

ICAS Response to:

# PSAA: Consultation on the draft prospectus for the national scheme for local auditor appointments from April 2023

8 July 2021



# Introduction

The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of chartered accountants and has a public interest remit. We represent over 22,000 members working across the UK and internationally. Our members work in the public and not for profit sectors, business and private practice. Approximately 10,000 of our members are based in Scotland and 10,000 in England.

ICAS has a Public Sector Panel consisting of senior members across the public sector, working for public sector organisations, their boards or as advisors and auditors. We welcome the opportunity to comment on this consultation and would be pleased to answer any questions on our responses.

Any enquiries should be addressed to [atelfer@icas.com](mailto:atelfer@icas.com) Head of Business Policy and Public Sector.

## Key points

We highlight the following key points:

1. The option to extend the five-year tenure by two years offers useful flexibility. It is appropriate to periodically assess and challenge what is an appropriate tenure period for achieving audit quality and auditor independence (both actual and perceived). It is also important to consider the potential costs (both financial and in terms of the efficiency and effectiveness of the audit) of rotating too frequently.
2. Fundamentally, effective governance in audited bodies is a key element to achieving audit quality. In particular, the roles and responsibilities of audited bodies to select the most appropriate auditor for their organisation need greater emphasis, whatever the auditor appointment framework. We believe that public bodies themselves should take a stronger interest and more active role in audit tendering and monitoring as part of achieving effective governance and achieving a high-quality audit.
3. We suggest that there would be benefit in the PSAA taking more of a leadership role in explaining and promoting the importance and benefits of a good quality audit to local bodies, the role of local bodies in achieving this and achieving mutual understanding of what to expect from a good working relationship to optimise the quality and value from audit.
4. We note that in general, the auditor registration process appears strongly focused on public sector experience which can reduce the supply of auditors. We encourage the PSAA to actively support market sustainability and choice through further engagement with the FRC.
5. Regarding the consultation process, we have made some observations on increasing transparency and inclusion in our response to question 8.

## Responses to the specific questions

**3. Is PSAA right to prioritise the awarding of new longer-term contracts with firms, based on realistic market bid prices, mitigating the risks of a less than fully successful procurement by holding in reserve the option to extend one or more of the existing audit services contracts for up to two years if required?**

See question 5 below.

**4. Is five years an appropriate term for bodies to sign up to scheme membership?**

See question 5 below.

**5. Is five years with the option to extend for up to two years subject to the supplier's agreement an appropriate term for the next audit services contracts?**

The option to extend the five-year tenure by two years offers useful flexibility. It is appropriate to periodically assess and challenge what is an appropriate tenure period for achieving audit quality and auditor independence (both actual and perceived). It is also important to consider the potential costs (both financial and in terms of the efficiency and effectiveness of the audit) of rotating too frequently. Costs are incurred not just by the audited body and appointed auditor but by all of the audit firms who tendered for the appointment.

We suggest that audit tenure should be reviewed more fundamentally to determine an optimum between quality and independence.

Whatever the auditor appointment model, we believe that public bodies themselves should take a stronger interest and more active role in audit tendering and monitoring as part of achieving effective governance and achieving a high-quality audit. For further information, please see our [public sector audit tendering guide](#).

**6. Is PSAA right to evaluate tender submissions on the basis of 80% quality and 20% price to align with market expectations and other recent public audit procurements?**

Tender evaluation of quality is critical. We agree that it is important to focus on quality first however there is a risk that the use of bands may be overly quantitative and risk becoming a tick-box exercise. We have received some feedback that despite the bandings, where competitive bidders meet the quality hurdles, the next stage in selection is based simply on price. It should be stressed that the final stages of selection should still focus primarily on quality (please see our [public sector audit tendering guide](#)).

Fundamentally, effective governance in audited bodies is a key element to achieving audit quality. In particular, the roles and responsibilities of audited bodies to ensure that the most appropriate auditor is selected for the organisation's needs greater emphasis. This applies whatever the appointment framework in place and includes undertaking regular monitoring and evaluation of their auditor to ensure quality and independence is upheld (see our [public body auditor evaluation guide](#)). This should include a mechanism to demonstrate openness to responding to challenge, if concerns exist.

We suggest that there would be benefit in the PSAA taking more of a leadership role in explaining and promoting the importance and benefits of a good quality audit to local bodies, the role of local bodies in achieving this and achieving mutual understanding of what to expect from a good working relationship (between the audit committee, finance director and his team, and the external auditors) with professional scepticism at the core. This is a pre-requisite for a high-quality audit. External audit performs a key role in supporting scrutiny and accountability. Please see our [public sector audit tendering guide](#) where we explain this further.

**7. Is PSAA right to seek to encourage market sustainability within the local audit market by accepting bids from firms that are currently proceeding through the local audit registration process; by accepting consortia bids which may involve an unregistered firm gaining experience by working alongside a registered firm; and by considering the inclusion of one or two lots specifically aimed at seeking to encourage additional capacity into the market?**

Yes, however we note that in general, the auditor registration process appears overly focused on public sector experience which can reduce the supply of auditors. We are not convinced that over-specialisation of auditors is necessary – a balance is needed.

In the interests of efficient and effective public audit, PSAA needs to actively support wider market sustainability. With reference to [question 9 in the supplier questionnaire](#), further engagement with the FRC is needed. More flexibility to allow a wider range of auditor experience to tender would benefit competition and may offer wider cross-sector insights and expertise that could benefit audited bodies.

**8. Is PSAA’s proposed approach to social value appropriate given the services to be procured will be delivered across the whole of England? Are there any alternative approaches that should be considered?**

Insufficient information was provided by this consultation for us, as an “other” stakeholder, to provide an informed view on this.

A policy of openness and transparency, including annual reporting by the PSAA on experience and progress is important for public accountability.

We stress that the PSAA needs to prioritise the principles of openness and transparency as a matter of public accountability. This includes:

- a) Applying good practice consultation standards (see further comment below)
- b) Providing high quality information on how the PSAA secures efficient and effective external audit of public funds as part of wider public reporting on the effectiveness, progress and continuous improvement of the audit appointments process.

Regarding this consultation process, we found the yes/ no approach for other stakeholders too restrictive for a consultation and offered limited opportunity to add other points beyond the set questions.

We strongly believe there is value in inviting comment from a wide range of stakeholders. However, we note that as an “other stakeholder” there are some questions where insufficient information was provided by the PSAA to enable an informed comment e.g. the question on social value. Normal good practice is to have a consultation paper providing an explanation and supporting evidence for the proposals and for the consultation questions to reference to this.

In our view it would be more transparent and inclusive to have one single consultation paper with the same information for a range of stakeholders rather than having separate surveys. This would better enable a holistic perspective of all the issues being considered.

**9. Is PSAA right to carry out research and to consider setting a minimum audit fee in the next appointing period, recognising the increasing level of audit work now required and the risk that smaller scale fees may not be sufficient to cover the actual cost of the audit? What would be the key issues for PSAA to consider in the event that it opts to set a minimum fee for a Code-compliant audit?**

It is important to identify and highlight the trade-off between cost and quality however this is a complex area. This needs to be addressed to ensure appropriate external audit assurance on the reporting of how public funds are applied, what has been achieved and also to sustain the audit market.

Whilst we understand the drive to protect audit quality by not having a price race to the bottom and also offering protection for audited bodies from excessive prices, introducing bands and a minimum fee risks being overly prescriptive and contrary to the fundamental economics of competition.

Fundamentally we would stress that reform should focus on the following:

- 1. A clear evidence basis identifying the need and options to effectively manage cost and audit quality trade-offs.

Further research evidence is required to identify what is needed, where (e.g. the type/ size of organisation) and how (e.g. what level of fee or if the audit model or funding model needs adapted) and how effective this would be. It should be possible to construct a detailed budget requirement for a range of small bodies to determine an expected fee (in normal conditions, and if the client meets all their responsibilities). Deviations can be discussed and challenged by the audit committee.

2. Ensuring that sufficient competition exists in the market is key – this should help erode the power of a small pool of suppliers quoting high fees over time.
3. Promoting responsibility of local bodies through education of those charged with governance and understanding of their responsibilities. This is critical so their focus is on selecting the most appropriate auditor for their organisation and being open to challenge if these duties are not being adhered to.

**10. In the context of the recent NAO report, should PSAA and other market participants strive to prioritise the timeliness of audit opinions in the next appointing period? What actions should PSAA or other market participants take in order to avoid delayed opinions blighting the next period?**

Yes, however the key point is a continuing focus on audit quality (recognising that there is a balance as the relevance of reporting and audit diminishes over time).

**11. Which specific benefits of the national scheme are valuable to you? Are there other benefits we should strive to develop?**

N/A

**12. What are the key issues which will influence your decision about scheme membership for the second appointing period?**

N/A

**13. To inform the further development of our procurement approach, please indicate whether or not you anticipate that your organisation is likely to opt into our scheme?**

N/A

##





**Contact us**

CA House, 21 Haymarket Yards, Edinburgh, UK, EH12 5BH

+44 (0) 131 347 0100

[connect@icas.com](mailto:connect@icas.com) | [icas.com](https://www.icas.com)

 @ICASaccounting  ICAS – The Professional Body of CAs