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Scottish Commission for Public Audit

Audit Scotland Budget Proposal for 2023-24



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Introduction

1. Section 11(9) of the Public Finance and Accountability (Scotland) Act 2000 requires that Audit Scotland prepares proposals for its use of resources and expenditure and sends these proposals to the Scottish Commission for Public Audit ("the Commission").¹ The Commission then examines the proposals and reports to the Parliament on them.
2. As Audit Scotland's budget forms part of the total Scottish budget, the Commission reports its views to the Parliament to assist Parliament's wider scrutiny of the overall Scottish Budget for 2023-24. Audit Scotland submitted its budget proposal for 2023-24 on 2 December 2022.²
3. The Commission took oral evidence on the budget proposal at its meeting on 14 December 2022 from: Professor Alan Alexander, Chair of the Board of Audit Scotland; Stephen Boyle, Auditor General for Scotland and Accountable Officer for Audit Scotland; Vicki Bibby, Chief Operating Officer, Martin Walker, Director, Corporate Support and Stuart Dennis, Corporate Finance Manager, Audit Scotland; and William Moyes, Chair of the Accounts Commission. We thank them for their evidence.³

Overview

4. The 2023-24 budget proposal explains that Audit Scotland—
 - ” ...is Scotland's national public sector audit agency which provides the Auditor General and the Accounts Commission with the services they need to carry out their duties.
5. Audit Scotland's budget is drawn from two main sources. These are fees charged to audited bodies and funding approved by the Scottish Parliament and which comes from the Scottish Consolidated Fund.
6. Audit Scotland's budget proposal for 2023-24 is based on a total expenditure of £34,993k. This represents an increase of £4,392k compared to its budget in 2022-23. This is comprised of:
 - £22,943k arising from fee income (£413k increase from 2022-23) and
 - £12,050k of Parliamentary approved funding which represents an increase of £563k from 2022-23.
7. In terms of the funding for which Parliamentary approval is sought, £12,050k is revenue funding and £150k is capital funding. Audit Scotland explains that the budget increase of £563k arises from:
 - increases in non-chargeable audit fees (new bodies and fee uplift), £449k
 - an increase in Accounts Commission support, £278k
 - an increase in performance audit, £101k
 - additional audit responsibilities arising from financial devolution to Scotland, £55k
 - the reduction in national fraud initiative, £220k
 - a reduction in capital, £100k
8. Audit Scotland explains that its budget proposal for 2023-24 will deliver:
 - assurance over the significant amount of public money being spent in Scotland
 - audit of 226 public bodies
 - independent evidence-based public reporting on how well public money is being used to:
 - rebuild the economy
 - repair the damage to communities
 - address inequalities and create a fairer, more just society
 - demonstrate good governance, transparency, financial management, fraud

prevention and long-term planning in public bodies

- further development of flexible and agile ways of working through enhancement of our digital and professional support capacity to ensure our audit reporting is keeping pace with the changes in public finances and services and in technological developments.

9. However, Audit Scotland notes that the budget has been prepared in the context of significant uncertainties which are listed below:

- the resources required to deliver public audit in Scotland to ensure a full recovery and development of a future hybrid operating model
- timing of budget statements from the UK and Scottish Governments
- economic downturn and impact on inflation/interest rates
- public sector pay policy challenges
- future digital and climate change audit requirements
- the cost and availability of goods/services
- financial assumptions used to estimate International Accounting Standard 19(IAS19) defined benefit pension costs.

10. The Auditor General for Scotland (and Accountable Officer), hereafter referred to as the AGS, explained that—

” over the past two years the scope and scale of our responsibilities have grown at a rate not seen since we were established back in 2000. Public spending in Scotland has increased by about a fifth and public bodies are and remain stretched to an extent similarly not seen. Although the pandemic has ebbed, public bodies had neither the time nor the space that they needed before further challenges unfolded.⁴

Increase in Accounts Commission support

11. Audit Scotland's budget proposal for 2023-24 includes an increase in Parliamentary approved funding of £563k, almost half of which arises from a £278k increase in the cost of support to the Accounts Commission.
12. When asked for an explanation of the reasons for this significant increase in costs directly attributable to the Accounts Commission, its Chair explained that on his appointment-
 - ” the Minister made clear to me that he was happy with the audit of local government, but he was not happy with the Commission's impact. He wanted us to make much more impact than we were making. ⁵
13. The Chair of the Accounts Commission went on to add-
 - ” The objective that has been set for the Commission is to go and make more impact and make sure that there are no serious problems in local authorities that we are not hitting. In our view, that meant that we had to increase our profile with the Parliament and that we had to be able to demonstrate that our work is having a lasting impact on service quality. To do that, we needed more dedicated resource. At that stage, two or maybe three members of staff of Audit Scotland were dedicated to supporting the Accounts Commission. ⁵
14. The Chair of the Accounts Commission clarified that of the increased £278k costs to support the Accounts Commission, £155k was attributable to the costs of the creation of a full-time Controller of Audit post and a further £65k was associated with creating analytical posts to work within the Accounts Commission's small secretariat team. He also clarified that some of the funding was required "to improve our website, because it is tangled up with Audit Scotland's website". ⁶
15. The Members of the Commission felt that the explanations provided at the meeting were not sufficiently detailed or 'fleshed out' and therefore, were not convinced by the explanation provided for these increased costs. The Commission wrote seeking further information from Audit Scotland, specifically around the drivers that led to the need for the change programme currently being carried out by the Accounts Commission. It also sought further information regarding the creation of a full-time post of Controller of Audit (a post that had previously existed as a part-time role, alongside the duties of the Executive Director of Performance and Best Value), along with information on the discussions that had taken place between the Accounts Commission and the Minister for Social Security and Local Government. ⁷
16. The Commission was also keen to learn more about the evaluation and assessments undertaken which identified the need for more staff for analytical work, stakeholder engagement and providing a refreshed website and how this related to the increase in the overall budget figure of £278k.
17. The Commission received two letters in response, one from the Chair of Audit

Scotland and the Auditor General for Scotland and a separate letter from the Chair of the Accounts Commission.

18. Audit Scotland explained in its letter that "We have agreed with the Chair of the Accounts Commission that he will write to you separately" as "The Accounts Commission was clear with Audit Scotland during 2022 that it required the creation of a stand-alone Controller of Audit to better discharge its responsibilities." ⁸
19. The additional information from the Chair of the Accounts Commission was helpful in clarifying what involvement the Minister for Social Security and Local Government had in setting the direction of the work of the Accounts Commission. In his letter, the Chair of the Accounts Commission reconfirmed that during his introductory meeting with the Minister on 2 February 2022, he expressed the opinion that "the [Accounts] Commission could make more impact than it was currently doing". ⁹
20. The Commission sought an explanation for the creation of the stand-alone post of Controller of Audit before funding had been secured (noting that an appointment to the post has already been made with the candidate taking up the role early in 2023). In his letter, the Chair of the Accounts Commission points to provisions in the Local Government (Scotland) Act 1973 giving the Commission power to "incur such expenses as appear to them to be necessary or expedient for the proper discharge of their functions, and such expenses shall be met by Audit Scotland." The Commission notes that Audit Scotland met the cost of the position last year from contingencies. ⁹
21. Having considered the information and explanations provided in the letter, the Commission is broadly content that due process around the creation of the full-time post of Controller of Audit has been followed.
22. In respect of the decision to institute the change programme, the Chair of the Accounts Commission explained in his letter that this was "prompted by my initial observations as incoming Chair and the dissatisfaction of most Commissioners with the organisation's performance and profile". He went on to give three examples to illustrate the Accounts Commission's concerns:
 - stakeholders in local government and the Parliament frequently refer erroneously to reports by the Accounts Commission as "Audit Scotland reports".
 - there are members of the Scottish Government at Cabinet level, and senior officials, whose comments suggest that they are largely unaware of the existence of the Accounts Commission and of its role and responsibilities, and believe that the scrutiny of Scottish local government is a matter for the Auditor General.
 - MSPs and the news media have recently referred concerns about certain local authorities to the Auditor General, apparently not realising that he has no locus in relation to local authorities. ⁹
23. The Accounts Commission, the Chair explains in his letter, seeks much better

recognition of its role and also wants "to build convincing evidence that local authorities are adopting the Commission's recommendations in audit reports, overview reports, briefings etc. and that these are having a demonstrable effect on the cost and quality of local services." ⁹

24. The Commission recognises that the public sector landscape can sometimes be confusing and, therefore, is not unsympathetic to some of the issues raised by the Chair of the Accounts Commission regarding the visibility of the organisation. However, the Commission still finds difficulty in reconciling the need for a full-time post (as identified by the Accounts Commission change programme and the supporting programme of work) with the evidence provided by the Chair of the Accounts Commission. Although more details were provided in written evidence, the Commission remains unconvinced by the rationale for the work, the full-time nature of the post of Controller of Audit and the budget increase to support this.

25. The Commission is also mindful that the budget proposal comes at a time when higher inflation, interest rates, and the cost-of-living crisis have impacted on many areas of public finances, as well as on households and businesses. The Scottish Fiscal Commission judges that Scotland is already in recession and forecasts that this year will see the biggest fall in living standards since Scottish records began in 1998.

26. It is even more difficult, within these current financial circumstances, where budgets are being tightly drawn, for the Commission to be satisfied that the business case for the post or the underpinning work, for example on stakeholder engagement and a website, has been fully made or explained.

Audit costs

27. Audit Scotland's budget proposal sets out that the increased cost of delivering a high-quality audit has in turn led to an increase in the fees and expenses that it is required to pay to external firms who undertake audit work on its behalf. This, in turn, has led to an increase in the fees that it requires to charge to audited bodies in order to 'break even'.
28. Audit Scotland has recently completed a procurement exercise to appoint firms to deliver public audit in Scotland for the next five years. The budget proposal states that the appointments have been made and payments to the firms are based on the bids they submitted as part of the tendering exercise.²

Fees and expenses paid to external audit firms

29. The budget proposal states that the fees payable to the professional external audit firms that support it in delivering its audit work will increase by £2,550k (56%) from £4,520k in 2022-23 to £7,000k in 2023-24. In its budget proposal, Audit Scotland describes the reason for this substantial increase as being due to the previous rates paid to firms being unsustainable. The budget proposal states that-

” ...the price reductions secured in the last two appointment rounds were not sustainable and as expected the cost of delivering a fully compliant high-quality audit has increased. Factors that have influenced the increase since the last appointment process include the additional scrutiny and risk evidenced in reviews of the external audit market and also increased regulation.²
30. The budget proposal also states that the market research Audit Scotland has undertaken offers assurance that the increased costs of private firms are a fair representation of current external audit market conditions.
31. The Commission sought further information from Audit Scotland on the additional standards and scrutiny that have driven the increase in costs.¹⁰
32. The Commission also queried whether consideration had been given to the delivery of audits, in particular the costs and benefits of having the audit work undertaken by in-house teams instead of external firms. The AGS explained that work has previously been undertaken to consider this issue and that-

” ...the Audit Scotland board weighed up the cost benefit of that question and came to the position that operating a mixed market in Scotland gave us the best balance of efficiency, access to expertise and predictability in the delivery of services.¹¹
33. Audit Scotland, in its letter of 20 December 2022, drew attention to the increased regulatory expectations and risk that led to the increase in costs that is being seen throughout the private and public sector audit market and across all sectors. It explained that there are increasing expectations of the audit profession and the quality of its work, especially around valuations for pensions, property, plant and equipment. The letter also explains that the respective fees proposed by the audit

firms were largely all consistent in terms of costs and were also consistent with an Audit Scotland in-house costing and benchmarking exercise.

34. The Commission notes the explanation for the increase in fees and expenses paid to external audit firms to undertake audit work on behalf of Audit Scotland.

Fees charged to audited bodies

35. Audit Scotland is required to directly charge certain audited bodies and relies on the Parliament to fund audit work for those bodies which it cannot bill directly. Its budget proposal states that it requires to increase fees to audited bodies by 19.4% and is seeking an increase of 4.8% resource from the Parliament to meet the cost of non-chargeable audits.

36. The budget proposal states-

” The fee rise was expected as we looked to secure the appointment of auditors for the next five years. The audit profession continues to experience considerable scrutiny, demand and risk in delivering a high-quality compliant audit.²

37. The Commission sought an explanation for the significant differences in the two increases along with assurances that non-chargeable audited bodies are not being cross-subsidised by those bodies who are billed for their audit work.

38. The AGS explained that-

” ...where Audit Scotland can charge a fee, it must charge on a sectoral basis and we have to break even on that basis. That is reflected in the variation by sector that we have as a result of market testing. We do not want to cross-subsidise by sector and the submissions that we received from the firms reflect both the variation and difference.

39. The AGS also stated that the new audit appointments offer price certainty for audited bodies for the next five years.

40. The Commission also sought an explanation for the variation across sectors in fee uplifts, in particular in relation to the further education section where the average fee increase is 57.5%. The AGS explained that-

” Historically, auditors of further education colleges have not broken even, given what it costs to deliver a standards-compliant audit and to meet the requirements of the code of audit practice that is set by the Auditor General and the Accounts Commission. That is coupled with the fact that, in the previous procurement round, audit firms gave significant discounts on the cost of delivering audits for all the reasons that we spoke about, such as the increasing costs relating to pay and other services. That has led to the costs for some sectors being significantly higher than the prevailing rate of inflation. There is therefore a variety of factors.¹²

41. In its letter of 20 December 2022, Audit Scotland explained that the fees it charges audited bodies are informed by the outcome of the procurement process to appoint external audit firms. It explains that the increase in fees is most acute in the further education sector due to the size of the organisations and the baseline cost required to deliver a code compliant audit (i.e. with the code of audit practice). With regards to the fees charged to colleges, the letter states-

” It is important to note that the percentage change is significant, but the change is less significant in absolute terms. The smallest increase is £8,810 and the largest £25,990. The average fee for an FE organisation under the previous audit appointment was £26,989. Under the new appointment this has risen to £42,506. The minimum FE audit fee is £24,140 and the maximum audit fee is £71,190.⁸

42. The Commission notes the explanation for the increases in the fees charged to audited bodies, in particular the fees charged to the further education sector.

Conclusion

43. Under the provisions of the Public Finance and Accountability (Scotland) Act 2000, the Commission is required to "examine the proposals [from Audit Scotland] and report to the Parliament" on them.
44. The budget proposal for 2023-24 from Audit Scotland is based on a total expenditure of £34,993k. This proposed expenditure includes £12,050k of Parliamentary-approved funding which represents an increase of £563k from 2022-23. Audit Scotland explains that a part of that increase of £563k is a sum of £278k, allocated against "Accounts Commission support".
45. The Commission is not required to approve the budget proposal from Audit Scotland but on previous occasions it has recommended approval of the proposals to the Parliament as part of the Budget (Scotland) Bill process.
46. On this occasion, the Commission reports to the Parliament that, while it is satisfied with the rationale behind much of Audit Scotland's budget proposal for 2023-24 and the increase sought over last financial year (relating to £285,000 of the overall requested increase), it draws the Parliament's attention to its serious concerns around the insufficient detail relating to the work described in the proposal as an "increase arising from...Accounts Commission support" amounting to £278,000.

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