of paper

1. This paper provides a summary of the fee setting strategy used by Audit Scotland's Audit Quality & Appointments team to set the fees for the external audit of public sector bodies whose auditors are appointed by the Accounts Commission (local government bodies) or the Auditor General (NHS, central government and further education bodies).
2. Comhairle nan Eilean Siar's Audit and Scrutiny Committee requested this information paper to aid members' understanding of this element of the Comhairle's expenditure.

Background

3. Audit Scotland's Audit Quality and Appointments team is responsible for the procurement of public sector external audit providers; each audit appointment round lasts for 5 years. The Audit Quality and Appointments team is also responsible for setting the level of fees charged to audited bodies. The fees cover the cost of delivering the external audit work set out in the [Code of Audit Practice](#). The main elements of this work are:
4. **Annual audits** are undertaken by Audit Scotland staff and private firms appointed by the Auditor General and the Accounts Commission.
5. **Performance audits** are carried out by Audit Scotland staff with assistance from external specialists and appointed auditors where appropriate.
6. **Best Value audit work** is carried out by appointed auditors of councils as part of the annual audit. Reports by the Controller of Audit to the Accounts Commission are prepared for each council at least once in each five-year audit appointment period.
7. Audit Scotland's work is funded by a combination of fees charged to audited bodies and resources provided by the Scottish Parliament. About three quarters of our income comes from fees.
8. The projected fees form part of Audit Scotland's budget proposal to the Scottish Commission for Public Audit which considers the proposal, takes evidence on it in public and reports to the Finance and Public Administration Committee of the Scottish Parliament as part of the overall scrutiny of the annual Budget Bill.

Fee strategy

9. In setting a fee strategy our aim is to provide high-quality independent public audit in Scotland while delivering best value in our work. This means the fee strategy needs to:
 - comply with statute
 - maintain the independence of Audit Scotland and its auditors

- reflect the way in which public services are organised and audited
 - be transparent, easy to understand and simple to operate
 - be sustainable and not volatile from year to year without reason.
10. The key principles of setting a fee for the audit are that: audit fees should be set with the objective of recovering the full cost of audit work in each sector; and the cost of the audit should not depend on the identity or location of the auditor.
11. Stakeholder consultation on the fee strategy was carried out prior to the previous audit appointment round (2016/17-2021/22). Respondents agreed with the principles of full cost recovery and that the audit fee should be the same whoever carried out the audit. They also agreed with the concept of cost pooling and the approaches to sharing these costs between bodies.
12. The tenders for the previous appointment round included a discount offered by the bidding firms. This reduced the cost of the audit and was reflected in the fee levels. A discount was not offered in the tenders for the current appointment round; the fees reflect the actual cost of audit provision.

Elements of the fee

13. The fee charged comprises the following elements, which are set out in the fee letter issued in December to each audited body:
- **Auditor remuneration:** the true cost of an auditor providing an audit; based on the average bid in the tender process for the 2022/23 to 2026/27 audit appointment.
 - **Pooled audit costs:** costs which would otherwise lead to different fees being charged depending on the identity or location of the appointed auditor (e.g. travel and subsistence costs). These pooled costs are distributed across the audited bodies in each sector in proportion to the expected level of auditor pay. For local government bodies pooled costs also include recoverable input VAT.
 - **Performance audit:** the cost of performance audits and briefings.
 - **Sectoral cap:** applied to prevent significant increases to fees for smaller bodies in each sector (e.g. from high inflation). Effectively subsidisation of smaller bodies by larger bodies within each sector.
 - **Audit support costs** represent the cost of the Audit Quality & Appointments team and the part of Audit Scotland that provides advice to all auditors including the firms. These costs are zero for all bodies this year (2023/24) because the costs are now directly funded by the Scottish Consolidated Fund. This change is one of the ways the Audit Quality & Appointments team has sought to contain fee increases.
14. The expected fee is set based on the expectation that an audited body has appropriate internal controls operating effectively throughout the year, has good governance arrangements, provides good quality accounts for audit together with a complete working papers package and sufficient capacity to support the audit process. Local auditors may increase the fee above the expected fee level if these expectations are not met.

15. Fees can be agreed between the auditor and audited body by varying the auditor remuneration by up to 10% above the level set (20% for smaller audited bodies), for example, where significant local issues require additional work to be undertaken. In exceptional circumstances higher remuneration can be agreed with the prior agreement of Audit Scotland.
16. The annual audit fee for Comhairle Nan Eilean Siar is agreed with management and set out in the Annual Audit Plan presented to the Audit & Scrutiny Committee. Any changes required to the fee during year are reported in the Annual Audit Report.

Further reading

17. The fee setting strategy "Our approach to setting audit fees" published in advance of the previous audit appointment round (2016/17 – 2021/22) remains relevant and is available on Audit Scotland's website here: https://www.audit-scotland.gov.uk/uploads/docs/um/audit_fee_approach.pdf
18. Further information on the regulatory expectations of local government auditors can be found [here](#) on the UK Parliament website. Although this applies to England, these expectations of the audit profession are recognised by audit providers operating across the UK.