



# Haverling

LONDON BOROUGH

## AUDIT COMMITTEE AGENDA

**7.30 pm**

**Monday  
16 May 2011**

**Committee Room 3A -  
Town Hall**

Members 6: Quorum 3

**COUNCILLORS:**

**Conservative Group  
( 4)**

**Residents' Group  
( 1)**

**Labour Group  
( 1)**

**Independent  
Residents' Group  
( 0)**

Georgina Galpin  
(Chairman)

Osman Dervish  
(Vice-Chair)

Roger Ramsey  
Frederick Thompson

Clarence Barrett

Paul McGeary

**For information about the meeting please contact:**

**James Goodwin 01708 432432  
james.goodwin@haverling.gov.uk**

## **AGENDA ITEMS**

### **1 CHAIRMAN'S ANNOUNCEMENT**

The Chairman will announce details of the arrangements in case of fire or other events that might require the meeting room or building's evacuation.

### **2 APOLOGIES FOR ABSENCE AND ANNOUNCEMENT OF SUBSTITUTE MEMBERS**

(if any) – received

### **3 DECLARATION OF INTERESTS**

Members are invited to declare any interests in any of the items on the agenda at this point of the meeting. Members may still declare an interest in any item at any time prior to the consideration of the matter.

### **4 MINUTES OF THE MEETING**

To approve as correct the minutes of the meeting held on 15 March 2011 and authorise the Chairman to sign them.

### **5 UPDATE ON OBJECTION TO ACCOUNTS ACTION PLAN (Pages 1 - 8)**

Report attached

### **6 PRIVATE SECTOR LEASED ACCOMMODATION (PSL) (Pages 9 - 14)**

Report attached.

### **7 EXTERNAL AUDIT FEES 2011/12 (Pages 15 - 22)**

Report attached.

### **8 INTERNAL AUDIT PROGRESS REPORT Q4 (Pages 23 - 50)**

Report attached.

### **9 ANNUAL FRAUD REVIEW (Pages 51 - 68)**

Report attached.

**10 FRAUD PROGRESS REPORT** (Pages 69 - 82)

Report attached.

**11 ANNUAL REVIEW OF THE COUNCIL'S WHISTLEBLOWING ARRANGEMENTS**  
(Pages 83 - 86)

Report attached.

**12 ANNUAL REPORT** (Pages 87 - 98)

Report attached.

**13 FUTURE OF PUBLIC AUDIT - GOVERNMENT CONSULTATION** (Pages 99 - 180)

Attached is a copy of the report submitted to the Governance Committee.

**14 URGENT BUSINESS**

To consider any other item in respect of which the Chairman is of the opinion, by reason of special circumstances which shall be specified in the minutes that the item should be considered at the meeting as a matter of urgency.

**15 EXCLUSION OF THE PUBLIC**

To consider whether the public should now be excluded from the remainder of the meeting on the grounds that it is likely that, in view of the nature of the business to be transacted or the nature of the proceedings, if members of the public were present during those items there would be disclosure to them of exempt information within the meaning of paragraph 3 of Schedule 12A to the Local Government Act 1972; and, if it is decided to exclude the public on those grounds, the Committee to resolve accordingly on the motion of the Chairman.

**Ian Buckmaster  
Committee Administration &  
Member Support Manager**

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**MINUTES OF A MEETING OF THE  
AUDIT COMMITTEE  
Havering Town Hall  
1 March 2011 (7.30pm – 9.05pm)**

**Present:**

**COUNCILLORS:**

**Conservative Group** Georgina Galpin (Chairman), Osman Dervish, Roger Ramsey and Frederick Thompson

**Residents' Group** Clarence Barrett

An apology for absence was received from Councillor Paul McGeary.

All decisions were taken unanimously with no votes against unless shown otherwise.

The Chairman advised the Committee of action to be taken in the event of emergency evacuation of the Town Hall becoming necessary.

There were no declarations of interest.

**23. MINUTES**

The minutes of the meeting held on 7 December 2010 were agreed as a correct record and signed by the Chairman.

**24. UPDATE ON OBJECTION TO ACCOUNTS ACTION PLAN**

The external auditors PricewaterhouseCoopers (PwC) informed the Committee that the objector who had submitted an objection to the 2009 accounts had submitted a similar objection to the 2010 accounts.

Officers advised the Committee of progress to date in responding to the objection and the recommendations of the External Auditors. The objector had appealed to the Leasehold Valuation Tribunal of the London Rent Assessment Panel on the basis that the charge being levied for the provision of television signalling was unreasonable. He had been successful in his appeal with a charge per annum being fixed for 2008/9 and 2009/10. Officers felt this was an unreasonable decision and were seeking leave to appeal.

The Committee were advised that the objector had claimed that an upgrade of the system to digital in 2001 never took place. This was challenged by the Council and investigations were on-going.

**Audit Committee, 1 March 2011**

Officers informed the Committee that negotiations were proceeding with Surtees in respect of the value for money aspects of the contract. Surtees had already agreed to cease charging separately for the two points in the same property. They had also agreed to forego any charges in respect of the Mardyke Estate. This should lead to savings of £150,000 pa.

Officers were exploring ways of breaking apart the contract which included both door entry and TV aerial/satellite installation.

PwC indicated that they were satisfied with the Council's progress in responding to the recommendations.

The Committee **noted** the report and requested a written up date at the next and future meetings until the matter was finally resolved.

**25. AUDIT OF PRIVATE SECTOR LEASING**

At the last meeting the Committee had considered an Internal Audit report on the work of the Private Sector Leasing Team. The Committee had expressed concern that the audit had identified 228 former tenant arrears, amounting to £487,109, which were not being currently investigated or pursued and had asked for additional information to be presented at this meeting.

Officers reported that as at period 10, 248 former tenant arrears had been identified totalling approximately £504,000. Steps had been taken to identify those debts where there was no prospect of recovery. In these circumstances the debt would be written off. As a result £58,000 of debt had been written off from 2 tenants who were deceased and 7 others where there was no contact. 59 tenants with low level debt had been identified, i.e. those with one week's arrears.

Officers informed the Committee that Homes in Havering had been asked to come up with a programme of recovery. Twelve debt collection agencies had been approached to ascertain if they would be interested in a contract to collect the arrears and none had shown any interest. A full time officer had been appointed on a six month contract to tackle the problem of long term arrears. Sixty cases had now been passed to legal services for action.

Nine tenants were on repayment plans which would eventually recover £27,700. A further 103 tenants with arrears of £240,000 were awaiting action.

The Committee were informed that as part of the restructure staff in the Private Sector Leasing Team were being reduced from 8.5 FTE posts to 7.5 FTE posts. Management needed to ensure staff's work was closely directed to achieve the right results. Officers explained that previously the focus of the Team had been driven by service delivery issues i.e. finding accommodation and dealing with the management issues which arose. Under the new arrangements one day a week would be focussed on arrears collection but as a result there would be less frequent property inspections.

**Audit Committee, 1 March 2011**

Early last year, an officer had been appointed on a short-term contract (for 6 weeks) to tackle the current level of arrears. This had resulted in the collection of £50,000 from the current arrears.

Officers stated that they believed that the current activities should make a significant in-road in to the problem but warned that seeking possession in the current economic climate could prove difficult.

The Committee **noted** the report and asked that a further written report be submitted to the next meeting providing details of the current level of total debt and how this is made up. The report should also indicate the age of the debts.

**26. EXTERNAL AUDIT INTERIM REPORT**

PwC informed the Committee that they were on site completing field work. The audit was substantially complete and they were pleased with the quality of the paperwork. They indicated there were no major surprises.

The Committee **noted** the report.

**27. EXTERNAL AUDIT ANNUAL PLAN 2010/11**

The Audit Plan submitted by PwC indicated the risks which would be assessed as part of the audit. These included the following significant risks:

- Revenue and expenditure recognition (standard risk)
- Fraud and Management Override of controls (standard risk)
- 2010/11 – the first year of reporting under International Financial Reporting Standards (IFRS),
- Leases, IFRS required building and land elements of leases to be analysed separately,
- Accruals for Employee Benefits.

Other risks included under the plan were;

- Increased pressures on budgets (common to all local authorities)
- Accounting for fixed assets
- Valuation
- Subsequent expenditure
- Assets under construction, and
- Assets held for sale.

Officers advised the Committee that the Council's own audit plan would complement the PwC work especially around system reviews. This would ensure the audit proceeded smoothly.

PwC indicated that for planning purposes, their overall materiality for the authority was estimated as 2% of gross expenditure in 2009/10. Similarly they proposed to treat misstatements of less than £250k as being clearly trivial. However, should a

pattern of misstatements emerge they would be investigated.

The Committee questioned the cost of the audit. PwC advised that the Council were classed as medium risk and this was reflected in the fee. PwC indicated that next year the Council should see a 10% reduction in the fee with a further reduction expected in 2012/13.

The Committee **noted** the report.

## 28. HOUSING AND COUNCIL TAX BENEFIT FRAUD UPDATE

The Committee received a report on the work of the Benefit Investigation Section during the period 1 April 2010 to 30 September 2010. Officers informed the Committee that in this period there were 20,665 claims for housing or council tax benefit, an increase of 893 when compared to the similar period last year. This could be attributed to the national economic climate.

During the period the Benefits Investigation Team received 334 referrals, an increase of 19 over the same period last year. The number of successful sanctions had increased from the same period last year:

	Qtr 1 & 2 10/11	Qtr 1 & 2 09/10
Administrative Penalties	18	11
Cautions	22	21
Prosecutions	22	8

The largest increase in prosecutions arose from the category "Living Together". Previously it had been difficult to prove fraud in court but a good working relationship between the Metropolitan Police and the Benefit Investigation Section had given rise to great success in this area.

Officers reported that the BBC had filmed the Benefit Investigation Section on two occasions for the documentary series 'Saints and Sinners.' Details of successful prosecutions were provided for the Committees information.

In 2009 the Council had agreed to carry out a review of single person discounts. A specialist company had been employed to carry out the initial work which had identified 5,652 cases which warranted further investigation. The position as at 31 January 2011 was as follows:



<b>Single Person Discount Initiative</b>	
Cases under review with Datatank	52
Non returns	222
Cases under investigation	170
Number of Single Person Discounts withdrawn	598
Value of Discounts withdrawn	£332,105.30

The Committee were also advised that a corporate initiative to review local authority tenancy fraud had been commenced. Working in partnership with Internal Audit and Homes in Havering a pilot of 40 cases had been investigated. This had resulted in two properties being returned to Homes in Havering with two more properties in the process of recovery.

Officers informed the Committee that an accredited Financial Investigations Officer had been recruited. This enabled the Council to seize the assets of people convicted of offences against the Council by use of the Proceeds of Crime Act 2002. Two investigations were in progress.

The Committee **noted** the report and congratulated officers on the good work. They also asked that in future they be provided with details of the amounts recovered following successful sanctions.

## **29. INTERNAL AUDIT PROGRESS REPORT**

The Internal Audit & Corporate Risk Manager submitted her quarterly report for the period ended 31 December 2010. During this period the Audit Team had completed three system audits, all of which were unqualified and none of which merited high recommendations.

The Committee were reminded that Schools Audit work had been brought back in-house last year with the programme starting in October. Three audits had been completed as at 31 January 2011. All had received either a full or substantial opinion. Officers advised that feedback from the schools had been very positive.

As requested at the last meeting (Minute no. 18 – 7 December 2010) officers had undertaken a review of all outstanding Recommendations. The Committee commended officers for the work undertaken to complete the review and were satisfied that they now had a much clearer picture.

The Committee **noted** the report.

### **30. REVIEW OF INTERNAL AUDIT CHARTER AND TERMS OF REFERENCE**

Officers submitted a report which reviewed the role of the Committee against best practice guidance issued by the Chartered Institute of Public Finance. An amended version of the Charter and Terms of Reference had been circulated with the agenda. There were minor changes to the Charter and the Committee **APPROVED** the updated Internal Audit Charter and Terms of Reference.

### **31. ANNUAL REVIEW OF AUDIT COMMITTEE EFFECTIVENESS**

The Committee considered a report which reviewed the role of the Audit Committee against best practice guidance issued by the Chartered Institute of Public Finance (CIPFA). A self assessment checklist had been produced by CIPFA, this had been undertaken by the Chairman of the Committee with assistance from the Interim Internal Audit and Corporate Risk Manager.

Officers advised that as a result of the assessment four areas had been highlighted for improvement in the Effectiveness Improvement Plan, these were:

1. Terms and reference should be agreed that cover the roles and responsibilities of the Audit Committee that were separate from the constitution;
2. A skills and knowledge assessment needs to be conducted to inform future training needs for the committee;
3. The Terms of Reference need to set out the frequency of meetings; and
4. A mechanism needed to be established for members of the committee to receive circulars and updates.

The Committee **noted** the report and **approved** the Effectiveness Improvement Plan as set out above.

### **32. INTERNAL AUDIT DRAFT STRATEGY AND PLAN FOR 2011/12**

In accordance with the Internal Audit Charter and Terms of Reference officers had submitted their proposed Strategy and Audit Plan for the forthcoming year. Officers informed the Committee that the proposed Audit Strategy for 2011/12 had been drafted following reference to best practice guidance provided by CIPFA. There were minimal changes needed to the strategy adopted last year.

**Audit Committee, 1 March 2011**

The Committee were also provided with details of the Audit Plan for 2011/12 which had been derived by reviewing and updating the Strategic Audit Plan and the list of key systems/areas of risk. Both the Corporate and Service Risk Registers had been considered.

Having considered the report the Committee:

- **Approved** the Internal Audit Strategy 2011/12 as submitted;
- **Approved** the Audit Plan 2011/12 as submitted; and
- **Noted** that any required changes to the Audit Plan arising during the financial year, as considered necessary by the Internal Audit and Corporate Risk Manager.

**33. 2009/10 AUDIT REPORT OF GRANT CLAIMS AND RETURNS**

The Committee received a report on the grants which required certification in 2009/10. All grants over £125k required certification and similar to last year this related to 10 claims. All had been certified although similar to last year 4 had been amended. A further claim had been qualified, similar to last year. This was the claim in respect of Housing Benefits and Council Tax.

PwC advised that their initial check had revealed 9 claims with errors resulting in the council overpaying benefits totalling £179.49, the largest error being £130. Another 40 cases were checked with a further 9 cases showing errors totalling £49.49. These errors were against a total claim of £90,986,752. As a result refresher training took place for all benefit staff in December 2010.

PwC had identified 5 recommendations to address in the 2010/11 Action Plan. All of these had been agreed by management and action had been taken to implement all the recommendations.

The Committee **noted** the report and acknowledged that the good standard of working papers had continued to contribute to the continued decrease in audit fees. It was anticipated that 9 grants would require certification in 2010/11.

**34. INTERNATIONAL REPORTING STANDARDS AND CLOSE-DOWN – PROJECT PLAN UPDATE**

Officers advised the Committee of progress to date in preparing for the implementation of International Reporting Standards in Local Authority Accounting and the closure timetable for 2010/11. The report also considered the potential impact of changes in the accounts and audit regulations affecting the process for approving the accounts.

The Committee **noted** that Phase 2 was substantially complete and that Phase 3 was on track.

**35. TREASURY MANAGEMENT UPDATE – Quarter 3 2010/11**

*The Committee resolved to excluded the public from the meeting during discussion of the following item on the grounds that if members of the public were present it was likely that, given the nature of the business to be transacted, that there would be disclosure to them of exempt information within the meaning of paragraph 3 of Schedule 12A to the Local Government Act 1972 which could reveal information relating to the financial or business affairs of any particular person (including the authority holding that information) and it was not in the public interest to publish this information.*

The Financial Services Manager presented the report that set out the context that was part of the Chartered Institute of Public Finance and Accountancy (CIPFA) revised Code of Practice for Treasury Management.

The revised Code suggested that Members would be informed of Treasury Management activities at least twice a year or preferably quarterly. The report ensured the Council was embracing Best Practice in accordance with CIPFA's revised Code of Practice.

The details of the report were outlined to the Committee, including that the Council had remained within its prudential indicators limits.

The Committee **NOTED** the report

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Chairman  
16 May 2011

# AUDIT COMMITTEE

# REPORT

16 May 2011

**Subject Heading:**

Response to a report from PWC on a complaint from Mr Macdonald

**Report Author and contact details:**

Sue Witherspoon, Head of Housing and Public Protection Extension 3747

**Policy context:**

The London Borough of Havering received a report from PWC detailing their recommendations in relation to a complaint from Mr Macdonald about his service charges. This report provides an update of actions taken.

**Financial summary:**

The report summarises the position on the costs and income related to the provision of TV aerials and satellite services for tenants and leaseholders of the London Borough of Havering. It notes that the cost of the service has not been reviewed by means of a tendered service since 1992; and considers the way forward to ensure value for money from this contract. It also notes that the cost of the service is not fully recovered from the tenants and leaseholders, and notes the proposed way forward to address this. The net cost of this service in 2010/2011 was around 175k

**The subject matter of this report deals with the following Council Objectives**

- Clean, safe and green borough
- Excellence in education and learning
- Opportunities for all through economic, social and cultural activity
- Value and enhance the life of every individual
- High customer satisfaction and a stable council tax

**SUMMARY**

1. The Council's Auditors, PWC wrote to the Director of Finance & Commerce on 9 August 2010 with the findings of an Investigation into a complaint from Mr Macdonald about the way in which charges for TV aerial services are levied.
2. This report sets out progress by the Housing Service against the recommendations of PWC in response to this complaint. A copy of the action plan is appended to this report.

## RECOMMENDATIONS

That the Committee:

1. Note the progress on actions in relation to the report by PWC on the issue of Service Charges

## REPORT DETAIL

### Background

1. The Council's Auditors, PWC wrote to the Director of Finance & Commerce on 9 August 2010 with the findings of their investigations, into a complaint by a leaseholder, Mr Macdonald. The complaint related to the way in which building insurance charges were levied, and the way in which charges were levied for access to TV and Satellite access points.
2. PWC were satisfied that the charges on buildings insurance were reasonably calculated and reflected the costs incurred by the Council, and made no recommendations as to any action in respect of this item.
3. In respect of the charges relating to TV/Satellite access points, PWC found that the Council was lawfully entitled to levy the charge. However, in 2005/6 the basis of recharging to leaseholders changed, but there was insufficient documentary evidence retained to explain how that decision had been arrived at. Also, PWC were concerned to note, that the full costs of the service were not being recovered and that the income from tenants and leaseholders did not cover the full charge. PWC recommended that this charge be reviewed.
4. PWC also noted that Mr Macdonald had not been properly charged for his TV Aerial access, and that this was the result of an oversight. PWC recommended that the Council check to ensure that there were not similar errors occurring in respect of other charges and other tenants or leaseholders.

5. PWC raised a concern that the decision taken by the Council in 2005, whilst strictly legal, as considered by the Council's Monitoring Officer, could have been better justified had a formal decision been recorded as an officer decision, either in consultation with the Lead Member (or the equivalent process at that relevant date).
6. A further point considered by PWC was the lack of transparency for the difference in the way in which leaseholders and tenants were charged. PWC considered that the charges should be the same, unless the services were different. Any difference should be justified in line with rational criteria. The charges to leaseholders were based on a figure for 52 weeks of the year, but the charges to tenants were based on a figure of 48 weeks of the year.
7. One of the points raised as part of the review, was that payments under the contract that the Council holds with Surtees, (who provide the access points for TV and Satellite television and who also maintain the equipment) have not been reconciled. The payments to Surtees are based on the number of access points, whilst there is no agreed list of access points between Surtees and the Council. PWC recommended that reconciliation should take place, and a review of the whole of the contract, and whether it provides value for money, should be undertaken.
8. Given the concerns with aspects of the contract with Surtees, PWC also recommended that there should be a review of all high value or lengthy contracts that are currently held by the Council.

Action taken to address the concerns raised

*Basis for charging*

9. The Housing Service has instituted a review of all service charges made to leaseholders and tenants. The review established a joint working party between Homes in Havering and the London Borough of Havering, to oversee the project, and a dedicated project officer has been undertaking the work. The review involved consultation with tenants through focus groups, a survey of all tenants, and workshops at the annual tenants' conference in October 2010.
10. Service charges in respect of most services have now been set in line with tenants' expressed wishes. Four service charges have been raised to ensure that the full cost of the service is being recovered:
  - Caretakers
  - Neighbourhood wardens
  - CCTV (fixed)
  - Bulk refuse removal

Two service charges were not increased in 2011/12 as tenants strongly expressed their view, that the service was not of an adequate standard. It has therefore been decided to carry out a full review of the service, and

ensure that it is improved to an acceptable standard before service charges are raised. These services are:

- Internal block cleaning
- CCTV (mobile)

Other services are due to be reviewed in the course of 2011/12. These are:

- Heating and hot water
- Grounds maintenance
- Sheltered cleaning
- TV access

#### Surtees contract - higher annual charges for leaseholders

- 14 As reported at the last meeting, although it is true that in charges raised directly through the service charges, leaseholders appear to pay more than tenants (through the annual charge), as the cost of the service is not fully met by the income, the shortfall has to be met by the HRA. This in effect means that tenants are subsidising leaseholders' services. The aim is to address this by raising charges for both leaseholders and tenants to ensure that they are fully recovered, and at the same time negotiate improvements in the value for money of this contract, to then reduce the cost to service charge payers, whether tenant or leaseholder.

#### General - errors in charging

- 15 The report from PWC identified that Mr Macdonald had actually not been charged for the TV aerial service in two successive years (2007/8 and 2008/09). When investigated, it emerged that this was an oversight. PWC therefore recommended that a check should be carried out to ensure that all leaseholders were being properly charged for all services that they received. This check has now been carried out, and tenants and leaseholders who were not being charged for the services that they were receiving were included in the service charge accounts for the year starting April 2011.



### General - documentation of use of delegated powers

- 16 This has now been dealt with, and formal decisions are recorded in an appropriate format.

### Surtees contract - signed copy of the original contract

- 17 Sealed copies of the original 1992 contract and the 1997 variation have been located. A poor quality copy of what appears to be a signed version of the 2001 variation, has also been located and it is accepted by Surtees that this is the appropriate document. Legal advice has been taken on the implications of these contractual documents and negotiations are currently underway on the subject of the TV aerial and satellite service

### Surtees contract - numbers of access points

- 18 A full list of addresses where services are being provided has now been reconciled with Surtees, and there is one common list between the contractor and ourselves which is being used as the basis of our contract.

### Surtees contract - benchmarking costs

- 19 One part of the Surtees contract relates to the provision of a repairs service for the door entry facilities. It has remained difficult to identify suitable benchmarking costs. The Council is seeking to tender the door entry part of the contract separately, which is the best form of benchmark. This matter is still in dispute between ourselves and Surtees.

### Wider Contract Review

- 20 Homes in Havering have reviewed all existing contracts and are ensuring that these are tendered in a timely way.
- 21 The Council has commissioned a wider contract review in terms of commodity contracts the results are being considered by individual departments.

### Conclusion

- 28 The PWC report has been helpful in identifying a number of difficulties in the way in which service charges have been calculated and recovered by the Council. The contract specifically for TV aerial (terrestrial and satellite) services was entered into in 1992, when the technology was new, and all landlords were relatively inexperienced in providing these kinds of services. The report has shown that the assumptions and charges made when the services were first provided are no longer appropriate, and that the Council needs to make sure it carries out regular reviews of such services and charges in order to ensure that its decision making remains logical and fair, and that the services provided are appropriate to its tenants and

leaseholders. The intention is that the Council's re-negotiation of this contract will produce better value, either through revised terms and conditions with Surtees, or through re-tendering.

- 29 It should be noted that a further objection to the accounts has been received from Mr Macdonald, and that a meeting has been held between PWC and Mr Macdonald in January. The basis of his objection appears to cover much of the same ground – in particular Buildings Insurance and the charge for TV terrestrial and satellite aerials. There are some areas where PWC have indicated that they will do further investigation, but there are others where they have indicated that these matters have either been dealt with, or are subject to other methods of investigation – e.g. Information Commissioner, Leasehold Valuation Tribunal or the Police.

## IMPLICATIONS AND RISKS

### **Financial implications and risks:**

1. This report is presented for information. It provides an up-date on actions being taken to improve procedures for TV/Satellite access charges, and service charges more widely.
2. The report refers to various actions being taken to improve process. As explained changes are being made so that the costs of various HRA services are more closely reflected by charges to the service recipients. Though the HRA has been able to absorb deficits, this has meant that some costs are being met by remaining tenants, and is being addressed as quickly as practicable.

### **Legal implications and risks:**

The report by PWC confirms that the objections to the accounts lodged by Mr Macdonald do not identify any illegal charging by the Council. Mr Macdonald made an application to the Leasehold Valuation Tribunal against the imposition of these charges. Whilst the Tribunal accepted that the charges were lawful, they found against the Council in terms of the amount of charge. The Council has obtained permission to appeal to the Upper Tribunal against this finding and the outcome should be known around about June or July 2011

**Human Resources implications and risks:** None arising directly from this report.

**Equalities implications and risks:** None arising directly from this report.

## BACKGROUND PAPERS

Working papers held within the Housing and Public Protection Service.



# AUDIT COMMITTEE

# REPORT

16 May 2011

<b>Subject Heading:</b>	Private Sector Leased Accommodation (PSL)
<b>Report Author and contact details:</b>	Sue Witherspoon, Head of Housing and Public Protection Extension 3747
<b>Policy context:</b>	Private Sector Leased Accommodation is a form of temporary accommodation primarily used to discharge the Council's duty to provide interim accommodation for homeless households
<b>Financial summary:</b>	The report summarises the financial position of PSL accommodation showing that on a turnover of £c9m, the Council collect around 96.5%.

**The subject matter of this report deals with the following Council Objectives**

Clean, safe and green borough	□
Excellence in education and learning	□
Opportunities for all through economic, social and cultural activity	□
Value and enhance the life of every individual	□
High customer satisfaction and a stable council tax	X

**SUMMARY**

This report sets out the framework in which the Council uses Private Sector Leased accommodation to support its duties under homelessness legislation, and other discretionary powers to intervene to prevent households from becoming homeless. It explains how the properties are procured and managed, and paid for within the Retained Housing Service.

**RECOMMENDATIONS**

That the Committee:

1. Note the financial position of the Council's Private Sector Leased (PSL) accommodation;
2. Note that there may be future budget pressures on this form of temporary accommodation as a result of the Government's changes to the Housing Benefit Subsidy system

<b>REPORT DETAIL</b>
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Background

1. The Council has a range of duties that arise under Homelessness legislation. The initial duty is that if the Council has reason to believe that someone may be homeless, the Council must investigate the circumstances. If the Council has reason to believe that the applicant may be homeless and be in priority need, then the Council has a duty to provide interim accommodation whilst those investigations take place. Priority need category applicants broadly include families with children, older people, and people who are vulnerable by reason of disability, health, mental illness or age. The further investigations involve assessing the households needs, and their previous housing history to establish whether the applicant has done anything deliberately, or recklessly that has led them to become homeless ("the intentionality test"). If a household has become homeless through no fault of their own, and are in priority need, then the Council has a duty to secure that settled accommodation shall become available to them. If the Council establishes that it does have an ongoing to duty to secure accommodation for the applicant and anyone who might reasonably be expected to live with them, then the obligation to provide interim accommodation continues until such settled accommodation becomes available.
2. Temporary accommodation has to be reasonably suitable. Havering currently provides emergency accommodation in hostels, and more long term temporary accommodation through properties leased from the private sector (PSL). Individual properties are leased on a three year basis from private landlords, and then managed by a team of 7.5 officers, including one Team Leader at SO2 level. The cost of funding this team is recovered from the rents charged to the tenants.
3. There is a specific limit on the amount of rent that the Council can charge the tenants, which is set by the Housing benefit subsidy system. This is 90% of the Local Housing Allowance (LHA), plus a Management fee of £40 pw. The LHA is also the amount that a private tenant who is renting the private sector can claim if they are benefit dependent and living in private rented accommodation. The LHA rate is set by the Valuation office, who

monitor rents within a Broad Market Rental Area, and who set the LHA rate at the 30<sup>th</sup> percentile of the market. In effect, benefit claimants can choose accommodation from accommodation available in the market where the rents are in the bottom third of the market.

#### Current Position

4. The Council currently leases 810 units of PSL accommodation from 650 different landlords. The rents payable by the tenants are, for 2011/12:

Size	Rent per week
1 BED	£180.19
2 BED	£216.54
3 BED	£258.08
4 BED	£330.77

5. The total rental income from this in 2010/11 was **£8,677,650**. In the year ended 31<sup>st</sup> March 2011, the PSL team collected **£8,374,175**, which comprises a collection rate of 96.5%. This compares favourably with the collection rate of Council Tax (96%) and Council housing rents (98%). The rents are very much higher than Council rents, so the arrears will accumulate more quickly. In addition, as the accommodation is only temporary, there is a higher proportion of people who leave without giving notice. Homeless households generally are more vulnerable and likely to have complex life histories, and therefore a collection rate of 96.5% in this context is very good.
6. Arrears owed by current tenants amount to £455,554. This includes some arrears built up from previous years. The current arrangements for the collection of rent are that:
- Letters are issued to tenants when arrears reach 2 weeks
  - Contact is made with tenants by telephone and home visits
  - All residents are provided with assistance in completing relevant Housing benefit forms
  - Staff will arrange to liaise with Housing benefit staff where benefit is not in payment
  - Staff will accept offers of payment from tenants for the repayment of arrears which are consistent with the tenants' ability to pay
  - Action is taken to serve Notice to Quit and take court action where arrears are not being reduced
  - Court action unfortunately takes time, and therefore it is likely that arrears will accumulate during the time taken to obtain court hearing dates, and execute bailiff's warrants
7. Former Tenants' Arrears (FTAs) that is, rent arrears which are owed by tenants who have left their accommodation amounts to **£634,681** at 31<sup>st</sup> March 2011. These arrears are owed by 213 tenants. These may be tenants who have disappeared, or in some cases have been rehoused.

Efforts are made to recover former tenants' arrears through correspondence and tracing agents, but where the arrears are very old, and there is no current address for the debtor, the debt may have to be written off. Debts are generally not written off where we know where the debtor lives, or they hold a current tenancy with the London Borough of Havering.

### The future

8. The Retained Housing Service have recently engaged an officer for a period of six months, dedicated to the collection of former tenant arrears, and to review and overhaul procedures to ensure that performance in this area is as good as it can be. However, it is important to bear in mind the factors that cause this income to be difficult to collect.
  
9. The PSL scheme houses more than just those to whom we owe a duty under homelessness legislation. We are also able to obtain and manage temporary accommodation in order to prevent people from becoming homeless, and as a result PSL accommodation has been used in order to assist people who are otherwise threatened with homelessness, who are not in priority need, or who may have made themselves homeless. In addition, some overcrowded households have moved into PSL accommodation as part of this overall scheme. The numbers are:

<b>Type of housing need</b>	<b>Number of households in each housing need group currently living in PSL accommodation</b>
Statutory Homeless households under s193 of the Housing Act 1996	381
Homelessness but not in priority need under s192(3) of the Housing Act 1996	111
Households on the Council's Housing Register who have been identified as overcrowded under the Government's new Bedroom Standard definition	262
People who are living in the Council's accommodation whose tenancy is coming to an end because they have no rights to succeed to the tenancy	8
Children and adults who are owed a social services duty but not a housing duty including young people requiring accommodation who are owed a duty under the Children (Leaving Care) Act 2000	36
Void	26
<b>Total</b>	<b>824</b>

11. In the past three years, the Government have indicated their intention to reduce the amount of money available for temporary accommodation support. As a result there have been a number of reductions to the Housing Benefit subsidy system, which has reduced the income the local authority



receives from PSL accommodation. The current system is in place until 2012/13 but it is likely that it will be further reduced after this date. The Council could therefore consider reducing its involvement in discretionary temporary accommodation schemes, and seek to find ways, where possible, to assist more households directly into sustainable housing options that do not involve the Council in managing an interim solution.

## IMPLICATIONS AND RISKS

### 12 Financial implications and risks:

#### *Collection*

This report was requested to clarify the arrears position on PSLs. The arrears have grown, year on year, as the operation has similarly grown:-

<b>Arrears</b>	<b>Year ending 2008/09</b>	<b>Year ending 2009/10</b>	<b>Year ending 2010/11</b>
Current	309,783	363,929	455,554
Former	290,015	443,480	634,681
<b>Total</b>	<b>599,798</b>	<b>807,409</b>	<b>1,090,235</b>

These arrears are covered in the accounts by a Bad Debt provision. While, at 31<sup>st</sup> March 2011, there is £1,090,235 of arrears, there is actually £923,000 worth of Bad Debt provision as cover, should some of the arrears prove non collectable.

As explained in paragraph 7 above, these debts are difficult to collect; it is for this reason that some councils ensure near 100% bad debt provision in this area. Paragraph 8 refers to measures being taken to improve the collection rate. This said, however, the context of these arrears is a collection rate running at 96.5% (paragraph 5 above).

#### *Medium Term*

Currently the PSL scheme is a cost effective method of providing temporary accommodation. Paragraph 11 refers to possible changes from 2013/14 in the government's subsidy system for PSLs. This may make the regime less

attractive financially. Any such changes will need to be monitored and addressed – in service and financial terms – when and if they become firmed up.

**Legal implications and risks:**

The Council has both a duty and a power to provide temporary accommodation for people who are homeless and in priority need whilst investigations are carried out into their cases. In addition, the Council has a duty to provide temporary accommodation for those to whom it owes a duty to provide settled accommodation, but where it is unable to provide that accommodation immediately. The Council further has powers to provide temporary accommodation in order to prevent people from becoming homeless.

Debt collection action can be taken in almost all cases where arrears have accrued, however, unless there is any realistic prospect of recovery this is often unproductive.

**Human Resources implications and risks:** None arising directly from this report.

If it is decided in the future, to reduce our stock of PSL accommodation, this will have implications for the team that manage the temporary accommodation function. However, this report does not propose any change of policy at present.

**Equalities implications and risks.**

A significant number of households who are assisted with temporary accommodation have vulnerabilities. This is because homelessness amongst families is often associated with difficult life events, such as debt, relationship breakdown and domestic abuse. In addition, those households who are assisted because they are vulnerable will have particular difficulties. They will only be entitled to assistance because they are vulnerable by reason of their age (this could be either old age, or young and vulnerable) disability, mental illness or other special reason.

Nothing in this report changes our duties to these households, who will continue to be assisted in line with current legislation.

**BACKGROUND PAPERS**

Working papers held within the Housing and Public Protection Service.

# AUDIT COMMITTEE

# REPORT

16 May 2011

**Subject Heading:**

**EXTERNAL AUDIT FEES 2011/12**

**Report Author and contact details:**

Mike Stringer  
Head of Finance & Procurement  
Tel: 01708 – 432101  
E-mail : [mike.stringer@havering.gov.uk](mailto:mike.stringer@havering.gov.uk)

Ciaran McLaughlin  
[ciaran.t.mclaughlin@uk.pwc.com](mailto:ciaran.t.mclaughlin@uk.pwc.com)  
PricewaterhouseCoopers

**Policy context:**

The Audit Committee are required to consider the External Auditor's fees.

**Financial summary:**

The letter from PwC sets out the proposed fees for the audit year 2011/12. The fee proposed is lower than that for 2010/11, as had been expected.

## SUMMARY

The Audit Commission appoints the external auditors for the Council. Auditors are rotated after a maximum of ten years service to an organisation. The Council's External Auditor is now PricewaterhouseCoopers LLP (PwC).

A report was considered by the Committee in June 2010 setting out the work that was proposed for the 2010/11 audit and the resultant fee.

This report presents the fee for the 2011/12 audit, and asks the Committee to note that the audit plan for the year will follow in due course.

## RECOMMENDATIONS

The Committee is asked to:

1. Consider and comment on the contents of the report and the fee letter.
2. Note that the 2011/12 audit plan will be presented at a subsequent meeting.

## REPORT DETAIL

PricewaterhouseCoopers (PwC) are the current External Auditor for the London Borough of Havering, as appointed by the Audit Commission.

The attached letter sets out how the fee for the 2011/12 audit has been arrived at, and shows a comparison to the fee for the 2010/11 plan.

The fee letter is presented for the Committee to review and make any comments on, taking into account that the plan covered by the fee will be presented to a subsequent meeting.

PwC have confirmed in their letter that the indicative audit fee for the Council's 2011/12 financial year is based on the risk-based audit approach set out in the Code of Audit Practice and work mandated by the Audit Commission for 2011/12.

The letter goes on to outline:

- The value for money work to be undertaken, and
- The grant certification work.

Representatives from PwC will be present at the meeting to explain the proposed fees further.

## IMPLICATIONS AND RISKS

### Financial implications and risks:

The Committee received a report in June 2010, summarising the proposed external audit fee, and containing the audit fee letter from PwC. The attached plan sets out the proposed fee for the 2011/12 audit year.

The details of the proposed fee, with a comparison of the elements making up the fee for both 2011/12 and the preceding year, is shown in the table below:

Element	2011/12 Fee £	2010/11 Fee £
Financial statements, value for money conclusion and Whole of Government Accounts	333,099	370,110
Pension Fund Audit	35,000	35,000
Certification of claims and returns	78,000	78,000
<b>TOTAL FEE</b>	<b>446,099</b>	<b>483,110</b>

The overall fee, taking into account all these elements, will be £446,099, as against the previous year's figure of £483,110, a reduction of £37,011 or 7.7%. This is broadly in line with the expected position from previous announcements by the Audit Commission, and also broadly in line with the £40k saving in fees included as part of the budget-setting process. The fees for both pensions and grants work have been held at the same level as 2010/11.

The fee includes estimated fees required to audit grants but does not include any additional work requested by the Council, or any additional work generated outside any assumptions on which the fee is based. As the letter indicates, the quoted fee is an estimate and may change to reflect the actual content of the audit plan.

The proposed fees are within the budget provision. There are no other financial implications or risks arising directly from this report.

**Legal implications and risks:**

None arising directly from this report

**Human Resources implications and risks:**

None arising directly from this report

**Equalities implications and risks:**

None arising directly from this report

**BACKGROUND PAPERS**

None.

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Andrew Blake-Herbert  
London Borough of Havering  
Town Hall  
Main Road  
Romford  
RM1 3BB

19 April 2011

Dear Andrew

**Annual Audit Fee 2011/12**

We are writing to confirm the audit work that we propose to undertake for the 2011/12 financial year at the London Borough of Havering. The fee is based on the risk-based approach to audit planning as set out in the Code of Audit Practice and work mandated by the Audit Commission for 2011/12.

As we have not yet completed our audit for 2010/11, the audit planning process for 2011/12, including the risk assessment, will continue as the year progresses and fees will be reviewed and updated as necessary.

The total indicative fee for the audit for 2011/12 is for £333,099 (excluding VAT) which compares to the planned fee of £370,110 for 2010/11. We propose to hold the fee for the Pension Fund at £35,000 - the scale fee – for the third successive year. A summary of this is shown in the table below.

<b>Audit area</b>	<b>Planned fee 2011/12 £</b>	<b>Planned fee 2010/11 £</b>
Financial statements, value for money conclusion and Whole of Government Accounts	333,099	370,110
Pension fund audit	35,000	35,000
Certification of claims and returns	78,000	78,000
<b>Total audit fee</b>	<b>446,099</b>	<b>483,110</b>

*PricewaterhouseCoopers LLP, 80 Strand, London WC2R 0AF  
T: +44 (0) 1224 210100, F: +44 (0) 1224 253318, www.pwc.co.uk*



The Audit Commission has published its work programme and scales of fees 2011/12<sup>1</sup>. The Audit Commission scale fee for the London Borough of Havering is £333,009. The fee proposed for 2011/12 matches the scale fee.

In setting the fee at this level, we have assumed that the general level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2010/11. A separate plan for the audit of the financial statements will be issued in November 2011. This will detail the risks identified, planned audit procedures and any changes in fee. If we need to make any significant amendments to the audit fee during the course of the audit, we will first discuss this with you and then prepare a report outlining the reasons why the fee needs to change for discussion with the audit committee.

It may be possible to reduce the audit fee further by addressing the issues we noted in the ISA260 report in the 2009/10 audit. We will also review the fee after the audit of the 2010/11 financial statements is completed.

We are required by the Code of Audit Practice to meet the requirements of the International Standards on auditing (UK and Ireland) revised, (clarity ISAs(UK&I)) as well undertake sufficient work to provide a conclusion on value for money. The audit fee is therefore based on the amount of work we are required to do to meet these standards. However, as indicated above, the audit fee is adjusted depending on the risk in relation to each specific audit. Whilst some risks are generic to all local authorities, others are specific to each audited body.

Failure to meet agreed timetables and/or the provision of poor documentation could mean that additional audit work is necessary, or our audit is delayed. In this case, we may charge additional fees to cover the costs incurred.

### ***Value for money conclusion***

Our value for money conclusion will be based on our assessment of the two criteria:

- The organisation has proper arrangements in place for securing financial resilience; and
- The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

### ***Value for money work***

We will apply a light touch approach to our Value for Money work at the authority. This will be based primarily on a review of the annual governance statement. We will conclude whether there are any matters arising from this work that we need to report, and will include these in the audit report at the end of the audit.

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<sup>1</sup> <http://www.audit-commission.gov.uk/SiteCollectionDocuments/Downloads/wpsoflocalgovt201112.pdf>





### ***Certification of claims and returns***

The quoted fee for grant certification work is an estimate only and will be charged at published daily rates. In 2011/12, the de minimis threshold below which we are not required to certify individual claims and returns will be £125,000, and the intermediate threshold below which are required to undertake only a light touch review will be £500,000. Above this threshold, certification work will be risk-based, taking account of the authority's overall control environment. We are required to report annually to those charged with governance on the results of certification work.

### ***Other matters***

We will issue a number of reports relating to our work over the course of the audit. These are listed at Appendix 1.

The key members of the audit team for the 2011/12 are:

Engagement Leader – Julian Rickett                      01603 883321    [julian.c.rickett@uk.pwc.com](mailto:julian.c.rickett@uk.pwc.com)

Engagement Director – Ciaran McLaughlin            020 7213 5253, [ciaran.t.mclaughlin@uk.pwc.com](mailto:ciaran.t.mclaughlin@uk.pwc.com)

Audit Manager – Chris Hughes                      020 7804 3392, [chris.hughes@uk.pwc.com](mailto:chris.hughes@uk.pwc.com)

Team Leader – Jessica Fogarty                      07894 443379, [jessica.fogarty@uk.pwc.com](mailto:jessica.fogarty@uk.pwc.com)

We are committed to providing you with a high quality service. If you are in any way dissatisfied, or would like to discuss how we can improve our service, please contact me in the first instance. Alternatively, you may prefer to discuss matters with Paul Woolston, our Audit Commission Lead Partner at our office at 89 Sandyford Road, Newcastle Upon Tyne, NE1 8HW, or Richard Sexton, UK Head of Assurance, at our office at 1 Embankment Place, London, WC2N 6NN. In this way we can ensure that your concerns are dealt with carefully and promptly. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. This will not affect your right to complain to the Institute of Chartered Accountants in England and Wales or to the Audit Commission.

Yours sincerely

Julian Rickett



### **Appendix 1: Planned outputs**

Our reports will be discussed and agreed with the appropriate officers before being issued to the Audit Committee.

<b>Planned output</b>	<b>Indicative date</b>
Audit plan	November 2011
Annual certification report (relating to claims and returns certified in the previous year)	February 2012
Internal Control Issues and recommendations for improvement	May 2012
ISA (UK&I) 260 report to those charged with governance	September 2012
Auditor's report giving the opinion on the financial statements and value for money conclusion	September 2012
Annual Audit letter	November 2012

# AUDIT COMMITTEE

<b>Subject Heading:</b>	Internal Audit Progress Report Q4
<b>Report Author and contact details:</b>	Paula Sisson – Internal Audit & Corporate Risk Manager ext 3733
<b>Policy context:</b>	To inform the Committee of progress towards delivery of the audit plan Quarter four 2010/11.
<b>Financial summary:</b>	N/a

**The subject matter of this report deals with the following Council Objectives**

Clean, safe and green borough	<input type="checkbox"/>
Excellence in education and learning	<input type="checkbox"/>
Opportunities for all through economic, social and cultural activity	<input type="checkbox"/>
Value and enhance the life of every individual	<input type="checkbox"/>
High customer satisfaction and a stable council tax	<input checked="" type="checkbox"/>

**SUMMARY**

This report advises the Committee on the work undertaken by the internal audit team during the period 1 January 2011 – 31 March 2011.

**RECOMMENDATIONS**

1. To note the contents of the report.
2. To raise any issues of concern and ask specific questions of officers where required.

## REPORT DETAIL

This progress report contains an update to the Committee regarding Internal Audit activity presented in seven sections.

Page

### **Section 1 Audit Work 1 January - 31 March 2011**

A summary of the reports finalised by the end of March is included in this section of the report.

### **Section 2 Management Summaries**

Summaries of all final reports issued in the period.

### **Section 3 Schools Audit Work**

A summary of schools work undertaken in the period.

### **Section 4 Budget & Resource Information**

The budgetary and resource position at the end of March are included for information.

### **Section 5 Key Performance Indicators**

The actual performance against target for key indicators is included.

### **Section 6 Changes to the Approved Audit Plan**

The changes made to the audit plan since the last meeting are detailed and explained in this section of the report.

### **Section 7 Outstanding Recommendations Summary Tables**

The details regarding status, as at the end of March, of all outstanding recommendations are included within tables for information.

## Section 1 Audit Work 1 January – 31 March 2011.

At the end of March 89% of the audit plan had been delivered. This was against a target for the period of 97%.

Schedule 1 details the work completed in quarter four. Details are listed in the table below and management summaries under Section 2 starting on page 4.

### SCHEDULE 1: 2010/2011 – Systems Audits Completed

Report	Opinion	Recommendations				Ref Below
		High	Med	Low	Total	
Schools Human Resources	Unqualified	0	0	0	0	2 (1)
Council Tax	Unqualified	0	1	0	1	2 (2)
Creditors	Unqualified	0	0	0	0	2 (3)
Main Accounting	Unqualified	0	0	0	0	2 (4)
Tranman Application	Qualified	3	7	1	11	2 (5)
IT Change Management	Unqualified	0	4	0	4	2 (6)
Housing Benefits	Unqualified	0	0	0	0	2 (7)
Payroll	Unqualified	0	1	1	2	2 (8)
Pensions	Unqualified	0	0	2	2	2 (9)
Debtors	Unqualified	0	0	1	1	2 (10)

## Section 2 Management Summaries

<b>Schools Human Resources</b>	<b>Schedule 2(1)</b>
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### 2.1 Background

- 2.1.1 This audit was planned to correspond with the start of the Internal Audit team's provision of the Internal Audit service to Schools, to ensure that the overall control environment at the Council was understood and evaluated to ensure the Council's risks are managed.
- 2.1.2 The team provide a traded service to schools, who determine what level of service they require which is agreed via a Service Level Agreement (SLA). There are a total of 79 schools, including secondary, primary and special schools, in the borough. Of these, 76 establishments buy-in services from the team at an annual cost of £558,229 (actual charges to schools for 2010/11).
- 2.1.3 Schools' HR are currently separate to the Council's corporate HR team, it is noted that plans are being considered to bring aspects of the Schools' HR into the shared service centre along with corporate HR team, however if agreed this will not take place until September 2011 at the earliest.
- 2.1.4 In 2009/10 all the Council's Human Resources functions were subject to an independent efficiency review so the scope of this audit has not included these risk areas to avoid duplication.

### 2.1.5 Summary of Audit Findings

- 2.1.6 A range of strategic and operational advice and guidance is given to all 79 schools in relation to the Council's statutory HR functions. In addition a range of strategic and operational advice and guidance, in accordance with the SLA, is available to those schools buying into traded services.
- 2.1.7 The small number of schools that purchase the traded services from other providers limits the risk to the team of providing services to schools that have not purchased them. At times, these schools may be provided with support and advice exceeding the statutory requirements. This is to manage risks to the Council as much as the risks to the school.
- 2.1.8 The Schools' HR team's reliance on school's buying into the Council's traded services makes it difficult to enforce non statutory requirements.
- 2.1.9 With the importance of Safer Recruitment within Schools, assurance on compliance with this would be valuable to the team. However, whilst information demonstrating this can be requested from schools, there no obligation for schools to provide it. As such and in order to gain some level

of assurance, this check will be incorporated into the Internal Audit work programme for school audits.

2.1.10 A review of officers with access to the team's shared information area, identified four officers who no longer required access to the data, action was taken to resolve this during the audit.

### **2.1.11 Audit Opinion**

2.1.12 As a result of this audit we have raised no recommendations for the service. However the Internal Audit schools audit programme has been amended to include an evaluation and testing of safer recruitment processes within schools to ensure that the Governors and Head Teachers as well as the Schools' HR team gains sufficient assurance that risks are being appropriately managed.

2.1.13 An **unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

<b>Council Tax</b>	<b>Schedule 2(2)</b>
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## **2.2 Background**

2.2.1 All properties are subject to Council Tax and to determine the amount payable they are allocated a band according to their market value as at 1<sup>st</sup> April 1991. The bands range from A to H dictating an amount payable for each band.

2.2.2 Money raised through the Council Tax is retained to fund Council spending. For the financial year 2009-10 income from Council Tax amounted to £117,286,400 from a total of £121,224,959.

### **2.2.3 Summary of Audit Findings**

2.2.4 The audit review found that recommendations raised as part of previous years audits have not yet been fully implemented. The Council is currently in the process of pulling central services such as Payroll, Human Resources and Procurement into an Internal Shared Service (ISS). Whilst this does not directly impact on the Council Tax team, the movement of the team from Finance to Customer Services will have an impact. As part of the move into Customer Services, the Council Tax team will be subject to a restructure which will further impact on the team.

2.2.5 The deadline for updating the procedures manual was March 2010. At the time of the last audit it was recognised that this deadline was unlikely to be met. Due to the introduction of Internal Shared Services, it was considered to be more efficient to wait until the new systems were implemented before completing the procedures manual. As part of the preparation for this move process mapping has been completed.

2.2.6 Spot checks on officers work was recommended as part of the 2009-10 audit. The implementation of these checks was delayed as one post responsible for the completion of these checks is vacant. The other is currently filled by a temporary employee. There is therefore an on-going risk that non compliance or human error is undetected in processes.

2.2.7 An annual report is run of all council tax liable properties where the liable party is unknown. A review of this report found that action has not been taken in recent years to identify the liable party.

### **2.2.8 Audit Opinion**

2.2.9 As a result of this audit we have raised one medium priority. The recommendation relates to the need to run regular reports and investigate those properties where the liable party is unknown. Prior recommendations will continue to be monitored via quarterly update and reporting to Audit Committee.

2.2.10 An **Unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

<b>Creditors</b>	<b>Schedule 2(3)</b>
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## **2.3 Background**

2.2.1 Creditors payments through the Council's bank account for 09-10 totalled over £415million

2.3.2 During the period 1<sup>st</sup> April 2010 – 31<sup>st</sup> October 2010, 52,085 invoices were paid, with a net total of over £250million.

### **2.3.3 Summary of Audit Findings**

2.3.4 In a sample of invoices, the authorised signatory did not have the relevant authorisation form held on FIS for 17 of the 48 tested. It was found that this information held on FIS was not necessarily up to date mainly due to a backlog in scanning of authorisation forms. However, it is expected that the forthcoming changes to the system in 2011/12 will help to address this.

2.3.5 A number of duplicate invoices were found to have been paid during audit testing. Further analysis identified that these were entered primarily by one member of staff with the same errors occurring. All duplicates over a minimum level were all picked up and recouped by the Systems Team and training concerns raised where required.

2.3.6 Due to a recent increase in other local authorities receiving false changes of information correspondence, additional controls have been put in place to mitigate any increased risk arising from this.



### 2.3.7 Audit Opinion

2.3.8 As a result of this audit no recommendations have been raised.

2.3.9 An **Unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

<b>Main Accounting</b>	<b>Schedule 2(4)</b>
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## 2.4 Background

2.4.1 Oracle Financials is the key financial system used by the Council. This audit has focused on administrative processes.

### 2.4.2 Summary of Audit Findings

2.4.3 Administrative processes tested during this audit were found to have good controls in place and no issues were found during the course of this audit.

### 2.4.4 Audit Opinion

2.4.5 No recommendations were raised as part of this audit

2.4.6 An **Unqualified** audit opinion has been given as the audit has found that the system of control is generally in place.

<b>Tranman Application</b>	<b>Schedule 2(5)</b>
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## 2.5 Background

2.5.1 The Passenger Transport Service (PTS) team at the Purfleet Depot uses the fleet management system, Tranman to keep an inventory of all of the vehicles that the Council holds through the full lifetime of their use. Passenger Transport Services vehicles are available for hire to Council affiliated groups (e.g. Nursing Homes/PTA's) and Council employees. The Hires module in the Tranman application is used to keep track of and pay invoices for all vehicles hired by the council from 3rd party companies for use to cover vehicles off the road or awaiting purchase and, to re-charge departments for the hire of these vehicles. The application is also used to log the amount of fuel used by all vehicles used by the Council, including hire vehicles to allow the costs to be recharged to departments.

- 2.5.2 The workshop at the depot is responsible for maintaining the entire Council fleet and any hired vehicles used by the Council. The workshop team use the Tranman application to raise work jobs on the system for carrying out fleet inspections, arranging MOT's, servicing, minor repairs and organising major repairs with approved repairers. The schedule of rates which is an industry list of the time required to complete a task within the Workshop. The fitters access a screen to log the time taken for the actual time taken on tasks. Jobs are then updated on Tranman to report on productivity.
- 2.5.3 The Storeman is responsible for maintaining an inventory of stock used regularly by the workshop fitters and maintains an inventory of stock items. Invoices sent by suppliers are manually input against stock orders through the system.
- 2.5.4 The Tranman application has been live at the Council since April 2008. There are 17 modules currently in use in the application which are used to carry out the activities described above. Our audit concentrated on the vehicles, stocks and hires modules of the system.
- 2.5.5 The application servers are hosted within Mercury House and managed by the Business Systems function with external support from the supplier, CIVICA.
- 2.5.6 **Summary of Audit Findings**
- 2.5.7 A generic username for the system administrator account is in use and is shared between team members on the Tranman application limiting accountability of its use.
- 2.5.8 Weak password controls have been set on the application and the user's passwords have been set to be the same as their User ID. Unsuccessful user login attempts are not restricted as user accounts are not disabled following three unsuccessful login attempts. The existing password controls do not maintain a history of users' passwords to prevent their re-use and to prevent passwords becoming well known.
- 2.5.9 A procedure has not been established for the creation and management of new user accounts and leaver's accounts. Periodic reviews of users and their access rights are not performed on a regular basis. Although usage of the system is limited to a small user base there are plans to extend the use of the Tranman application.
- 2.5.10 User account sessions remain active if a user closes the application window without logging out of the system. This can mean that other users cannot login into the Tranman application when the number of active users exceeds the licences available. There is a requirement for an analysis to be carried out to determine if the current number of user licenses on the system is adequate.

- 2.5.11 User access on the system has only been restricted as per the modules that a user requires access to. Access to any fields or tabs within the modules has not been restricted to ensure the segregation of duties within modules. This is mainly due to uncertainty on whether the functionality is available in the application to be able to restrict access within a module. An analysis is still to be carried out to help ensure user group permissions are allocated in line with users' job roles.
- 2.5.12 Validation checks are not in place on the Order Number field when creating a new stock order, as any value is accepted and the unit price for an item of stock being ordered can be amended. A supplier code has been set internally on the system by the Stores team and a corresponding creditor code has to be selected so that the correct supplier is paid.
- 2.5.13 The process for the input of invoices onto the system should be reviewed to ensure that these are authorised or reviewed by senior management following input.
- 2.5.14 Amendments to master data such as adding or deleting new supplier codes are not recorded and the changes are not submitted to the requestor for approval.
- 2.5.15 The interface data from Tranman to Oracle (General Ledger and Accounts Payable) are reconciled to ensure accuracy. However, the control totals are not received for the text file generated from the fuel system TimePlan to ensure these can be reconciled with the total number of records being imported into Tranman for the amount of fuel used by the Fleet. There is a risk that the client may be unaware of any records which may not have been imported into Tranman and thus may not be recharged to the appropriate department for use of the fuel. However there is a further reconciliation with Oracle that may pick up cases of fuel being incorrectly transferred.
- 2.5.16 Although an audit trail facility has been set up on the system, an audit log is only created for transactions which run or creates a report. The system administrator was unable to confirm if any other transactions or record changes are audited. Additionally, the audit trail facility on the system does not log the details of which fields have been changed and does not record details of the data entered. Master data for core system data changes or unsuccessful logon attempts to access the system are also not captured.
- 2.5.17 A change control and patch management procedure is not in place to implement any updates on the Tranman application. Currently, the third party supplier CIVICA applies and tests any changes directly on to the live environment following testing.
- 2.5.18 A formally documented Business Continuity Plan is not in place for the Passenger Transport Services team. Confirmation also needs to be received from the Emergency Planning Officer to help ensure a Disaster Recovery Plan has been developed and documented for the Tranman application.

## 2.5.19 **Audit Opinion**

2.5.20 As a result of this audit we have raised 3 high priority, 7 medium priority and 1 low priority recommendations.

2.6.21 In order to further improve the control environment, management need to ensure that:

2.6.22 Password controls on the system are strengthened to incorporate strong passwords requiring a specific length, change frequency and history period. (High)

2.6.23 The system inactivity timeout should be enabled to ensure inactive account sessions are logged out or additional user licenses are purchased, so that the number of active user accounts do not exceed the licenses available. (Low)

2.6.24 A new user and leaver's procedure should be developed. Regular periodic reviews of dormant user accounts on the system should be performed to ensure that staff that no longer require access to the application are removed in a timely manner. (Medium)

2.6.25 User access permissions on the application are reviewed to ensure that users do not have excessive permissions and are in line with those duties required to complete jobs. (Medium)

2.6.26 User accounts are assigned a unique name and use of the shared system administrator account is discontinued for routine system access. The system administrators are provided with training and support on how to use the System Administrator functionality on the application.(Medium)

2.6.27 Data input validation controls on the system are enhanced to ensure data accuracy over specific fields on the system. (Medium)

2.6.28 Amendments to master data changes should be recorded and approved. (Medium)

2.6.29 The control totals of the text file received from TimePlan should be reviewed when transferring fuel records into Tranman to ensure all the records have been imported successfully and recharged to departments correctly. (High)

2.6.30 The audit trail facility is enhanced to maintain a record of all user transactions including details of the change made, master data changes as well as any failed logons into the system. (Medium)

2.6.31 A change control procedure should be implemented to ensure all patches and fixes to the Tranman application are authorised, back-out plans are specified and changes are tested on the test environment prior to being installed on the live environment. (Medium)

2.6.32 A formal Business Continuity Plan is documented for the continuation of the Passenger Transport Service function in the event of a disruption to normal use of the system. Formal and robust disaster recovery arrangements are implemented for the Tranman application and that these are tested on a periodic basis to help ensure that the system can be recovered in line with service expectations. (High)

2.6.33 A **qualified** audit opinion has been given as the audit has found weaknesses in the system of internal control that may put the Council's objectives at risk.

<b>IT Change Management</b>	<b>Schedule 2(6)</b>
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## **2.7 Background**

**2.7.22** The Council operates a shared ICT service with the London Borough of Newham. Given this arrangement, a review of the change management processes in place within each Council is being performed by an external consultant. The aim of the third party review is to promote the alignment of the change management function across these organisations. At the time of our audit this review had not reported to management.

**2.7.23** ICT is managed at two levels within the Council. Business Systems manage the core infrastructure that is in place and provide system support as required by Council services. In addition, local support teams are in place to provide IT support to specific systems within Departments in collaboration with the IT system providers. These local support teams operate independently of Business Systems and as such have their own processes and procedures which are followed, including those relating to change management.

**2.7.24** Business Systems centrally manages change that is made to the core IT infrastructure and systems that it supports. A formal scope of the changes that are managed by Business Systems has been formally documented and made available on the Council's Intranet.

**2.7.25** The change management process that is in place is founded on the principles of ITIL change management. Operationally supporting this process is the Hornbill Supportworks system, which is ITIL v3 compatible. This system enables the electronic management of requests for change and the authorisation of these changes following agreement.

**2.7.26** An interim Change Manager is in place pending the outcome of the review of the change management process and the formalisation of the arrangements with the London Borough of Newham.

**2.7.27** The Change Manager is the only permanent member of the Change Advisory Board (CAB). The technical leads and security lead form the remainder of the CAB based on the nature of the changes that are due for review at the individual meeting. The CAB meets on a weekly basis to approve changes. Specific representatives outside of Business Systems

may be invited to the CAB as required to review a change pertinent to that area.

2.7.28 The ICT environment is undergoing significant change. An agreement is in place with ACS to host the Council's infrastructure with the exception of the network. In light of this agreement, work is underway to transfer the servers from the current data centre to the ACS data centres located in Newport and Telford. It is anticipated that the existing Council's data centre will still be operational until March 2011.

2.7.29 The management of systems is to become more centralised as systems and servers are transferred from local team management to the ACS managed environment. This will have implications for the management of changes for these systems.

2.7.30 In addition to the transfer of the hardware within the data centres, a refresh of the network infrastructure is also being performed. The objective of this refresh is to enable improved connectivity between the Council and the London Borough of Newham.

### **2.7.10 Summary of Audit Findings**

2.7.11 A Change Management Policy and a Change Management Process have been documented. These documents detail the principles and steps to be followed when managing a change from initial request through to the post-change review and closure. Whilst the Change Management Process document remains relevant in principle, it was noted that the process itself is now more automated with the use of Supportworks. The interim Change Manager has documented the process that is followed within Supportworks to manage changes but the Change Management Process has not been updated.

2.7.12 A formal corporate IT replacement programme is currently not in place to guide hardware replacement. Departments have budgets that they may use at their discretion to request the procurement of additional hardware assets if required. However, management has noted that plans are in place to formalise the IT replacement programme and manage this centrally within Business Systems. This is expected to occur in the 2011/12 financial year.

2.7.13 Procedures are in place to log and resolve faults that are identified with the performance of hardware. However, processes for the proactive monitoring of hardware performance are not in place.

2.7.14 Supportworks provides Configuration Management Database (CMDB) functionality in the Assetworks module. The CMDB is updated to reflect the core systems that are in use within the Council and also details the desktops and laptops that are in place. Details of the servers, the systems that are hosted on these servers and the non-core software that is in use are not currently updated on the CMDB.

### 2.7.15 Audit Opinion

- 2.7.16 As a result of this audit we have raised 4 medium priority recommendations.
- 2.7.17 In order to further improve the control environment, management need to ensure that:
- 2.7.18 The Change Management Process and the details available on the Intranet are updated to reflect the change management processes that are in place and are required to be followed;
- 2.7.19 A formal IT replacement programme is established to provide guidance on when IT hardware assets should be replaced;
- 2.7.20 Adequate arrangements are in place to proactively monitor the performance of hardware assets and investigate and resolve any discrepancies that are identified as part of this monitoring; and
- 2.7.21 The CMDB is updated to reflect the core configuration items in place within the ICT estate and the interrelationship of these configuration items.
- 2.7.22 An **unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

<b>Housing Benefit</b>	<b>Schedule 2(7)</b>
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## 2.8 Background

- 2.8.1 Housing Benefit is governed by the guidelines issued from the Department of Work and Pensions (DWP) and subject to review from the Audit Commission.
- 2.8.2 Havering's Housing Benefit Service, aims to help residents of the Borough on low incomes by providing means tested funding to assist residents in paying their rent.

### 2.8.3 Summary of Audit Findings

- 2.8.4 A low priority recommendation was raised as part of the 09/10 Housing Benefits audit, which set out the need for minimum criteria to be devised relating to the level of accuracy checks to be undertaken within the team. A Housing Benefit Quality Assurance policy was developed as a result of this recommendation.
- 2.8.5 Testing undertaken during the audit review found inconsistencies in the level of checks being undertaken within each of the three teams, however, further investigation found that these were appropriate based on the level of work

and the experience of staff involved. No recommendation was raised as a result of this issue.

### **2.8.6 Audit Opinion**

2.8.7 As a result of this audit no recommendations have been raised.

2.8.8 An **unqualified** audit opinion has been given as the audit has found that the system of control is generally in place.

<b>Payroll</b>	<b>Schedule 2(8)</b>
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## **2.9 Background**

2.9.1 Havering Council's total payments for Salaries and Wages for 2009/10 amounted to £199,117,574.

### **2.9.2 Summary of Audit Findings**

2.9.3 A check of pensions remunerations forms found that in 50% (6/12) of cases checked the forms needed to be corrected by someone within the pensions team after being received from Payroll. In order for pensions to place more reliance on these forms, the level of errors need to be reduced. Results from the previous three pensions audits have shown a large proportion of these forms contain errors when passed from payroll to pensions, meaning the pensions team have to spend time and resources re-checking each form. This means that a payroll control actually lies in the Pensions Team. A secondary check has been enforced by the Payroll manager since November 2010.

2.9.4 The document storage system, Comino, is used by Payroll, Pensions and HR. Each department is responsible for scanning and saving documents. Some forms are required to be viewed by all three departments. Similar forms relating to different staff are saved in different locations, making it difficult to locate them at a later date.

2.9.5 Overtime payment authorisation is not controlled by payroll and in some cases large amounts of overtime are being claimed on a consistent basis by some members of staff. A report was run by the Payroll Manager and passed to HR for monitoring as a result of previous audit recommendations. However it was later decided that this wasn't utilised by HR and therefore stopped. It was found in one case that the hourly rate was wrong; this was checked by the Payroll manager and found to be an adjustment for previous underpayments.

2.9.6 Due to the imminent move of the Payroll function into Internal Shared Services it was decided to not test procedural compliance during this audit as the information would become obsolete. It was felt that it would be best to test the procedures which are developed after the move.



## 2.9.7 Audit Opinion

2.9.8 As a result of this audit we have raised one low priority recommendation, and one medium priority recommendation.

2.9.9 Recommendations relate to:

- The need for guidance to be created for the use of Comino, to allow for ease of finding stored information (Low)
- The need for more reliance to be placed upon the accuracy of pensions remunerations forms, to avoid Pension Staff having to undertake corrections (Medium)

2.9.10 An **Unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

<b>Pensions</b>	<b>Schedule 2(9)</b>
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## 2.10 Background

2.10.1 The London Borough of Havering (LBH) has a partnership arrangement with the London Borough of Redbridge in order to reduce costs and share knowledge and data

### 2.10.3 Summary of Audit Findings

2.10.4 A check of pensions remunerations forms found that in 50% of cases checked the pensions remuneration form needed to be corrected by someone within the Pensions team after being received from Payroll. In order for Pensions to place more reliance on these forms, the level of errors need to be reduced. Results from the previous three pensions audits have shown a large proportion of these forms contain errors when passed from payroll to pensions, meaning the Pensions Team have to spend time and resources re-checking each form. This means that a payroll control actually lies in the Pensions Team. A secondary check has been enforced by the Payroll manager since November 2011.

2.10.5 The document storage system, Comino, is used by Payroll, Pensions and HR. Each department is responsible for scanning and saving documents. Some forms are required to be viewed by all three departments. Similar forms relating to different staff are saved in different locations, making it difficult to locate them at a later date.

2.10.6 The lack of interface between the current payroll and pensions systems should be addressed by the imminent move to Internal Shared Services, where both departments will be using Oracle based systems.

2.10.7 Errors highlighted by the Pensions manager regarding the accuracy of data received will be reviewed and tested during the next Pensions audit after the move to the new systems.

### 2.10.8 Audit Opinion

2.10.9 As a result of this audit we have raised two low priority recommendations.

2.10.10 Recommendations relate to:

- The need for guidance to be created for the use of Comino, to allow for ease of finding stored information at a later date
- The need for more reliance to be placed upon the accuracy of pensions remunerations forms, due to additional checking which is taking place.

2.10.11 An **Unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

<b>Debtors</b>	<b>Schedule 2(10)</b>
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### 2.11 Background

2.11.1 The management of debtors relates to the raising of invoices for services provided by the Council, including subsequent cash collection and debt management.

2.11.2 In 2009/10 a total of 23,361 invoices were raised totalling £160,567,609. Between April 2010 and February 2011 a total of 25,001 invoices were raised totalling £185,557,184.

#### 2.11.3 Summary of Audit Findings

2.11.4 A total of one low priority and four medium priority recommendations were raised as a result of the 2009/10 Debtors audit. All of these recommendations have been implemented.

2.11.5 During the previous years audit, it was noted that the procedures manual was being reviewed and updated in line with the implementation of the new Oracle system. This audit found that the review has not been completed due to the planned implementation of Internal Shared Service (ISS). As the processes surrounding Debtors under ISS have yet to be determined, no recommendation is being raised regarding this issue as procedures will be completed once ISS goes live.

2.11.6 No formal processes have been established to monitor the quality of the data being entered onto the system. Whilst the current size and experience of the team mitigates some of the risk, the implementation of ISS and the likely expansion of the team will increase the level of risk to the Council.

2.11.7 Evidence to support debts raised centrally are held by source departments. The review found one department where the debt could not be proved and resulted in a request being made for the debt to be cancelled. Given the low amount involved and the implementation of ISS no recommendation has been raised. However, this issue will be revisited as part of the next audit.

2.11.8 Testing undertaken on the 15 cases referred to Legal Services found that cases had been progressed in an appropriate and timely manner, however, the summary sheet in one case had not been kept up to date. As this appears to be an isolated incident, no recommendation has been raised.

### **2.11.9 Audit Opinion**

2.11.10 As a result of this audit we have raised one low priority recommendation relating to the need to carry out spot checks of the quality of the information being entered onto Oracle.

2.11.11 An **Unqualified** audit opinion has been given as the audit has found that the system of control is generally in place and any recommendations being made are to enhance the control environment.

### Section 3: 2010/2011 – School Audits Completed as at 31 Mar 2011

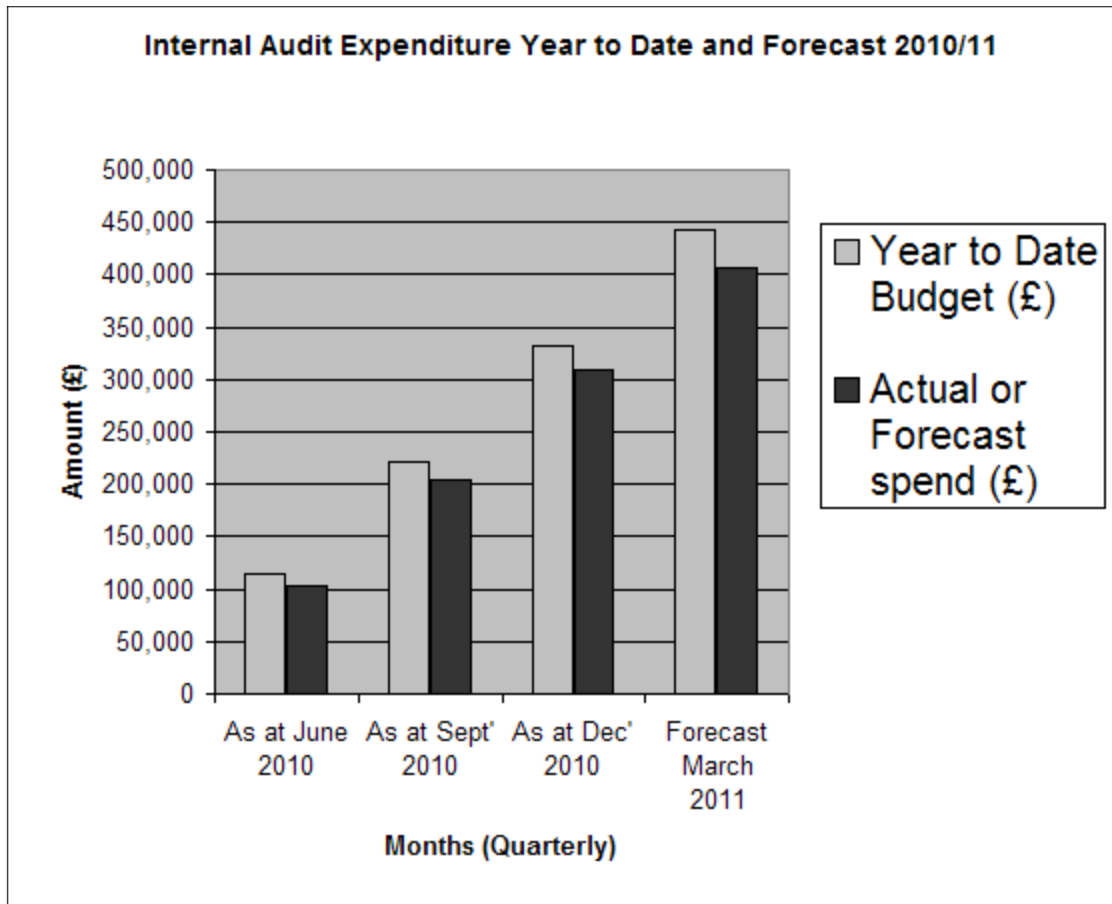
Report	Opinion	Recommendations			
		High	Med	Low	Total
Engayne Primary	Full			2	2
St Marys RC Primary	Substantial	2	4	5	11
Harold Court Primary	Substantial	1	7	1	9
Crownfield Junior	Substantial		4	3	7
Brookside Infant	Substantial		4	5	9
Towers Junior	Substantial		6	7	13
Mead Primary	Substantial		3		3
Whybridge Junior	Substantial		8	6	14
Benhurst Primary	Substantial		4	3	7
Squirrels Heath Infant	Substantial	1	3	1	5
Scargill Infant	Substantial		7	6	13
<b>Total</b>		<b>4</b>	<b>50</b>	<b>39</b>	<b>93</b>

Management summaries will only be included in the quarterly progress reports when we have given limited or no assurance during an audit. There are no school audits in this quarter that have given cause for concern.

**Section 4 Budget & Resource Information.**

Internal Audit (F620) 2010/11 Year to Date Expenditure and Forecast as at end March 2011

	<b>As at June 2010</b>	<b>As at Sept' 2010</b>	<b>As at Dec' 2010</b>	<b>Forecast March 2011</b>
Year to Date Budget (£)	113,623	221,330	332,280	442,660
Actual or Forecast spend (£)	102,291	204,036	308,700	405,901
Variance (£)	<b>-11,332</b>	<b>-17,294</b>	<b>-23,580</b>	<b>-36,759</b>



Quarter 1 variance due to expected delay in start of IT audits and therefore invoices.

Quarter 2 variance due to delay in receipt of IT audit invoices.

Quarter 3 variance due to the above plus additional income from schools

Quarter 4 variance due to under spend on Computer audits and the team carrying a vacancy.

## Section 5 Key Performance Indicators

The tables below detail the profiled targets for the year and the performance to date at the end of March 2011 (excluding schools).

<b>Audit Plan Delivered (%)</b>										
	<b>Q1</b>	<b>Jul</b>	<b>Aug</b>	<b>Sept</b>	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>
Actual	20	28	34	41	52	59	60	71	81	89
Cumulative Target	16	25	30	38	45	57	65	75	86	97

At the end of March 2011 the team is a little behind target with 89% of the audit plan having been delivered. This is not anticipated to have an affect on the overall target being reached as we are ahead of schedule for the issuing of final reports.

<b>KPI 01 - Briefs issued</b>										
	<b>Q1</b>	<b>Jul</b>	<b>Aug</b>	<b>Sept</b>	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>
Actual	24	32	40	42	49	49	53	53	56	57
Cumulative Target	16	23	28	35	42	49	52	55	57	57

It is estimated the team will undertake 57 audit assignments. The outputs of this work is reported in various ways to the committee depending on the type of work. Outputs from Fraud investigations are not counted in the 57. At the end of March the team had issued all 57 audit briefs.

<b>KPI 02 – Draft Reports</b>											
	<b>Q1</b>	<b>Jul</b>	<b>Aug</b>	<b>Sept</b>	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>
Actual	6	9	16	25	26	26	29	36	45	49	
Cumulative Target	7	11	16	22	28	32	37	38	45	51	57

<b>KPI 03 – Final Reports</b>											
	<b>Q1</b>	<b>Jul</b>	<b>Aug</b>	<b>Sept</b>	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>
Actual	4	7	11	16	23	24	25	32	40	46	
Cumulative Target	3	7	11	16	22	26	32	33	38	45	57

46 Final Reports had been issued at the end of March. This includes fraud proactive and non systems assurance work the outcomes of which are not included in this report.

## Schools Key Performance Indicators

The tables below detail the profiled targets for the year and the performance to the end of January.

<b>School Audit Plan Delivered (%)</b>							
	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>
Actual				38	62	88	
Cumulative Target			25	50	75	92	100

The team has completed 88% of the schools audit programme, slightly less than projected, in the main due to some minor delay in issuing reports earlier in the year.

<b>Briefs issued</b>						
	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>
Actual	2	4	9	15	15	15
Cumulative Target	2	5	8	12	15	15

<b>Fieldwork (site visit) completed</b>						
	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>
Actual	1	5	6	10	13	15
Cumulative Target	1	4	6	9	12	15

<b>Draft Reports</b>							
	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>
Actual			3	3	7	12	
Cumulative Target		3	6	8	10	13	15

<b>Final Reports</b>							
	<b>Oct</b>	<b>Nov</b>	<b>Dec</b>	<b>Jan</b>	<b>Feb</b>	<b>Mar</b>	<b>Apr</b>
Actual				3	4	11	
Cumulative Target			3	6	9	12	15

At the end of March the team had completed all site visits. This is the major aspect of the schools audit work taking 66% of the budget. Draft and Final reports were both just one report behind target but there is not anticipated to be any difficulty in having all reports issued by the end of April.

## **Section 6 – Changes to the Approved 2010/11 Audit Plan**

In March 2010 the Audit Committee approved an Annual Audit Plan for the 2010/11 financial year totalling 1530 days.

At the previous update committee were informed that deliverables had been reduced to 60 rather than 70. It has since been necessary to defer three pieces of work to 11/12. These are Transitions, Disabled Facility Grants and Welfare Benefits into Care reducing the number of deliverables to 57.



## Section 7 – Outstanding Recommendations Summary Tables

### Categorisation of recommendations

High: Fundamental control requirement needing implementation as soon as possible

Medium: Important Control that should be implemented

Low: Pertaining to Best Practice

### Outstanding Internal Audit Recommendations – 2008/09

Review in 2008/09	HoS Responsible	Outstanding			Position as at end Sept 10		
		High	Medium	Low	In Progress	Not Started	Position Unknown
E Payments	Business Systems		1		1		
Commissioning of Works	Asset Management	1			1		
IT Security & Data Management	Business Systems	1			1		
Telecommunications	Business Systems	1			1		
Homelessness, Hostels & Housing Aid	Housing & Public Protection		1		1		
Trading Standards	Housing & Public Protection	1			1		
Cemeteries & Crematorium	Housing & Public Protection		1		1		
<b>Total</b>		<b>4</b>	<b>3</b>	<b>0</b>	<b>7</b>		

E-Payments has a revised date of July 2011

Commissioning of Works has a revised date of July 2011

IT Security and Data Management has a revised date of June 2011

Telecommunications has a revised date of June 2011

Homelessness, Hostels and Housing Aid has a revised date of June 2011  
 Trading Standards has a revised date of April 2011  
 Cemeteries and Crematorium recommendation has been revised to April 2013

### Outstanding Internal Audit Recommendations – 2009/10

Review in 2009/10	HoS Responsible	Outstanding			Position as at end Sept 10		
		High	Medium	Low	In Progress	Not Started	Position Unknown
Integrated Youth Services	Children's and Young people		3	1	4		
Climate Change	Culture & Community		1		1		
Government Connect GCSx	Business Systems	3	2		5		
Contract Completion	Asset Management		1	1	2		
Integrated Children's Systems	Children's and Young People		1		1		
<b>Total</b>		<b>3</b>	<b>8</b>	<b>2</b>	<b>13</b>	<b>0</b>	<b>0</b>

Integrated Youth Services has revised dates of April 2011 for the medium recommendations and May 2011 for the low recommendation.  
 Climate Change has a revised date of April 2011  
 Government Connect GCSx has three high priority with revised dates of June, September and December 2011 and two medium with revised dates of July 2011  
 Contract Completion has due dates of June 2011  
 Integrated Children's Systems has one revised date of June 2011.

**Outstanding Internal Audit Recommendations – 2010/11**

Review in 2010/11	HoS Responsible	Outstanding			Position as at end June10		
		High	Medium	Low	In Progress	Not Started	Position Unknown
Private Sector Leasing	Culture & Community		2		2		
Corporate Support Team	Asset Management		1	1	2		
	<b>Total</b>		<b>3</b>	<b>1</b>	<b>4</b>	<b>0</b>	<b>0</b>

Private Sector Leasing - In progress update will be provided to Audit Committee by HoS  
 Corporate Support team have due dates of June 2011





## IMPLICATIONS AND RISKS

### **Financial implications and risks:**

By maintaining an adequate audit service to serve the Council, management are supported in the effective identification and efficient management of risks. Failure to maximise the performance of the service may lead to losses caused by insufficient or ineffective controls or even failure to achieve objectives where risks are not mitigated. In addition recommendations may arise from any audit work undertaken and managers have the opportunity of commenting on these before they are finalised. In accepting audit recommendations, the managers are obligated to consider financial risks and costs associated with the implications of the recommendations. Managers are also required to identify implementation dates and then put in place appropriate actions to ensure these are achieved. Failure to either implement at all or meet the target date may have control implications, although these would be highlighted by any subsequent audit work.

### **Legal implications and risks:**

There are no apparent legal implications arising from the noting of this report.

### **Human Resources implications and risks:**

Any HR implications arising from the implementation of these recommendations will be dealt with within the Council's existing HR policies and procedures.

### **Equalities implications and risks:**

None arising directly from this report

## BACKGROUND PAPERS

*None.*

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# AUDIT COMMITTEE

**Subject Heading:**

Annual Fraud Review

**Report Author and contact details:**

Paula Sisson  
Interim Internal Audit & Corporate Risk  
Manager  
Tel: 01708 - 433733.  
E-mail : paula.sisson@havering.gov.uk  
To update the committee on the annual  
review of the anti fraud and corruption  
arrangements

**Policy context:**

**Financial summary:**

N/A

**The subject matter of this report deals with the following Council Objectives**

Clean, safe and green borough	X
Excellence in education and learning	
Opportunities for all through economic, social and cultural activity	X
Value and enhance the life of every individual	X
High customer satisfaction and a stable council tax	X

**SUMMARY**

This report updates the committee on the annual review of the anti fraud and corruption arrangements which includes a review of the Council's strategy.

**RECOMMENDATIONS**

1. To comment on the findings of the review of anti fraud and corruptions arrangements.
2. To approve the revised Anti Fraud & Corruption Strategy.

## REPORT DETAIL

A review of the Anti Fraud and Corruption Strategy is planned annually. The most recent review was completed in April 2011.

The Council has a Benefit Investigation Section within Customer Services and a Fraud and Special Investigations Team within the Internal Audit service. Performance of both the Investigation teams is reported to the Audit Committee bi annually.

The teams aim to continuously develop and improve the services they provide to the Council and annually a formal review of the arrangements takes place. This year the review has been completed by the Interim Internal Audit & Corporate Risk Manager and the Benefits Manager.

### **Appendix 1. Anti Fraud & Corruption Review**

**Appendix 2. Anti Fraud & Corruption Strategy** - Only minor changes have been necessary, changes have been tracked.

## IMPLICATIONS AND RISKS

### **Financial implications and risks:**

Fraud and corruption will often lead to financial loss to the authority. By maintaining robust anti fraud and corruption arrangements and a clear strategy in this area, the risk of such losses will be reduced. Arrangements must be sufficient to ensure that controls are implemented, based on risk, to prevent, deter and detect fraud. The work of the Investigation teams often identifies losses which may be recouped by the Council. There are no financial implications or risks arising directly from this report.

### **Legal implications and risks:**

None arising directly from this report



**Human Resources implications and risks:**

None arising directly from this report

**Equalities implications and risks:**

None arising directly from this report

**BACKGROUND PAPERS**

Anti Fraud and Corruption Strategy 2009

The Red Book 2

Fraud Act 2006

Police and Criminal Evidence Act 1984

Regulation of Investigatory Powers Act 2000



## Appendix 1

**Fraud Review**

The areas of the review undertaken are outlined below, along with a brief update on findings and actions.

Area	Progress & Actions
<b>Strategies and policies – update and refresh</b>	<p>The review of the fraud strategy is complete and the confidential reporting policy was last reviewed in April 2011 [no changes necessary].</p> <p>The Housing and Council Tax Benefit Sanctions Policy was reviewed in January 2011.</p>
<b>Reporting Processes – content, frequency and recipients of reports</b>	<p>Audit Committee receive performance reports from the two teams at alternative quarterly meetings during the year.</p> <p>Performance indicators for Internal Audit are reported to CMT quarterly. The Benefit Investigation Section report on performance objectives in the Customer Service Performance Pack, on Havering Performs and submit returns to the Department for Work and Pensions.</p>
<b>Feedback from External Audit</b>	<p>Both the Internal Audit team and Benefit Investigation Section are subject to external audit review annually, as part of the Accounts work. Findings and recommendations are received by Senior Management and Members.</p>
<b>Liaison with other agencies</b>	<p>Links with other agencies have been strengthened substantially since the last review in September 2009. The Benefit Investigation Section have forged a close working relationship with the local police resulting in several arrests. Joint working with the DWP, HMRC and UK Borders Agency has also been very successful.</p> <p>The Internal Audit team has been working closely with Homes in Havering to combat tenancy fraud and the initiative was extended to all RSLs within the borough from 1 April 2011.</p>
<b>Fraud manual – update and refresh</b>	<p>The Internal Audit Fraud Manual was reviewed and updated in July 2010 whilst the Housing and Council Tax Benefit Fraud Manual is refreshed every two years or as required when legislative changes occur. The next refresh is due this year, 2011.</p>
<b>Awareness and training</b>	<p>Posters advertising the Fraud Hotline telephone number are located around the borough in key locations.</p>

Area	Progress & Actions
<b>programme</b>	<p>Note pads and drinks coasters with the current fraud poster logo and Fraud Hotline number are regularly distributed at events around the borough and were given out at recent Audit Committee anti-fraud training.</p> <p>In addition, the Fraud Hotline number is advertised in the Benefit Booklet that goes to 20,000 homes as part of annual billing.</p> <p>Fraud awareness sessions are run annually for Housing Benefits staff and front line services, including Homes in Havering.</p> <p>A new 'e' learning package focussing on corporate fraud issues has been rolled out to all managers and members of the Audit Committee. This will be rolled out to all staff in May 2011.</p>
<b>Structure of the team, direction of travel and succession planning</b>	<p>The fraud team in Internal Audit consists of three FTEs. There will be a full review of the structure of Internal Audit during 2011.</p> <p>The Benefit Investigation Section currently has eight FTE posts, including a Financial Investigator post that is a recent addition to the team. This officer will undertake financial investigations in order to confiscate assets (usually money) deemed to be proceeds of crime.</p> <p>The council has been awarded a further £100k grant for the next two years to tackle the issue of tenancy fraud across the borough. A recruitment exercise is underway to recruit two new investigators who will tackle tenancy issues such as sub-letting, false RTB and obtaining tenancies by deception. Included in this work will be investigations for and on behalf of local RSLs.</p>



# **ANTI FRAUD AND CORRUPTION STRATEGY**

Version: April 2011



**Havering**  
LONDON BOROUGH

## **ANTI FRAUD & CORRUPTION POLICY STATEMENT**

This Council requires Members, employees and contractors working on its behalf to act with honesty and integrity at all times, when dealing with resources owned by the Council or those for which it is responsible. This includes the responsibility for ensuring that assets are safeguarded and that procedures exist within areas of their responsibility to prevent and detect fraud.

Fraud is an ever-present threat to resources and hence must be of concern to everyone. The Council will rigorously enforce sanctions laid down in its "Disciplinary Procedures" and will seek prosecutions where necessary in order to deter fraudulent activity. The Council is unequivocal in its support of the Police and other external agencies fighting fraud and corruption within the public sector. We have already established arrangements for co-operation and joint working with outside bodies. In addition we actively foster relationships with external organisations for the purpose of introducing new initiatives to help combat fraud.

We recognise the important part our employees play in countering the damage that fraud can do if unchecked. We actively encourage the reporting of concerns about fraud and corruption and a "Confidential Reporting (Whistle Blowing) Policy" is available to address this.

**Cheryl Coppel**  
**Chief Executive**

## 1. INTRODUCTION

- 1.1 In carrying out its functions and responsibilities, the Council has always sought to adopt a culture of openness and fairness and has expected that elected members and employees at all levels will adopt the highest standards of propriety and accountability.
- 1.2 In adopting this strategy the Council seeks to demonstrate clearly that it is firmly committed to dealing with fraud and corruption and will deal equally with perpetrators from inside and outside the Council.
- 1.3 This strategy document embodies a series of measures designed to frustrate any attempted fraudulent or corrupt act and the steps to be taken if such an act occurs. For ease of understanding, it is separated into five areas:
- Culture Section 2
  - Prevention Section 3
  - Deterrence Section 4
  - Detection and investigation Section 5
  - Awareness and Training Section 6
- 1.4 The Council is also aware of the high degree of external scrutiny of its affairs by a variety of bodies such as the Audit Commission, the Local Government Ombudsman, HM Revenue and Customs and other inspection bodies. These bodies are important in highlighting any areas where improvements can be made.
- 1.5 Fraud and corruption are defined by the Audit Commission as:
- Fraud – *“the intentional distortion of financial statements or other records by persons internal or external to the Council which is carried out to conceal the misappropriation of assets or otherwise for gain”*.
- Corruption – *“the offering, giving, soliciting or acceptance of an inducement or reward which may influence the action of any person”*.
- Fraud can also be defined as *“the intentional distortion of financial statements or other records by persons internal or external to the Council which is carried out to mislead or misrepresent”*.
- This strategy also covers *“the failure to disclose an interest in order to gain financial or other pecuniary gain.”*
- 1.6 Fraud is an ever present threat to the resources available to the Council. It is unfair to honest residents, its perpetrators are criminals and their actions will not be tolerated.

## **2. CULTURE**

- 2.1 The culture of the Council has always been one of openness and the core values of accountability and probity support this. The Council's culture therefore supports its opposition to fraud and corruption.
- 2.2 The prevention/detection of fraud/corruption and the protection of the public purse are everyone's responsibility.
- 2.3 The Council's elected members and employees play an important role in creating and maintaining this culture. They are positively encouraged to raise concerns regarding fraud and corruption, immaterial of seniority, rank or status, in the knowledge that such concerns will, wherever possible, be treated in confidence.
- 2.4 Concerns must be raised when members or employees reasonably believe that one or more of the following has occurred;, is in the process of occurring; or is likely to occur:
- a criminal offence;
  - a failure to comply with a statutory or legal obligation;
  - improper unauthorised use of public or other funds;
  - a miscarriage of justice;
  - maladministration, misconduct or malpractice;
  - endangering of an individual's health and safety;
  - damage to the environment; and/or
  - deliberate concealment of any of the above.
- 2.5 Processes are also in place to ensure the public, contractors and partners of the Council are aware of the arrangements and feel confident highlighting concerns.
- 2.6 All allegations received, including anonymous allegations, will be taken seriously and will be risk assessed in line with the appropriate procedure before a decision is taken regarding the commencement of an investigation. All investigations will be conducted in line with relevant legislation and council policy.
- 2.7 The Council will deal firmly with those who defraud the Council, or who are corrupt, or where there has been financial malpractice. There is, of course, a need to ensure that any investigation process is not abused and, therefore, any such incidents (such as employees raising malicious allegations) may be dealt with as a disciplinary matter.
- 2.8 When fraud or corruption has occurred because of a breakdown or weakness in the Council's systems or procedures, Managers will ensure that appropriate



improvements in systems of control are implemented to prevent a reoccurrence.

### **3. PREVENTION**

#### **3.1 The Role of Elected Members**

- 3.1.1 As elected representatives, all members of the Council have a duty to citizens to protect the Council from all forms of abuse.
- 3.1.2 This is achieved by supporting the anti-fraud and corruption strategy, promoting a culture of openness and compliance with the national code of conduct for members, the Council's procedure rules and the relevant legislation.
- 3.1.3 Elected members sign to confirm that they have read and understood the national code of conduct when they take office. These conduct and ethical matters are specifically brought to the attention of members during induction and include the declaration and registration of interests. The Assistant Chief Executive, Legal and Democratic Services advises members of new legislative or procedural requirements.

#### **3.2 The Role of Managers**

- 3.2.1 Managers at all levels are responsible for the communication and implementation of this strategy in their work area. They are also responsible for ensuring that their employees are aware of the Council's policies, procedure rules, and that the requirements of each are being met in their everyday business activities. In addition, managers must make their employees aware of the requirements of the national code of conduct for local government employees through the induction process.
- 3.2.2 Managers are expected to strive to create an environment in which their staff feel able to approach them with any concerns they may have about suspected irregularities.
- 3.2.3 The Council recognises that a key preventative measure in dealing with fraud and corruption is for managers to take effective steps at the recruitment stage to establish, as far as possible, the honesty and integrity of potential employees, whether for permanent, temporary or casual posts.
- 3.2.4 The Council has a formal recruitment procedure, which contains appropriate safeguards on matters such as written references and verifying qualifications held. As with other public bodies, Criminal Records Bureau or appropriate checks are undertaken on employees. Further checks may be introduced in areas where an increased risk of potential fraud and corruption has been identified.

### **3.3 Responsibilities of Employees**

3.3.1 Each employee is governed in their work by the Council's procedure rules, Financial Framework, Procurement and Contract Rules and other codes of conduct and policies (e.g. Health and Safety, Business Systems Policy). They are also governed by the code of conduct for local government employees. Included in these are guidelines on gifts and hospitality and codes of conduct associated with professional and personal conduct and conflicts of interest. These are issued to all employees when they join the Council. All documents are also available to employees on the Council's intranet.

3.3.2 The Financial Procedure Rules clearly state:

“Every employee of the Council is responsible for reporting any matter that they believe to involve financial irregularity or misadministration in the Council's business, to their Group Directors, Assistant Chief Executive, Assistant Directors and Heads of Service, or directly to the Internal Audit & Corporate Risk Manager”.

3.3.3 In addition employees are responsible for ensuring that they follow the instructions given to them by management, particularly in relation to the safekeeping of the assets of the Council. These will be included in induction training and procedure manuals.

### **3.4 Responsibilities of Contractors and Partners**

3.4.1 The Council expects all of its contractors, suppliers and partner organisations and individuals to act with honesty and integrity and for appropriate governance arrangements to be in place.

3.4.2 In accordance with the Contract and Financial Rules, arrangements are in place, to have designated employees monitoring and controlling contracts. These employees will ensure contractors are aware of the arrangements in place for preventing fraud and corruption and the process by which concern can be raised. They will also ensure that terms of reference require contractors to co-operate with any investigation undertaken by Council officers. The Council will take relevant action where the anti-fraud approach is not deemed to be sufficiently rigorous.

3.4.3 Any person employed either through an agency on a temporary appointment, is expected to comply with the same rules as permanent employees within the organisation.

3.4.4 Partnership working is a key focus for the Council and key to the achievement of corporate objectives and goals. Responsibilities will regards reporting fraud and corruption as well as the means to do so will continue to be communicated during liaison meetings to ensure robust arrangements are in

place. The Council will reconsider its membership of a partnership where the anti-fraud approach is not deemed to be sufficiently rigorous.

### **3.5 Conflicts of Interest**

3.5.1 Both elected members and employees must ensure that they avoid situations where there is a potential for a conflict of interest. Such situations can arise with externalisation of services, tendering of contracts, planning and land issues, etc. Effective role separation will ensure decisions made are seen to be based upon impartial advice and avoid questions about improper disclosure of confidential information.

### **3.6 Role of Internal Audit**

3.6.1 Internal Audit is within the Finance and Commerce Directorate and it plays a vital preventative role in trying to ensure that systems and procedures are in place.

3.6.2 Internal Audit promotes an anti-fraud culture and zero tolerance to fraud via workshops, training and presentations.

3.6.3 It would be impossible to eradicate fraud completely and Internal Audit support management in considering risks within their areas, including the risk of fraud, and ensuring that appropriate controls are applied to prevent, deter and detect.

3.6.4 Internal Audit investigate cases of suspected irregularity, except welfare benefit, council tax and social tenancy fraud matters (see below), and liaise with management to recommend changes in procedures to prevent or mitigate further losses to the Council.

3.6.5 Internal Audit assists the Chief Financial Officer whose statutory role as S151 Officer requires him to ensure that the proper arrangements are in place to administer the Councils finances.

### **3.7 The Role of the Benefits Investigation Section**

3.7.1 The Benefits Investigation Section is responsible for the investigation of welfare benefit fraud, council tax irregularities and social tenancy fraud, in accordance with the requirements of relevant legislation. In cases where employees are involved, they will work with Internal Audit and senior management to ensure that correct procedures are followed and that this strategy is adhered to.

### **3.8 The Role of External Audit**

3.8.1 Independent external audit is an essential safeguard in the stewardship of public money. This role is delivered through the carrying out of specific reviews that are designed to test (amongst other things) the adequacy of the Council's financial systems, and arrangements for preventing and detecting

fraud and corruption. It is not the external auditor's function to prevent fraud and irregularity, but the integrity of public funds is at all times a matter of general concern. External auditors are always alert to the possibility of fraud and irregularity, and will act without undue delay if grounds for suspicion come to their notice. The external auditor has a responsibility to review the Council's arrangements to prevent and detect fraud and irregularity including arrangements designed to limit the opportunity for corrupt practices.

### **3.9 Co-operation with Others**

3.9.1 The Council will keep under review arrangements to develop and encourage the exchange of information on national and local fraud and corruption activity and as such links will be maintained with external agencies including:

- Metropolitan Police;
- London Audit Group;
- External Audit;
- Audit Commission;
- National Anti-Fraud Network;
- HM Revenue and Customs;
- Department of Works and Pensions;
- London Boroughs Fraud Investigation Group
- .

3.9.2 The Council will continue to participate in the National Fraud Initiative data matching exercise, which takes place every two years.

## **4. DETERRENCE**

### **4.1 Prosecution**

4.1.1 The Council has adopted a Benefits Sanction and Prosecution Policy and the Council's general prosecution policy is included within the Fraud Manual. This ensures consistency, whilst recognising that it may not always be in the public interest to refer cases for criminal proceedings.

### **4.2 Disciplinary Action**

4.2.1 Theft, fraud and corruption are serious offences against the Council and employees will face disciplinary action if there is evidence that they have been involved in these activities. Disciplinary action will be taken in addition to, or instead of, criminal proceedings, depending on the circumstances of each individual case, but in a consistent manner.

4.2.2 Members will face appropriate action under this strategy if they are found to have been involved in theft, fraud or corruption against the Council. Action will be taken in addition to, or instead of, criminal proceedings, depending on the

circumstances of each individual case, but in a consistent manner. Such cases, if not referred to the police, will be referred to the standards committee or group leader, as appropriate.

### **4.3 Publicity**

- 4.3.1 The Council's Head of Communications will optimise the publicity opportunities associated with anti-fraud and corruption activity within the Council. S/he will also ensure that the results of any action taken, including prosecutions, are appropriately reported via our internal and external publications.
- 4.3.2 In cases where financial loss to the Council has occurred, the Council will seek to recover the loss and where appropriate advertise this fact.
- 4.3.3 All anti-fraud and corruption activities, including the update of this strategy, will be publicised in order to make the employees and the public aware of the Council's commitment to taking action on fraud and corruption when it occurs.
- 4.3.4 Regular reports will be made to the elected members and in particular the Audit Committee about countering fraud and corruption activities and their success.

## **5. DETECTION AND INVESTIGATION**

- 5.1 Internal Audit plays an important role in the detection of fraud and corruption. Included in their Strategic plan are reviews of system financial controls and specific pro-active fraud and corruption tests, spot checks and unannounced visits.
- 5.2 In addition to Internal Audit, there are numerous systems controls in place to deter fraud and corruption, but it is often the vigilance of employees and members of the public that aids detection.
- 5.3 In some cases frauds are discovered by chance or 'tip-off' and arrangements are in place to enable such information to be properly dealt with.
- 5.4 All suspected irregularities are required to be reported (verbally or in writing) to the Internal Audit and Corporate Risk Manager either by the person with whom the initial concern was raised or by the originator. This is essential to the strategy, and:
  - ensures the consistent treatment of information regarding fraud and corruption;
  - facilitates a proper and thorough investigation by an experienced audit team.
- 5.5 Investigations undertaken by Internal Audit, or other appropriate Officers, must comply with codes of practice and other regulated powers. All interviews and gathering of evidence must be conducted in accordance with the Police and Criminal Evidence Act 1984 and the Regulation of Investigatory Powers Act 2000.

- 5.6 This process will apply to all the following areas:
- a) fraud/corruption by elected members
  - b) internal fraud/corruption
  - c) other fraud/corruption by Council employees
  - d) fraud by contractors and their employees
  - e) external fraud (the public).
- 5.7 Any decision to refer a matter to the police will be taken by the Internal Audit and Corporate Risk Manager and where appropriate following consultation with the Finance and Commerce Group Director and the Council's Monitoring Officer.
- 5.8 Depending on the nature of an allegation under b) to e), the Internal Audit and Corporate Risk Manager or the Principal Audit Manager, Fraud will normally work closely with the Director concerned and Human Resources to ensure that all allegations are thoroughly investigated and reported upon.
- 5.9 The Council's disciplinary procedures will be used where necessary to facilitate a thorough investigation of any allegations of improper behaviour by employees.
- 5.10 The use of technology is an essential tool for Internal Audit in detecting and identifying misuse and abuse of IT systems. Blue Coat is a web-based reporting tool that enables Internal Audit and Business Systems to run reports to investigate and identify Internet use of staff. A protocol is in place to ensure forensic examinations, either planned or random, are performed to a high level of confidentiality and securely.
- 5.11 All investigations are recorded on a case management system This allows management to, monitor investigations and receive regular performance reports

## **6. AWARENESS AND TRAINING**

- 6.1 The Council recognises that the continuing success of this strategy and its general credibility will depend in part on the effectiveness of programmed training and an awareness of elected members and employees throughout the Council.
- 6.2 To facilitate this, positive and appropriate provision has been made via induction for new employees. The Internal Audit and Corporate Risk Manager also manages the annual fraud awareness campaign and this includes specialist training for certain elected members and employees.
- 6.3 The Chief Executive also communicates with employees on a regular basis reminding them of the importance of being vigilant and alert to the effects of fraud and encouraging employees to report any matter of concern.

- 6.4 The Internal Audit & Corporate Risk Manager reports general fraud and corruption issues to Corporate Management Team and Risk Management Group to ensure management consider the implications of issues arising and ensure appropriate steps have been taken to prevent similar issues in other parts of the Council. Internal publications are also used to communicate issues and good news stories with regards the prevention or detection of fraudulent activity.

## **7. CONCLUSION**

- 7.1 The Council sets and maintains high ethical standards and a culture of openness, with core values of accountability and transparency. This strategy fully supports the Council's desire to maintain an honest Council, free from fraud and corruption.
- 7.2 The Council has in place a network of systems and procedures to assist it in dealing with fraud and corruption when it occurs. It is determined that these arrangements will keep pace with any future developments in techniques to both prevent and detect fraudulent or corrupt activity that may affect its operation.
- 7.3 The Council will maintain a continuous review of all these systems and procedures through Internal Audit.

## **8. STRATEGY REVIEW**

- 8.1 This strategy will be reviewed annually and presented for approval by the Audit Committee.
- 8.2 The next review will be completed in April 2012.

## **9. KEY CONTACTS**

Principal Audit Manager (Fraud) – Chris Nower ext 2617

Internal Audit & Corporate Risk Manager – Vanessa Bateman ext 3733

Benefits Manager – Chris Henry, ext 2413



# AUDIT COMMITTEE

**Subject Heading:**

**FRAUD PROGRESS REPORT**

**Report Author and contact details:**

Paula Sisson  
Internal Audit & Corporate Risk Manager  
Tel: 01708 - 433733.  
E-mail : paula.sisson@havering.gov.uk

**Policy context:**

To update the Committee on the actions taken against fraud and corruption.

**Financial summary:**

N/A

**The subject matter of this report deals with the following Council Objectives**

Clean, safe and green borough	X
Excellence in education and learning	X
Opportunities for all through economic, social and cultural activity	X
Value and enhance the life of every individual	X
High customer satisfaction and a stable council tax	X

**SUMMARY**

To advise the Committee of anti fraud and corruption work undertaken by the internal audit team during the period 1 October 2010 to 31 March 2011.

**RECOMMENDATIONS**

1. To note the contents of the report.
2. To raise any issues of concern and ask specific questions of officers where required, either with regards the cases highlighted or the performance of the team.

## REPORT DETAIL

The progress report contains three sections; the content of each section is outlined below:

### **Section 1. Fraud Work October to March**

- A) Table of 'Fraud Hotline' reports.
- B) Table of completed cases.
- C) Work in progress as at end of September.
- D) Details of savings and losses for the period.

### **Section 2. Key Performance Indicator**

The results for the fraud specific key performance indicator are presented in this section of the report. Other key Performance indicators are reported quarterly as part of the Internal Audit Progress report.

### **Section 3. National Fraud Initiative 2008/9 Summary**

Update on work on the NFI 2008/9

## IMPLICATIONS AND RISKS

### **Financial implications and risks:**

Fraud and corruption will often lead to financial loss to the authority. By maintaining robust anti fraud and corruption arrangements and a clear strategy in this area, the risk of such losses will be reduced. Arrangements must be sufficient to ensure that controls are implemented, based on risk, to prevent, deter and detect fraud. The work of the fraud team often identifies losses which may be recouped by the Council. There are no financial implications or risks arising directly from this report.

### **Legal implications and risks:**

None arising directly from this report

### **Human Resources implications and risks:**

None arising directly from this report

**Equalities implications and risks:**

None arising directly from this report

**BACKGROUND PAPERS**

None.

**Section 1 Fraud Work 1<sup>st</sup> October 2010 to 31 March 2011**

**A) Fraud Hotline Reports Received**

<b>CALLER</b>	<b>CALL CONTENT</b>	<b>DETAILS / RESULT OF INVESTIGATION</b>
Member of the public	Tenant no longer living at property but may still be claiming Housing Benefits.	Tenant registered as leaving property on 10/04/10, HB also ceased. No further action required.
Anonymous	Alleged Member of Staff falsely claiming hours spent not working.	Internal Audit to investigate. Following covert surveillance management have been presented with sufficient evidence to conduct a disciplinary hearing.
Anonymous	Alleged claiming SPD and Housing Benefits but lives with someone and is working.	Issued to HB Fraud. Investigated and no case to answer.
Anonymous	Caller alleged SPD being claimed but two persons living at address.	Issued to HB Fraud and Council Tax. Investigated and no case to answer. Property sold.
Anonymous	Caller alleged SPD being claimed but partner and four children living at address.	Issued to HB Fraud and Council Tax. Case closed as fraud can not be proven.
Anonymous	Alleged non payment of Council Tax.	Issued to Council Tax for further enquiries.
Member of public	Alleged letting of property.	Issued to HB Fraud to monitor if claims received from family. No benefits in payment.
Anonymous	Alleged claiming of HB and CT by single parent now living with partner.	Issued to HB Fraud. In progress
Anonymous	Council tenant attempting to Sub Let or buy property.	Issued to Homes in Havering.
Anonymous	Tennant claiming housing benefit on a property owned by her mother.	Issued to HB Fraud. In progress
Anonymous	Alleged claiming of benefit but working.	Issued to HB Fraud. In progress

CALLER	CALL CONTENT	DETAILS / RESULT OF INVESTIGATION
Anonymous	Alleged claiming of SPD but lives with someone.	Passed to London Borough of Redbridge Fraud Section.
Member of public	Possible misappropriation of college funds.	To be investigated by the Governing Body and auditors.
Anonymous	Alleged Non declaration of employment whilst claiming Full benefits.	Issued to HB Fraud. Claim suspended. Case closed
Anonymous	Alleged resident is receiving SPD but had not declared new living arrangement.	No case to answer

**B) Completed Cases**

38 cases were completed and closed during the period 1 October 2010 to 31<sup>st</sup> March 2011.

CEX = Chief Executive  
 F&C = Finance & Commerce  
 C&C = Culture & Community  
 SC&L = Social Care & Learning  
 H in H = Homes in Havering  
 L&D = Legal and Democratic Services

<b>Job Code</b>	<b>Audit Name</b>	<b>Directorate</b>	<b>Type of Audit</b>	<b>Result of Audit</b>
T8raak	Claims of mis management	CEX	General fraud issues	Management Action Plan
T8raaz	Document review for vehicle usage for Council business	CEX	Breach of Council Procedures	Management Action Plan
T8raap	Review of Highways contracts	C & C	Breach of Council Procedures	Management Action Plan
T8raaq	Management of amenity facility	C & C	Miscellaneous	No further action required
T8raav	Laptop abuse	C & C	PC – misuse and abuse	No further action required
T8saaf	Alleged breach of Council procedures and mis use of Council time.	C & C	Misuse of Council time	Contract ceased.
T8saah	Alleged involvement by member of staff in family benefit claim	C & C	Breach of Council procedures	Insufficient Evidence
T8saai	Possible Internet abuse	C & C	PC abuse	No case to answer
T8paar	Allegations TMO mis-management	C & C	Homes in Havering	Management Action Plan
T8qaaz	Leaseholders – Proposed itemised works	C & C	Homes in Havering	Insufficient evidence
PA0048	Purchasing Strategies	F & C	Pro active	Management Action Plan
PA0054	Training Courses – Non Attendance	F&C	Pro active	Management Action Plan

<b>Job Code</b>	<b>Audit Name</b>	<b>Directorate</b>	<b>Type of Audit</b>	<b>Result of Audit</b>
PA0056	Banking arrangements	F&C	Pro active	Management Action Plan
T8maa	National Fraud Initiative 2008/09	F & C	NFI	Investigations and recovery
T8qaaf	Review of Business Systems Policy Version 4	F & C	Miscellaneous	Issued
T8qaag	Whistleblowing hotline	F & C	Miscellaneous	Nine cases
T8qaah	Fraud Hotline	F & C	Miscellaneous	41 cases
T8qaai	Advice to Directorates	F & C	Miscellaneous	Not applicable
T8qaai	Advice to other LA's	F & C	Miscellaneous	Not applicable
T8raam	Possible Internet abuse	F & C	PC misuse and abuse	Member of staff dismissed
T8raar	Confirmation of professional qualifications	F & C	Falsification of records	Management Action Plan
T8raat	Cheque fraud	F & C	Cheque changed by third party	Refund paid by Bank
T8raau	Review GroupWise activity	F & C	PC misuse and abuse	Insufficient evidence
T8raax	Possible Internet abuse	F & C	PC misuse and abuse	Management Action Plan
T8saab	Alleged unauthorised use of car park pass	F&C	Falsification of records	Insufficient evidence
T8saad	Payroll information	H in H	Miscellaneous	Reports produced
T8qaal	Review of personal Internet use	L & D	PC misuse and abuse	Management Action Plan
T8raah	Review of Internet usage	L & D	PC misuse and abuse	Staff dismissed
T8raaj	Review of personal Internet use and flexi records	L & D	PC misuse and abuse	Member of staff resigned
PA0047	Review Homecare Providers	SC&L	Pro active	Management Action Plan
T8paac	Review financial management – Day Centre	SC&L	General Fraud issues	Management Action Plan

<b>Job Code</b>	<b>Audit Name</b>	<b>Directorate</b>	<b>Type of Audit</b>	<b>Result of Audit</b>
T8qaax	Alleged misuse of older persons finances	SC&L	General Fraud issues	Insufficient evidence
T8raaf	Alleged PC, Internet and abuse of working times	SC&L	PC misuse and abuse	Insufficient evidence
T8raan	Disciplinary hearing	SC&L	Breach of Council procedures	Member of staff dismissed
T8raas	Review of laptop contents	SC&L	PC misuse and abuse	Insufficient evidence
T8raay	Possible misappropriation/ theft of monies	SC&L	Theft of monies	Member of staff resigned
T8saac	Alleged misappropriation of income	SC&L	Falsification of records	Insufficient evidence – Management Action Plan



### C) Work In Progress as at 31<sup>st</sup> March 2011

At the end of March 2011 there were 16 cases in progress.  
The table below indicates the case by name.

Code	Audit Name
PA0055	Home Ownership
PA0057	Honoraria
T80aai	E learning – Focus on Fraud
T8qaaa	Internet Abuse
T8qaau	NFI 2010/11
T8raag	Costs relating to Day Centres
T8raaw	Mis use of Council time – Transport Services
T8saaa	Overpayment of pension to deceased member
T8saae	Review of Overtime
T8saag	Alleged mis-management of personal finances
T8saaj	Alleged inappropriate images on laptop
T8saak	Allegation re various grant payments
T8saal	Review of flexi, annual leave and working from home procedures
T8saam	Review of Citrix reports
T8saan	Possible misuse and abuse Internet
T8saao	Possible misuse and abuse Internet

There are also additional assignments which are ongoing throughout the financial year. These tasks include:

- Fraud Awareness Training - E-learning Fraud and Corruption Awareness training;
- Fraud Awareness Campaign;
- Requests from other Local Authorities and Government Agencies;
- Whistleblower Reports;
- Fraud Hotline Reports;
- Advice to Directorates;
- Bluecoat Internet forensic software discussions;

## D) Savings and Losses

When a fraud is committed there may be two elements to the financial consequences. The table below details the losses identified in the period 1<sup>st</sup> October 2010 to 31<sup>st</sup> March 2011 and the case details.

Definitions of terms in table:

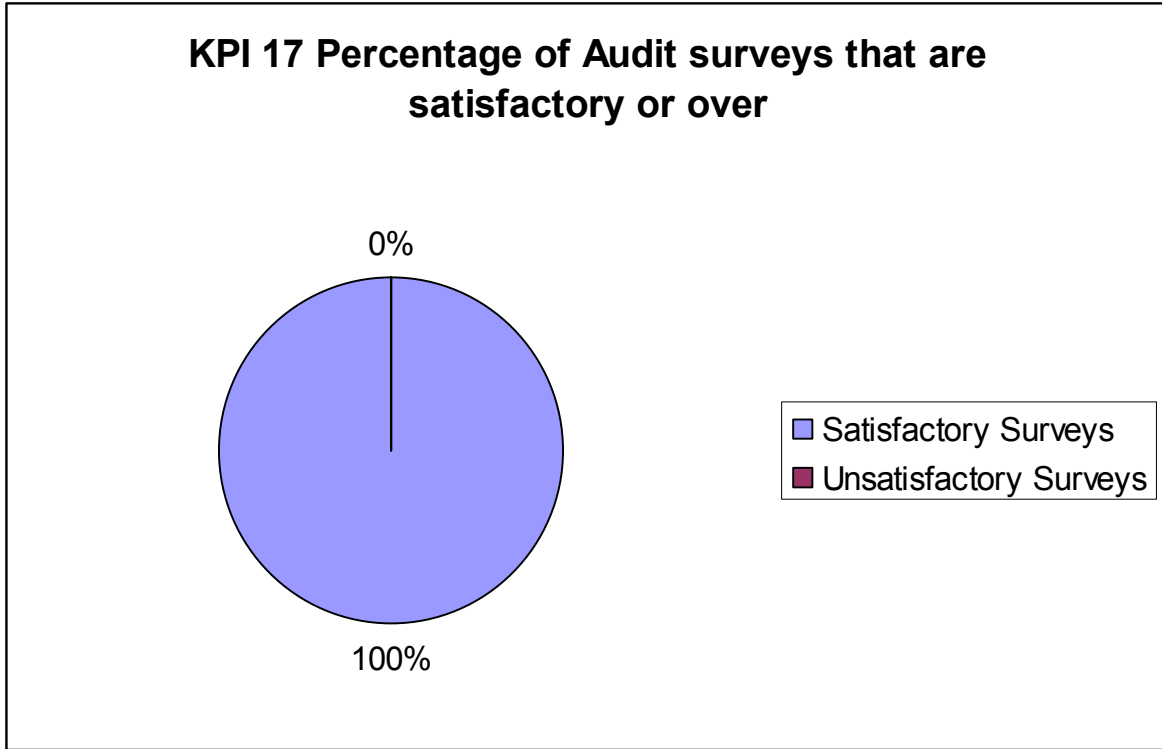
**Losses** - These are the sums of money that the audit determined have been lost or stolen.

**Savings** - refer to the amounts of money that the detection of the fraud has prevented being lost. A prime example of this would be the discount on a right to buy. If we prevent the sale then we prevent the discount being given and thereby we save the Council money.

**Management to recover** - These are the actual sums of money which management can take action to recover from those "lost".

Case details	Savings identified	Losses Identified	Management to recover	Details
Day Centre – Bank account and expenses	1,749	1,078	2,827	
Alteration of cheque details		202	202	Third party intercepted cheque and change payee. Bank repaid amount.
Misappropriation of monies		5112		Due to the lack of complete records Internal Audit are unable to properly account for monies received.
Additional charges and loss of income		518	473	Overpayment of bank charges and lack of income.

**Section 2 Key Performance Indicator**



All surveys returned were satisfactory and above.

## **Section 3 National Fraud Initiative (NFI) 2008/09 Summary Report.**

### **Introduction**

The National Fraud Initiative (NFI) is a data matching exercise designed to help participating bodies identify possible cases of fraud and detect and correct any consequential under or overpayments from the public purse. It has been run every two years since 1996 and, to date, has been used to identify fraud and overpayments totalling nearly £450 million.

The core of the NFI is the matching of data to help reduce the level of Housing and Council Tax Benefit fraud, Payroll and Occupational Pension fraud and Housing Tenancy fraud. All government bodies are required to provide mandatory and risk based data sets.

### **Results of matches**

A programme of key dates and actions were set out in order that the Council could fully participate in the 2008/09 exercise and once again, the exercise has proven successful with overpayments, fraud and financial savings having been identified. The overall summary is as follows;

- Cases processed – 5,135
- Investigated – 829
- Cleared – 5089
- Frauds – 23
- Errors – 23
- Total - £264,318.90
- Cases for recovery – 10
- Amount recoverable - £65,557.73

### **Headline results for NFI 2008/09 - Housing & Council Tax Benefit**

- Benefit Fraud investigations identified overpayments of £158,380 and Income Support/Job Seeker Allowance of £42,554.
- There were 19 cases of fraud and four cases due to Council error which resulted in two prosecutions, seven administrative penalties and one official caution.

The Housing Benefit overpayment cases can be broken down as follows:

- Students claiming HB/CTB that they were not entitled to – three cases, value £7,116
- NHS employees, work not declared on claim – three cases, value £12,272

- Local government employees, work not declared on claim – 11 cases, value £121,564
- Local government pensioners, claiming HB having either not declared or under-declared their pension – three cases, value £59,982

### **Headline Results for NFI 2008/09 - Non Benefit Matters**

- Three cases where an occupational pension continued to be paid after the death of the pensioner with associated overpayments of £340, which were recovered.
- Two cases of un-abated pensions causing subsequent overpayments of £9,139 which were recovered.
- One council property was recovered as a result of detected tenancy fraud.
- One employee was dismissed where the investigation confirmed that the employee was working for another employer whilst registered sick with the Council. The employee also repaid an overpayment of £1,124.
- 743 deceased persons' blue badges being cancelled.
- One employee was dismissed as a failed asylum seeker who had no entitlement to work in the United Kingdom. The value of the salary paid (inc. on-costs) totalled £51,973 of which superannuation and national insurance contributions amounting to £17,459.67 were recovered.

### **Reporting results to the Audit Commission**

The reports are now web based and this enables the Council to review and update records instantly. The Audit Commission were able to monitor the performance of each authority and met with the Council's Key Contact to discuss our performance. There were no adverse comments received following the meeting with the Audit Commission who have complimented the Council on the work undertaken.

### **Costs**

It is estimated the staff cost of investigating the resulting data matches was approximately £22,000. The most significant costs being generated by the Internal Audit and Housing Benefit Fraud Teams. As in previous years an NFI fee is set for each type of audited body based on the number and range of core datasets applicable and the cost to the Council was £4,150.

The NFI is run over a two year period and the fees paid and staff costs covers the two financial years 2008/09 and 2009/10.

### **Conclusion**

The results during the past years have demonstrated that the NFI exercise is effective and is an additional tool which enhances the Council's ability to identify fraud which is not otherwise available.

The matching exercise continues to highlight overpayments, fraud and subsequent savings for the Council although the work involved is time consuming.

The Key Contact has provided regular feedback to the Audit Commission regarding the functionality of the web based application and the content of reports in order to assist in improvements for subsequent exercises.

# AUDIT COMMITTEE

**Subject Heading:**

**ANNUAL REVIEW OF THE COUNCIL'S  
WHISTLEBLOWING ARRANGEMENTS**

**Report Author and contact details:**

**Paula Sisson**  
**Interim Internal Audit & Corporate Risk  
Manager**  
**Tel: 01708 433733**  
E-mail: paula.sisson@havering.gov.uk

**Policy context:**

To update the Committee on the  
arrangements in place and report on  
activity in 2010/11.

**Financial summary:**

N/A

<b>SUMMARY</b>
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Robust arrangements regarding Whistleblowing, also known as 'Confidential Reporting', is a key in maintaining effective governance arrangements within the Public Sector. It is a process used to "empower the honest majority" in the fight against fraud and corruption.

The review of the Council's Whistleblowing arrangements was undertaken in March 2011, by the Interim Internal Audit & Corporate Risk Manager (IA&CRM). No specific actions have arisen from the review.

London Borough of Havering received 10 Whistleblowing reports during the period April 2010 – March 2011.

<b>RECOMMENDATIONS</b>
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- 1 To note the contents of the report.

<b>REPORT DETAIL</b>
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1. **Whistleblowing Arrangements**

1.1 The details of the Whistleblowing reports received in 2010/11 are contained in the table below.

1.2 The Whistleblowing information is located with the Human Resources policies and procedures on the intranet. All new starters to the organisation receive a copy of the policy as part of their induction pack, which they are asked to sign a declaration indicating they have received and read. Reminders are sent to all staff in year via team briefs and pay slip messages. Information on Whistleblowing is also included within the manager's induction days and other training/awareness workshops.

	<b>How Received</b>	<b>Description</b>	<b>Action taken</b>
1	Email	Concerns regarding external commitments of member of staff	Member of staff has been spoken to with regards to future conduct.
2	Member of Staff	Allegation of use and misuse of computer	Internal Audit carried out forensic examination of PC. No case to answer.
3	Anonymous	Allegation of misuse of internet and abuse of time recording	Internal Audit investigation. In progress.
4	Anonymous Letter	Concerns raised relating to day centres	Internal Audit investigation in progress
5	Member of Staff	Concerns re. the employment of a relative	Internal Audit review of recruitment process. No case to answer
6	Anonymous	Concerns re. payment of members allowance and HB claims	DWP investigation in progress
7	Member of staff	Concerns relating to flexi records	Review of flexi sheets and car park logs carried out. Warning issued to staff member.



	<b>How Received</b>	<b>Description</b>	<b>Action taken</b>
8	Anonymous	Allegations of misuse and abuse of internet during working hours	Internal Audit investigation carried out member of staff dismissed.
9	Anonymous	Allegations of abuse of working hours and failure to follow council procedures	Internal Audit investigation carried out agency workers contract ended.
10	Anonymous	Alleged abuse of working time.	Internal Audit Investigation in progress.

1.3 The 10 Whistleblower reports in the period compares to 6 received during 2009/10.

## IMPLICATIONS AND RISKS

### **Financial implications and risks:**

Fraud and corruption will often lead to financial loss to the authority. By maintaining robust anti fraud and corruption arrangements and a clear strategy in this area, the risk of such losses will be reduced. Arrangements must be sufficient to ensure that controls are implemented, based on risk, to prevent, deter and detect fraud. The work of the fraud team often identifies losses which may be recouped by the Council. There are no financial implications or risks arising directly from this report.

### **Legal implications and risks:**

None arising directly from this report.

### **Human Resources implications and risks:**

None arising directly from this report.

**Equalities implications and risks:**

None arising directly from this report.

**BACKGROUND PAPERS**

None.



# AUDIT COMMITTEE

**Subject Heading:**

Annual Report of Audit Committee

**Report Author and contact details:**

Paula Sisson  
Interim Internal Audit & Corporate Risk Manager  
Tel: 01708 - 433733.

**Policy context:**

E-mail : paula.sisson@havering.gov.uk  
The Annual report of the work of the Audit Committee

**Financial summary:**

N/A

**The subject matter of this report deals with the following Council Objectives**

- Clean, safe and green borough X
- Excellence in education and learning X
- Opportunities for all through economic, social and cultural activity X
- Value and enhance the life of every individual X
- High customer satisfaction and a stable council tax X

**SUMMARY**

In accordance with best practice the Committee submits an annual report to the Council on the work of the Committee. The Draft report is attached at appendix 1.

## RECOMMENDATIONS

1. To comment on the draft report.
2. To agree the final report should be presented to the next appropriate Council Meeting.

## REPORT DETAIL

### **Annual Report 2010/11**

The report contains the following information

- Information;
- Background;
- Structure;
- Coverage;
- Key issues arising/considered;
- Work to ensure effectiveness; and
- Priorities for forthcoming year.

Key highlights from the report are:

- The Committee maintained its usual work plan based on its Terms of Reference but also considered specific reports and assurances on: Treasury Management, International Financial Reporting Standards (IFRS); an objection to the council's accounts and Former Tenant arrears on PSLs.
- The Committee received training on Treasury Management, Risk Management, Fraud and Corruption, the role of Audit Committee and Accounting Principles.
- Appendix A of the report details agenda items considered at each meeting.

## IMPLICATIONS AND RISKS

### **Financial implications and risks:**

None directly arising from this report, however the existence of an effective Audit Committee is fundamental in ensuring the Council maintains a robust system of internal control. Failure of the Audit Committee to undertake its duties in an effective manner may result in issues that arise not being addressed.

### **Legal implications and risks:**

None arising directly from this report

### **Human Resources implications and risks:**

None arising directly from this report

### **Equalities implications and risks:**

None arising directly from this report

## BACKGROUND PAPERS

None





**ANNUAL REPORT ON THE  
WORK OF  
THE AUDIT COMMITTEE**

**April 2011**

## **1. Introduction**

1.1 This report covers the period April 2010 to March 2011 and outlines:-

- Information relating to the Audit Committee;
- The coverage of work undertaken by the Audit Committee;
- Key issues arising;
- Actions taken during the year, including training, to ensure the effectiveness of the Audit Committee; and
- Future planned work and challenges.

## **2. Background**

2.1 The Audit Committee has been in place for a number of years and has as its terms of reference:

- To consider and monitor the Authority's risk management and internal control environment.
- To focus audit resources.
- To receive and approve the Annual Statement of Accounts.
- To monitor performance of internal and external audit.
- To monitor proactive fraud and corruption arrangements.

## **3. The Audit Structure**

Audit Committee     Cllr Georgina Galpin (Chair from May 2011)  
                              Cllr Osman Dervish  
                              Cllr Roger Ramsey  
                              Cllr Frederick Thompson  
                              Cllr Clarence Barrett  
                              Cllr Paul McGeary

Internal Auditors     Internal Service

External Auditors     PricewaterhouseCoopers

## **4. Audit Committee coverage**

4.1 The Audit Committee has received the reports as set out in Appendix A. The coverage can broadly be categorised as regular and specific. More information on both is set out below.

### **4.2 Regular Work**

The Committee has regularly reviewed:

- Progress against the audit plan and performance;
- Key findings/issues arising from each audit undertaken;
- Progress against implementation of the recommendations;
- Anti fraud and corruption activity, including frauds identified;
- The Corporate Risk Register; and
- Progress against External Audit's Plan.



**4.3 Specific Review / Reports**

There were several during the year including a review and approval of:

- the Risk Management Strategy;
- the Anti Fraud and Corruption Strategy;
- the Statement of Accounts including Annual Governance Statement;
- the Internal Audit Strategy; and
- the Annual Audit Plan,

The Committee also received assurances via:

- Annual Report from Internal Audit;
- The work of External Audit;
- Annual report on schools audit activity and findings;

**5. Key issues arising**

- 5.1 Members of the Audit Committee have been regularly briefed on the objection to the Statement of Accounts by a resident and the subsequent enquiry by PwC.
- 5.2 Members expressed concerns regarding the number of outstanding audit recommendations and were subsequently briefed on a successful exercise to clear these.
- 5.3 Debt recovery in Private Sector Leasing was highlighted as an issue. Members were briefed by the Head of Housing and Public Protection on this matter and will continue to receive regular briefings
- 5.4 The Committee received regular reports from Officers on the progress against the implementation of the International Financial Reporting Standards and on Treasury Management matters.

**6. Work to ensure effectiveness of Committee**

- 6.1 The Committee has received dedicated training and awareness sessions on, The role of Audit Committee, Treasury Management, Risk Management, and Fraud and corruption during the year.
- 6.2 In February the annual review of the committee's effectiveness was undertaken. The Committee completed a self assessment against CIPFA best practice guidance and noted the outcome and areas for possible improvement. No significant issues arose as a result of this exercise.
- 6.3 The Chairman met with the Internal Audit and Corporate Risk Manager during the year to gain assurance regarding the independence of the team and to advise that direct channels of communication are accessible should they be needed.

**7. Priorities and work plan for the forthcoming year**

- 7.1 The Audit Committee is currently planned to meet on five occasions over the next municipal year. There are specific reports planned throughout the year, running through a mix of quarterly progress reports and annual reviews of specific strategies and policies within the remit of the Committee, together with progress reports from the Council's external auditor.
- 7.2 Officers will ensure any new members on the Committee in the new municipal year are adequately trained in their new role.
- 7.3 All members of the Committee will continue to be briefed regarding the implications of the change to compliance with the International Financial Reporting Standards as this will be necessary to allow the Committee to fulfil its role in approving the accounts.
- 7.4 The Committee will be involved in the consultation process regarding "The Future of Public Audit"
- 7.5 Committee will continue to focus on ensuring Value for Money and challenging weak areas that have been highlighted by the work of Internal Audit.

**AUDIT COMMITTEE AGENDA ITEMS  
FROM APRIL 2010 TO DATE**

**13th April 2010**

- Benefit Subsidy Grants Report
- Internal Audit Charter and Terms of Reference
- Internal Audit Interim Progress Report
- Annual Review of Whistleblowing Arrangements
- CRB
- Urgent Business

**23<sup>rd</sup> June 2010**

- Annual Statement of Accounts 2009/10 containing Annual Governance Statement
- Annual Audit Letter
- External Audit Fee Letter
- External Audit Progress Report
- Annual Treasury Management
- Annual Head of Internal Audit Report
- Internal Audit Progress Report
- CRB
- Urgent Business

**23<sup>rd</sup> September 2010**

- Annual Statement of Accounts
- Housing and Council Tax Benefit Fraud update
- Internal Audit Progress Report
- Annual Review of Schools Internal Audit 2009/10
- Treasury Update
- Urgent Business

**7th December 2010**

- Update on objection to the Accounts
- Annual Audit Letter
- IFRS Accounts closedown update
- Annual Review of Risk Management arrangements
- Internal Audit Progress Report
- Annual Review of Risk Management Arrangements
- Fraud Progress Report
- AGS update report
- Treasury Management Strategy and Update
- Urgent Business

**1<sup>st</sup> March 2010**

- Update on Objection to Accounts Action Plan
- External Audit Plan
- Housing Benefit Fraud Progress Report
- Annual Review of the Audit Committees Effectiveness
- Internal Audit Progress Report
- Internal Audit Charter and TOR

- Internal Audit Plan 11/12 and Strategy
- Grants Report
- IFRS Update
- Urgent Business

**APPENDIX B**

**AUDIT COMMITTEE MEMBERS TRAINING / AWARENESS**

<b>Timescale</b>	<b>Session</b>	<b>Coverage</b>
June 2010	Session 1	Annual Accounts
September 2010	Session 2	The Role of Audit Committee
November 2010	Session 3 (not linked to Committee Meeting)	Treasury Management
December 2010	Session 4	Risk Management
March 2011	Session 5	Fraud and Corruption
May 2011	Session 6	Schools Finance and Audit Programme.

**AUDIT COMMITTEE – FORWARD PLAN / TRAINING**

<b>FORWARD PLAN</b>	<b>AGENDA ITEM</b>	<b>PLANNED TRAINING</b>
23 <sup>rd</sup> June 2011	<ul style="list-style-type: none"> <li>• Annual Accounts - TBC</li> <li>• AGS - TBC</li> <li>• External Audit Fee Letter</li> <li>• Annual Letter 2010/11</li> <li>• External Audit Progress Report</li> <li>• Internal Audit Progress Report</li> <li>• Money laundering annual review</li> <li>• Head of Audit Annual Report and Opinion</li> <li>• Treasury Management Report</li> </ul>	Shared Services – TBC
September 2011	<ul style="list-style-type: none"> <li>• Annual Accounts</li> <li>• External Audit Annual Plan</li> <li>• Internal Audit Progress Report inc Outstanding Recommendations Report</li> <li>• Housing Benefit Fraud Progress Report</li> <li>• Annual School Report</li> </ul>	Annual Accounts - TBC
December 2011	<ul style="list-style-type: none"> <li>• Annual Review of Risk Management Arrangements</li> <li>• Annual Audit Letter</li> <li>• Internal Audit Progress Report</li> <li>• Fraud Progress Report</li> <li>• Treasury Management Report</li> </ul>	Treasury Mgt Refresher (Nov) TBC  Risk Management & Assurance - refresher
March 2012	<ul style="list-style-type: none"> <li>• External Audit 11/12 Plan</li> <li>• Internal Audit Draft 12/13 plan and strategy.</li> <li>• Internal Audit progress report</li> <li>• Housing Benefit Fraud Progress Report</li> <li>• Annual Review of Audit Committee Effectiveness</li> <li>• Internal Audit Charter and Terms of Reference</li> <li>• Annual Grants review</li> <li>•</li> </ul>	Fraud and corruption update
April 2011	<ul style="list-style-type: none"> <li>• Interim Internal Audit Progress Report</li> <li>• Whistle blowing</li> <li>• Annual Report of Audit Committee</li> <li>• Fraud progress report inc. NFI update</li> </ul>	TBC

**GOVERNANCE  
COMMITTEE**

**REPORT**

11 MAY 2011

**Subject Heading:**

Future of Local Public Audit –  
Government Consultation

**Report Author and contact details:**

Mike Stringer  
Head of Finance & Procurement  
[Mike.stringer@havering.gov.uk](mailto:Mike.stringer@havering.gov.uk)  
01708 432101

**Policy context:**

To consider the Government’s  
consultation document on the future of  
local public audit and to approve the  
Council’s response to it

**Financial summary:**

There are no immediate financial  
consequences from the consultation,  
although changes to the landscape of  
public audit will inevitably create financial  
implications

**The subject matter of this report deals with the following Council Objectives**

- Clean, safe and green borough
- Excellence in education and learning
- Opportunities for all through economic, social and cultural activity
- Value and enhance the life of every individual
- High customer satisfaction and a stable council tax

**SUMMARY**

This report sets out a summary of the Government’s consultation document on the future of local public audit and includes a draft response for comment on and approval by the Committee.





independent auditor. This appointment would be made on the advice of an independent audit committee. Auditors would be regulated under a system which mirrors that of the audit of companies with a role for the Financial Reporting Council and the professional audit bodies. DCLG envisages that the National Audit Office will set the code of audit practice and have put forward options for the scope of audit in the new framework.

5. The consultation asks a number of questions, 50 in total, of which a number relate to two-tier authorities and smaller authorities, on which DCLG is seeking responses.
6. The consultation document is divided into 6 sections and is attached at Appendix A; a summary of each section follows, together with comments on the proposals:
  - Introduction
  - Regulation of local public audit
  - Commissioning local public audit services
  - Scope of audit and the work of auditors
  - Arrangements for smaller bodies
  - List of consultation questions.

#### *Regulation of Local Public Audit*

7. The Audit Commission is currently responsible for setting audit standards through codes of practice for local government (and health) bodies. Once the Commission has been abolished, local public audit will need to be regulated differently. The consultation paper proposes a regulatory system for local public audit that is similar to that for private company audit under the Companies Act 2006. The consultation proposes that:
  - The National Audit Office would develop and maintain codes of audit practice and any supporting guidance. Any codes of practice will require parliamentary approval as under the current system
  - The Financial Reporting Council, the body responsible for the supervision of private sector external auditors, will regulate who can undertake local public audit work.
8. There would be a list (referred to as the register of local public statutory auditors in the consultation paper) of audit firms who are recognised as qualified to undertake public audit work. Local councils would be required to appoint their external audit from those firms on the register. The consultation paper states that the costs of the new regulatory regime will be passed on to individual audit firms, who are likely to recover such costs as part of their audit fee.

**Comments**

9. Whilst it could be argued that the introduction of a register of audit firms suitable for public audit work will restrict the choice local councils have in appointing their own external auditor, the system does have the advantage of removing the need for individual authorities to confirm the qualification and experience of audit firms to provide a quality audit service. In addition, the likelihood is that only larger auditing firms would have the skills and capacity to be able to undertake extensive audit work across local authorities, certainly the larger unitary ones. This it could be argued may restrict local choice, but the current system in reality only allows either the Audit Commission (via the District Auditor) or one of the “Big Four” audit practices to undertake the work.
10. However, any regulatory framework will have a cost attached to it, which will inevitably be passed onto to councils in audit fees. Therefore it is essential that any regulatory system is kept straightforward to ensure that costs are kept as low as possible for councils and they do not in themselves act as a barrier to entry for audit firms wishing to apply to be placed on the register. Clearly, predicting the level of audit fees given the Government’s stated intention to reduce the overall costs of the audit regime, set against what many commentators see as an inevitable increase in market costs, will be very difficult until this is implemented.

*Commissioning local public audit services*

11. The consultation paper proposes that all larger local public bodies (defined as those with income/expenditure over £6.5million as in the revised Accounts and Audit Regulations) will be able to appoint its own auditor. The appointed auditor must be on the register of local public statutory auditors.
12. The appointment will be made by full Council, on the advice of an audit committee with opportunities for the electorate to make an input. It is proposed that the Secretary of State should have the power to appoint an external auditor to any local public body who fails to appoint a suitable one themselves. Auditors would be appointed annually, but with a requirement to open the role to competition at least every five years. The council could re-appoint the incumbent audit firm for a maximum of ten years, after which a different audit firm must be used for further audit work.
13. The consultation paper recognises that there is more than one way of arranging such an audit committee but sets out the following possible structure:
  - The audit committee chair and vice-chair would both be independent of the local public body (i.e. not elected members)
  - The elected members on the audit committee should be non-executive, non-cabinet members from the audited body

- At least one member should have recent and relevant financial experience, but with a recommendation that a third of the members have recent and relevant financial experience where possible.
  - There would be a majority of members of the committee who are independent of the local public body.
14. Independent members can only be considered for a position if they:
- Have not been a member or an officer of the public body within five years before the date of appointment
  - Are not a member or officer of any other relevant body
  - Are not a relative or close friend of a member or an officer of the body
  - Have applied for the appointment
  - Have been approved by a majority of the members of the council
  - Position has been advertised in at least one local newspaper and in other similar publications and/or websites.
15. The consultation paper also seeks views on the role of the new audit committee and presents two options:
- **Option One:** The audit committee would be required to provide advice to the council on the engagement and resignation or removal of the auditor. It would then be for the council to decide whether or not the committee has any other function or duty
  - **Option Two:** There would be a much more detailed mandatory role for the audit committee, possibly including providing advice on the procurement and selection of an auditor, ensuring effective relations between internal and external audit and reviewing audit reports and quality. Under this option the audit committee would report annually to the full council on its activities during the year.
16. The consultation paper recognises that individual bodies might wish to co-operate on the appointment of an auditor and so the following legislation will allow both joint procurement of audit services and joint audit committees.

***Comments***

17. Members should be aware that the audit committee proposed in the consultation is substantially different to current local government audit committees. These proposals substantially amend the role of an audit committee and make it largely independent from the full council. Whilst it could be argued that the proposals ensure that an audit committee is totally independent from the council, the working relationship between the two bodies requires careful consideration. The consultation paper is seeking comments on such issues, including whether independent audit committee members would need to be remunerated for their work.
18. This raises the question of what level of remuneration would be appropriate, given the background of an independent member is likely to be significantly



No other contracted services require the involvement of full Council in their selection, and historically only issues of major concern have been flagged by auditors with the Council, so this seems an unnecessarily bureaucratic step.

25. In addition, the trend for modern local government is to remove operational decisions, such as the award of contracts, from the political process, except for larger, longer contracts. This is partly because such decisions are in many cases not strategic and partly because not all members will have either experience or training in the contract process. Elevation of a decision to appoint an auditor to full Council implies that all members would need to be trained in procurement decision-making. The only alternative would be for the decision to be made by the Audit Committee, and then simply ratified by full Council, which would seem to be solely a bureaucratic exercise.
26. It would be worthwhile considering that, if there is to be a list of approved auditors from which the Councils must choose, then it would be advantageous if their procurement was covered by either national or regional framework contracts with savings on procurement costs for both the audit firms and Councils – the value of a 5 year audit contract being comfortably in excess for the EU threshold for such services.
27. On the future role of the audit committee, option 1 is in reality just an external auditor appointment committee that would only need to meet annually to recommend the external auditor (the consultation paper does not really explain why there should be an annual appointment within a 5 year contract. Option 2 is slightly wider, but does not take on the full extent of the work carried out by the Council's existing Audit Committee. Unless the Council wanted to give all the Audit Committee work to the new body, there may be the need for an "internal Audit" Committee and an "external Audit" Committee.
28. Finally, it is not clear if the paper is proposing the adoption of a specific model for audit committees, or to allow local authorities to select their preferred model. Either way, there is a risk that, to avoid the potential impact an independently-led audit committee might have, a local authority may choose to water down the remit of the committee, leaving it largely bereft of any meaningful role.

*Scope of audit and the work of auditors*

29. Currently, public sector bodies are subject to audit with a wider scope than in the private sector, including, for example, value for money and legality issues. The consultation paper presents four possible options for the scope of the audit of councils. These are:
  - **Option one:** The scope of the audit would become similar to private companies with the auditor giving an opinion on the financial statements and review and report on other information published with the financial statements.

- **Option two:** The scope would be similar to the current system in local government, with auditors providing an opinion of the financial statements, concluding as to whether there were proper arrangements to secure value for money and reviewing and reporting on other information including the annual governance statement.
  - **Option three:** New arrangements to provide stronger assurances on regularity and propriety, financial resilience and value for money.
  - **Option four:** A new requirement for councils to prepare and publish an annual report, which would be reviewed by the auditor with them providing reasonable assurance on the annual report.
30. Auditors would continue to have the power to prepare public interest reports, with the costs of such reports being recovered from the audited body. Local people would still be able to question the auditor, but the right to make formal objections to the accounts would be removed. Audit firms would be able to provide such non-audit services as long as they adhere to the ethical standards produced by the Auditing Practice Board and that permission is sought from the audit committee.
31. One of the key elements on this section concerns the right of objection to the accounts. As the paper points out, this dates back some 150 years, and the cost of investigating an objection can often be disproportionate to the nature of the objection. It is now proposed to remove the right of objection, but to allow members of the public to make representations, with the auditor having discretion in deciding whether to follow these up or not. The individual would have the right to go to judicial review if not satisfied with an auditor's decision not to investigate.

***Comments***

32. Clearly there is a trade off between the amount of audit work undertaken and the cost of the audit to a local council. There is the added issue of how much additional work councils wish to undertake, for example the production of an annual report and its publication brings with it an additional level of cost, and if the auditors' powers extend to this, an additional audit fee as well. Auditors are already charged with commenting on value for money, there is a risk that any additional requirements will lead to the type of bureaucracy introduced as part of the use of resources assessment, with a consequent impact on both audit fees and local authority workload.
33. Option two is the closest to the current arrangement and provides both members and the local community with an assurance on both the financial statements of the council and its associated value for money and governance arrangements. It could be argued that, unless there are good reasons to the contrary, this model has worked well. Whilst the general financial climate remains volatile, the public sector in general and local government in particular has remained financially stable, with robust budget-setting and a proven ability to overcome budget problems. Introducing additional checks would seem to be contradictory to a reduction in central

controls and further indicate a lack of trust in the sector's ability to self-police its financial performance.

34. The removal of the right of objection, where residents can object to the whole of an authority's accounts on the basis of a single issue, seems a sensible and appropriate measure. However, the auditor would still have discretion to follow up a representation, and there is the possibility that auditors could adopt a risk-averse strategy; in turn, this seems to imply that authorities would therefore still have to foot the bill for any such work.

*Arrangements for smaller bodies*

35. This is not relevant to Havering.

*Proposed Response to Consultation*

36. The report sets out comments on the different elements of the consultation paper and these have formed the basis for the proposed response, which is set out in Appendix B for comment on and otherwise approval by the Committee. This response covers the broad areas of the paper rather than every individual question posed in the consultation paper.
37. At this stage, it is unclear whether there will be an attempt to reach an agreed position on responses between London authorities. It is possible that either London Councils or the Society of London Treasurers will seek to make a single, agreed submission. Given that consultation is open until the end of June, it is proposed to delegate approval of the final version of the response to the Cabinet Member for Value. If an agreed London position can be reached which removes the need for a local response, provided the points raised in the draft response and debated with the Committee are duly reflected, then this delegation would allow a decision to be made not to also make a local submission.
38. Officers have held an informal discussion with the Chair of the Audit Committee and broadly speaking, her views are in line with the comments contained in this report. Any further comments from the Chair will be reported at the meeting. This report is also being referred to the Audit Committee for their information.

**IMPLICATIONS AND RISKS**

**Financial implications and risks:**

Whilst this is purely for discussion at this stage, the proposed changes are likely to carry financial implications and risks. The future level of audit fees is unknown, and whilst the abolition of the Audit Commission should reduce costs, there has

been considerable speculation that market forces will drive costs in the opposite direction.

In addition, the prospect of engaging independent members may give rise to both additional costs – if some form of remuneration is needed, and for providing appropriate training – and risks, as it may prove difficult to attract suitable candidates into these roles.

The process for appointing an external auditor is not one which local authorities have undertaken for many years. Although the procurement process is likely to be a standard one, this will bring an additional workload for authorities to absorb.

The removal of the right of objection to the accounts would be replaced by an ability to make representations to an auditor. In practice, this could well mean that the cost of any additional work by an auditor would be at a similar level to that arising from an existing objection.

**Legal implications and risks:**

There are no direct legal implications from the proposed decision. Depending on the final proposals from the government after considering the results of the consultation exercise, it is probable that the Council will have to vary its constitution to incorporate a new form of external audit committee. It will be necessary to appoint an external auditor via a competitive procurement exercise.

**Human Resources implications and risks:**

None arising directly from this report.

**Equalities implications and risks:**

None arising directly from this report.

**BACKGROUND PAPERS**

None.



APPENDIX A

COMMUNITIES & LOCAL GOVERNMENT  
THE FUTURE OF LOCAL PUBLIC AUDIT  
CONSULTATION DOCUMENT

DRAFT RESPONSE

TO BE FORMATTED – DRAFT CONTENT ONLY  
LETTER FROM ANDREW BLAKE-HERBERT, GROUP DIRECTOR FINANCE &  
COMMERCE

Thank you for the opportunity of commenting on the consultation paper on the Future of Local Public Audit. Our comments are set out below under each of the main headings of the consultation paper.

*Regulation of Local Public Audit*

Whilst it could be argued that the introduction of a register of audit firms suitable for public audit work will restrict the choice local councils have in appointing their own external auditor, the system does have the advantage of removing the need for individual authorities to confirm the qualification and experience of audit firms to provide a quality audit service. In addition, the likelihood is that only larger auditing firms would have the skills and capacity to be able to undertake extensive audit work across local authorities, certainly the larger unitary ones. This it could be argued may restrict local choice, but the current system in reality only allows either the Audit Commission (via the District Auditor) or one of the “Big Four” audit practices to undertake the work.

However, any regulatory framework will have a cost attached to it, which will inevitably be passed onto to councils in audit fees. Therefore it is essential that any regulatory system is kept straightforward to ensure that costs are kept as low as possible for councils and they do not in themselves act as a barrier to entry for audit firms wishing to apply to be placed on the register. Clearly, predicting the level of audit fees given the Government’s stated intention to reduce the overall costs of the audit regime, set against what many commentators see as an inevitable increase in market costs, will be very difficult until this is implemented. As much certainty as possible is needed in the scale of audit fees, especially in the current financial climate.

*Commissioning local public audit services*

The audit committee proposed in the consultation paper is substantially different to current local government audit committees. These proposals substantially amend the role of an audit committee and make it largely independent from the full council. Whilst it could be argued that the proposals ensure that an audit committee is totally independent from the council, the working relationship between the two bodies requires careful consideration.

The consultation paper asks whether independent audit committee members would need to be remunerated for their work. This raises the question of what level of remuneration would be appropriate, given the background of an independent member is likely to be significantly different to that of an elected member. It is not clear from the paper who would set the level of remuneration and who would be

expected to fund such remuneration, although the assumption is that this would fall to the local authority. Whether the existing remuneration contained within our existing Members Allowances' Scheme would be sufficient to attract the type of candidate with "recent and relevant financial experience" remains to be seen, but is clearly a risk. There is no current requirement for elected members to have any particular qualifications, experience or background; this is partly because their level of involvement in the running of an authority will vary. Training is provided to assist members in their particular areas of involvement, for example in pensions administration or treasury management. There is a risk that less well-qualified yet democratically elected members would be over-whelmed by independent, unaccountable, experts

In addition, if there are more "applicants" than independent roles, it is assumed that there would then need to be some form of appointment process; this may leave authorities facing disputes from unsuccessful candidates, as well as the additional expense of making such appointments. Finally, what happens if an authority is unable to attract suitably qualified members is also not clear.

We believe that there are significant issues arising from this aspect of the paper. Council Members are directly accountable to the local community, and as part of the democratic purpose, are also accountable to the Council itself; their responsibilities are also governed by the Council's rules of procedure. Independent members would have no such accountabilities, and may in fact have vested interests. If such members are being remunerated by a local authority, how truly independent are they?

A further issue is that members of a local authority are bound by its rules, including those of confidentiality. This applies not only to the papers produced for meetings, but also the issues discussed at them. Strict rules prohibit the use of such information. There is a need to ensure that the rules regarding conflicts of interest and confidentiality apply to the independent members.

The paper proposes that independent members would be elected by a majority of members on council. This risks turning a process to appoint independent members into a political one. It is not clear how any appointment process would operate, for example is the appointment to be preceded by interview and if so, who should conduct it. This applies especially if there are more applicants than positions. Currently, the allocation of the number of places on each committee is decided on a proportional basis, reflecting the political composition of each council. It is also not clear if this would remain the approach.

The planned appointment of independent members does not make clear the proposed duration of their appointment. Elected members serve a four year term, whereas the proposal is that appointed auditors would be in place for five years. So it is possible that there will be a churn of members at differing times, with elected members possibly changing every four years but independent members to a different timescale.

Turning to the issue of membership, council rules currently require a quorum, ie a minimum number of members. Whilst council procedure rules provide for

substitutes being nominated for any member unable to attend a meeting, it would not appear to be feasible for this to operate for independent members. This runs the risk of meetings becoming inquorate if independent members are unable to attend, thus bringing committee work to a halt.

At present, only senior officers are barred from standing to be an elected member. The rules proposed in the paper would mean that no council officer would be able to become an independent member.

The paper proposes that the appointment of the auditor would be a decision of full Council, whilst offering two different options for the involvement of the audit committee in the process. Currently, auditors are appointed by the Audit Commission. There are therefore issues over both the skills needed to appoint an auditor, and the resources and cost implications of doing so. No other contracted services require the involvement of full Council in their selection, and historically only issues of major concern have been flagged by auditors with the Council, so this seems an unnecessarily bureaucratic step.

In addition, the trend for modern local government is to remove operational decisions, such as the award of contracts, from the political process, except for larger, longer contracts. This is partly because such decisions are in many cases not strategic and partly because not all members will have either experience or training in the contract process. Elevation of a decision to appoint an auditor to full Council implies that all members would need to be trained in procurement decision-making. The only alternative would be for the decision to be made by the Audit Committee, and then simply ratified by full Council, which would seem to be solely a bureaucratic exercise.

It would be worthwhile considering that, if there is to be a list of approved auditors from which the Councils must choose, then it would be advantageous if their procurement was covered by either national or regional framework contracts with savings on procurement costs for both the audit firms and Councils – the value of a 5 year audit contract being comfortably in excess for the EU threshold for such services. This would then reduce procurement costs and enable Councils to select their auditors without the need of running their own procurement process.

Contract length is usually dictated by a variety of factors, which will include the ability to achieve best value for money. Whilst an initial five year contract for an auditor would seem sensible, it is unlikely any other type of contract would have a similar length extension period. Ten years is a long time for an auditor to be in place; part of the key controls over the operation of the audit function is to practice rotation to avoid over-familiarity. We would therefore wish to see either a shorter extension period, say two years, or a slightly longer single appointment period.

On the nature of the audit committee, option 1 is in reality just an external auditor appointment committee that would only need to meet annually to recommend the external auditor. It should be noted that the consultation paper does not really explain why there should be an annual appointment within a 5 year contract, unless there is a further proposal to annually review performance, which in turn suggests an ability to change more frequently. Option 2 is slightly wider, but does

not take on the full extent of the work carried out by the Council's existing Audit Committee. Unless the Council wanted to give all the existing Audit Committee work to the new body, there may be the need for an "internal Audit" Committee and an "external Audit" Committee. This seems to add a further layer of bureaucracy rather than reducing it.

Finally, it is not clear if the paper is proposing the adoption of a specific model for audit committees, or to allow local authorities to select their preferred model. Either way, there is a risk that, to avoid the potential impact an independently-led audit committee might have, a local authority may choose to water down the remit of the committee, leaving it largely bereft of any meaningful role.

*Scope of audit and the work of auditors*

Clearly there is a trade off between the amount of audit work undertaken and the cost of the audit to a local council. There is the added issue of how much additional work councils wish to undertake, for example the production of an annual report and its publication brings with it an additional level of cost, and if the auditors' powers extend to this, an additional audit fee as well. Auditors are already charged with commenting on value for money, there is a risk that any additional requirements will lead to the type of bureaucracy introduced as part of the use of resources assessment, with a consequent impact on both audit fees and local authority workload.

The enforced publication of an annual report – and the subsequent requirement to audit it – flies in the face of removing bureaucracy. It should be a local choice whether such reports are produced, bearing in mind much of this information can be made readily available at minimal cost to the local community. The publication of the annual accounts already provides detailed information on a local authority's finances, and this would be the place to include any commentary on value for money; it is unclear what further purpose a prescribed annual report would have.

Option two is the closest to the current arrangement and provides both members and the local community with an assurance on both the financial statements of the council and its associated value for money and governance arrangements. It could be argued that, unless there are good reasons to the contrary, this model has worked well. Whilst the general financial climate remains volatile, the public sector in general and local government in particular has remained financially stable, with robust budget-setting and a proven ability to overcome budget problems. Introducing additional checks would seem to be contradictory to a reduction in central controls and further indicate a lack of trust in the sector's ability to self-police its financial performance.

The removal of the right of objection, where residents can object to the whole of an authority's accounts on the basis of a single issue, seems a sensible and appropriate measure. However, the auditor would still have discretion to follow up a representation, and there is the possibility that auditors could adopt a risk-averse strategy; in turn, this seems to imply that authorities would therefore still have to foot the bill for any such work.





## Future of local public audit Consultation



# Future of local public audit

## **Consultation**

March 2011  
Department for Communities and Local Government



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## Ministerial foreword

*“...The Audit Commission has lost its way. Rather than being a watchdog that champions taxpayers' interests, it has become the creature of the Whitehall state. We need to redress this balance.”*

Secretary of State for Communities and Local Government 13 August 2010

On 13 August, the Secretary of State for Communities and Local Government announced our plans to disband the Audit Commission and re-focus audit on helping local people hold their councils and other local public bodies to account for local spending decisions.

We want to drive power downwards to people. We want local public bodies to be more accountable to their citizens, to you the taxpayer, rather than upwards to Whitehall. That is what localism is all about.

The current arrangements for local audit, whereby a single organisation - the Audit Commission - is the regulator, commissioner and provider of local audit services are inefficient and unnecessarily centralised. The Audit Commission has increased the professionalism and the quality of local government audit, but, it has also become too focused on reporting to central Government and supporting the previous era of a target driven Government.

We are clear that centralised inspection and supervision have no part in localism and that they can be an unnecessary burden on frontline services at a time when they must be tightening their belts and focusing on service delivery; they also drive a culture of compliance rather than initiative and problem solving. If our local services are going to be genuinely responsive, tailored to the needs of local people, then they must be accountable to those same people. This is why we want to put in place a new locally focused audit regime, which is open and transparent but retains the high quality of audit that we expect.

This consultation sets out our vision for the future of local audit. This vision is firmly based on four principles. The first of these is localism. When reforms are complete local public bodies will be free to appoint their own independent external auditors from a more competitive and open market. The second is transparency; local public bodies will become increasingly accountable for their spending decisions to the people who ultimately provide their resources. The third is to remove the overheads charged by the Audit Commission to service the central government machine. At a time when we are taking decisive action to reduce the deficit, we think it is important that we deliver a framework which sees a reduction in the overall cost of audit to local bodies. The fourth principle is high standards of auditing. Make no mistake, we are determined that audit will remain both robust and efficient and that the new framework will follow the established principles of public audit.

To meet these principles, the consultation sets out proposals which would see all local public bodies with a turnover of over £6.5m appointing their own independent auditor. This appointment would be made on the advice of an independent audit committee.

Auditors would be regulated under a system which mirrors that of the audit of companies with a role for the Financial Reporting Council and the professional audit bodies. We envisage that the National Audit Office will set the code of audit practice and we have put forward options for the scope of audit in the new framework. The consultation document also sets out how transparency will be increased in the new framework and our proposals for auditing smaller bodies with a turnover below £6.5m in a proportionate way.

Alongside these proposals, the consultation asks a number of questions, to which I would welcome your responses. Your contribution will help us to further develop the framework before publishing legislation in draft in the autumn.

We look forward to hearing your comments on how we can make the future of local audit robust and efficient while ensuring that local public bodies are truly accountable to those they serve.

A handwritten signature in black ink, appearing to read 'Grant Shapps'.

Rt. Hon Grant Shapps MP

## Glossary

### **Accountancy and Actuarial Disciplinary Board**

An independent board which has the ability to investigate and discipline accountants and actuaries who are members of the following professional bodies: the Association of Chartered Certified Accountants; the Chartered Institute of Management Accountants; the Chartered Institute of Public Finance and Accountancy and the Institute of Chartered Accountants in England and Wales; the Institute of Chartered Accountants of Ireland and the Institute of Chartered Accountants of Scotland.

<http://www.frc.org.uk/aadb/>

### **Charities Act 1993**

The Charities Act 1993 sets out the regulatory framework in which charities operate.

[http://www.charity-commission.gov.uk/About\\_us/Regulation/default.aspx](http://www.charity-commission.gov.uk/About_us/Regulation/default.aspx)

### **CIPFA**

Chartered Institute of Public Finance and Accountancy is the professional body for people in public finance.

[www.cipfa.org.uk](http://www.cipfa.org.uk)

### **Companies Act 2006**

The Companies Act 2006 forms the primary source of UK company law.

<http://www.companieshouse.gov.uk/companiesAct/companiesAct.shtml>

### **Comptroller and Auditor General**

Created by the Exchequer and Audit Departments Act 1866 to authorise funding to Government departments and examine departmental accounts, reporting the results to Parliament.

### **Drainage Boards**

An operating authority, established in areas of England and Wales with particular drainage needs. The Board is responsible for work to secure clean water drainage and water level management.

<http://www.ada.org.uk/>

### **Financial Reporting Council**

The Financial Reporting Council is the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment.

They also oversee the regulatory activities of the professional accountancy bodies and operate independent disciplinary arrangements for public interest cases involving accountants and actuaries.

<http://frc.org.uk/>

### **Freedom of Information Act 2000**

Legislation which enables any member of the public to request information from a public body.

### **Grant Certification**

The Audit Commission is required by the Audit Commission Act 1998 to make arrangements for the certification of grant claims when requested to do so by public bodies in receipt of grant funds.

### **Health and Social Care Bill**

The Bill takes forward the areas of Equity and Excellence: *Liberating the NHS* (July 2010) and the subsequent Government response *Liberating the NHS: legislative framework and next steps* (December 2010). It also includes provision to strengthen public health services and reform the Department's arm's length bodies.

### **International Financial Reporting Standards**

IFRS is an independent, not for profit private sector organisation which works on behalf of the public sector to develop standardised financial reporting standards.

<http://www.ifrs.org/>

### **LASAAC**

The Local Authority (Scotland) Accounts Advisory Committee (LASAAC) develops and promotes proper accounting practice for local government in Scotland in line with legislation, International Financial Reporting Standards (overseen by the International Accounting Standards Board) and the work of the Financial Reporting Advisory Board.

<http://www.cipfa.org.uk/pt/cipfalasaac/index.cfm>

### **Lord Sharman**

Liberal Democrat peer, previously the spokesman for Business, Enterprise and Regulatory Reform and former chairman of KMPG. Lord Sharman's review of audit and accountability for central government, *Holding to Account: the Review of Audit and Accountability in Central Government* was published in February 2001.

[http://archive.treasury.gov.uk/docs/2001/sharman\\_1302.html](http://archive.treasury.gov.uk/docs/2001/sharman_1302.html)

### **Management Commentary**

A narrative report which provides the context or background to the financial position, performance and cash flow of an authority or public body.

### **National Fraud Initiative**

Since 1996 the Audit Commission has run the National Fraud Initiative (NFI), an exercise that matches electronic data within and between audited bodies to prevent

and detect fraud. This includes police authorities, local probation boards and fire and rescue authorities as well as local councils.

[www.audit-commission.gov.uk/nfi](http://www.audit-commission.gov.uk/nfi)

### **Police Reform and Social Responsibility Bill**

The Bill will make the police service more accountable to local people by replacing police authorities with directly elected police and crime commissioners to be introduced from May 2012.

### **Professional Oversight Board**

The Professional Oversight Board (POB), formerly known as the Professional Oversight Board for Accountancy, is a UK regulatory body specialising in the accounting, auditing and actuarial professions.

[www.frc.org.uk/pob](http://www.frc.org.uk/pob)

### **Public Audit Forum**

The public audit agencies, the National Audit Office, the Northern Ireland Audit Office, the Audit Commission for Local Authorities and the National Health Service in England, the Wales Audit Office and Audit Scotland have established the Public Audit Forum to provide a focus for developmental thinking in relation to public audit.

<http://www.public-audit-forum.gov.uk>

### **Public Interest Reports**

Under Section 8 of the Audit Commission Act 1998, the appointed auditor is required to consider whether to issue a report in the public interest on any significant matter coming to his or her notice in the course of an audit, and to bring it to the attention of the audited body and the public.

### **Public Interest Disclosure Act 1998**

The Public Interest Disclosure Act 1998 is an Act that protects whistleblowers from detrimental treatment by their employer.

### **Remuneration report**

Companies produce a report containing certain information concerning director's remuneration, governed by the Directors' Remuneration Report Regulations 2002,

### **Section 151 officer**

Section 151 of the Local Government Act 1972 requires every local authority to make arrangements for the proper administration of their financial affairs and requires one officer to be nominated to take responsibility for the administration of those affairs.

**Special Health Authorities**

Special health authorities are health authorities that provide a health service to the whole of England, not just to a local community. They have been set up to provide a national service to the NHS or the public under section 9 of the NHS Act 1977. They are independent, but can be subject to ministerial direction in the same way as other NHS bodies.

**Unitary Authority**

Since 1996 the two-tier structure of local government has ceased to exist in Scotland and Wales, and in some parts of England, and has been replaced by single-tier unitary authorities, responsible for all local government services.

**Whole of Government Accounts**

Whole of Government Accounts (WGA) are full accruals based accounts covering the whole public sector and audited by the National Audit Office. WGA is a consolidation of the accounts of about 1500 bodies from central government, devolved administrations, the health service, local government and public corporations.



# Section 1

## 1. Introduction

- 1.1. On 13 August 2010, the Secretary of State for Communities and Local Government announced plans to disband the Audit Commission, transfer the work of the Audit Commission's in-house practice into the private sector and put in place a new local audit framework. Local authorities would be free to appoint their own independent external auditors and there would be a new audit framework for local health bodies. A new decentralised audit regime would be established and councils and local health bodies would still be subject to robust auditing.
- 1.2. The Secretary of State was clear that safeguards would be developed to ensure independence, competence and quality, regulated within a statutory framework.
- 1.3. This consultation paper discusses the Government's proposals for how a new local audit framework could work and seeks your views.
- 1.4. This document has been developed by the Department for Communities and Local Government. Our proposals have been discussed with a wide range of partners and bodies which will be affected by the changes. These include the Audit Commission, the National Audit Office, the Financial Reporting Council, accountancy professional bodies, local government, other local public bodies and Government departments with an interest.

### **What is audit and why is it important?**

- 1.5. An audit is the review of financial statements, resulting in the publication of an independent opinion on whether those statements have been prepared, in all material respects, in accordance with the applicable financial reporting framework and present a true and fair view. A summary of accounting arrangements for local bodies other than those in the health sector is at appendix A.
- 1.6. The audit of public bodies plays a key role in ensuring that those responsible for handling public money are held accountable for the use of that money. Public audit strengthens accountability, both upwards to the elected or appointed members who make decisions about the allocation of resources, and outwards to the consumers and beneficiaries, taxpayers and the wider community. Regular public audit also provides assurance on bodies' arrangements for managing their finances properly, including their arrangements for value for money and to safeguard public money.

## **Current arrangements for the audit of local public bodies in England**

- 1.7. There are approximately 11,000 local public bodies which, together, are responsible for some £200bn of public money. Of these, there are 353 local authorities; 268 NHS bodies (in addition to Special Health Authorities audited by the National Audit Office, and Foundation Trusts); 38 police authorities; and 215 other bodies, including fire and rescue authorities; national park authorities; conservation boards; larger internal drainage boards, joint committees; and probation trusts. The remaining 9,800 bodies, with income or expenditure ranging from £1m down to £1,000 or less, comprise: 9,400 parish and town councils; 150 internal drainage boards; and 250 other bodies (for example, charter trustees and port health authorities). A list of the categories of bodies audited by the Audit Commission is set out in Appendix B.
- 1.8. The current system for the audit of local public bodies is operated and overseen by the Audit Commission under the provisions of the Audit Commission Act 1998 (as amended). Since its inception in 1983, the Audit Commission has acted as the regulator, commissioner and provider of local audit services.
- 1.9. Acting as the overall regulator, the Audit Commission publishes two statutory Codes of audit practice - one for local government bodies and one for health bodies - which are approved by Parliament. These set the standards for audit and require auditors to comply with the auditing and ethical standards issued by the Auditing Practices Board<sup>1</sup> (which is part of the Financial Reporting Council)<sup>2</sup>. The Commission monitors the quality of audit, although the professional accountancy bodies also monitor their members.
- 1.10. Acting as the commissioner, the Audit Commission appoints auditors, either from its in-house practice or from firms contracted to the Commission, to local public bodies.
- 1.11. The Audit Commission also acts as the main provider in the current system, with 70 per cent of local public audits undertaken by its in-house practice.

## **Proposals for a new audit framework for local public bodies**

- 1.12. The Government believes that the current arrangements for local public audit, whereby a single organisation is the regulator, commissioner and provider of local audit services are unnecessarily centralised. There is a lack of transparency and clarity as well as potential conflicts between the roles.
- 1.13. The proposals set out in this consultation build on the statutory arrangements and professional ethical and technical standards that currently apply to companies. However, those arrangements have been adapted to ensure that the principles of public sector audit are maintained.

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<sup>1</sup> <http://www.frc.org.uk/apb/>

<sup>2</sup> <http://www.frc.org.uk/>

- 1.14. The proposed new local audit regime would continue to provide Parliament with the assurances it needs on public spending. The National Audit Office would prepare the Codes of audit practice, which prescribe the way in which auditors are to carry out their functions, and which would continue to be approved by Parliament, and associated guidance. The National Audit Office would also continue to audit Government departments providing funding to local public bodies and will continue to receive Whole of Government Accounts returns. Registration of audit firms and auditors, as well as monitoring and enforcement of audit standards, would be undertaken by the accountancy professional bodies, under the supervision of the Financial Reporting Council (as this builds on their existing role in the regulation of private sector auditors) and its operating bodies.
- 1.15. Principal local authorities would appoint their own auditors, with decisions made by full council, taking into account advice from an independently chaired audit committee. Different arrangements would apply for some other local public bodies and these are explained in section 3.
- 1.16. Localism and decentralisation can only work if central government is prepared to trust local bodies, communities and citizens. We have aimed to design a local audit system which provides the rigour needed for Parliament, but allows local public bodies to take more responsibility in the way they procure audit services. These changes go hand in hand with the Government's actions to increase transparency in local government and will help enable local people and local organisations to hold their local public bodies to account for the way that their money is spent.

## Design principles

- 1.17. In proposing a new framework for local public audit, we have followed a set of design principles:
- **localism and decentralisation** – freeing up local public bodies, subject to appropriate safeguards, to appoint their own independent external auditors from a more competitive and open market, while ensuring a proportionate approach for smaller bodies
  - **transparency** – ensuring that the results of audit work are easily accessible to the public, helping local people to hold councils and other local public bodies to account for local spending decisions
  - **lower audit fees** – achieving a reduction in the overall cost of audit
  - **high standards of auditing** – ensuring that there is effective and transparent regulation of public audit, and conformity to the principles of public audit
- 1.18. These principles are not wholly independent. For instance, there is a clear relationship between the quality and scope of the audit and the level of audit fees. We wish to find the right balance to ensure an effective, robust, quality audit for local bodies while keeping fees as low as possible.

1.19. We have also had regard to the principles of local public audit, which were codified in 1998 by the Public Audit Forum, but have deep historical roots. They are:

- **Independence of public sector auditors from the organisations being audited.** Auditors must be independent, to avoid improper influence and allow work to be carried out freely. Independence encompasses the methods of appointment of auditors; the financial relationship between auditor and audited bodies, discretion in the amount of work necessary, the ability to follow up the implementation of recommendations, and the ability to have access to information necessary for audit work.
- **The wide scope of public audit, covering the audit of financial statements, regularity, propriety and value for money.** Public audit involves more than an opinion on accounts. It also covers issues such as regularity, propriety and value for money. In this way, it helps to contribute to corporate governance arrangements of public bodies.
- **The ability of public auditors to make the results of their audits available to the public, to democratically elected representatives and other key stakeholders.** To be effective, there must be appropriate reporting arrangements, under which auditors report the results of their work both to the bodies responsible for funding and to the public.

**Q1: Have we identified the correct design principles? If not what other principles should be considered? Do the proposals in this document meet these design principles?**

### **What this consultation covers**

1.20. This consultation focuses on the audit of local public bodies that currently have auditors appointed by the Audit Commission. It sets out, in sections 2 and 3, our proposals for the regulation and commissioning of audit, including the various elements of the new regulatory framework and the role local public bodies will have when appointing an auditor. Section 4 covers the scope of local public audit and the work of auditors, while section 5 deals with the way that the proposed framework would apply to smaller local bodies, such as parish councils.

### **LOCAL BODIES COVERED BY THIS CONSULTATION**

1.21. This document sets out proposals for a new framework for most bodies currently audited by the Audit Commission and listed in appendix B.

1.22. However, the Police Reform and Social Responsibility Bill, which is currently before Parliament, aims to make a number of significant reforms to the policing system. This includes provisions to abolish police authorities (excluding the City of London) and replace them with directly elected Police and Crime Commissioners for each police force outside London, and the Mayor's Office for Policing and Crime for the Metropolitan Police.

- 1.23. Police and Crime Commissioners (and Mayor's Office for Policing and Crime) will be responsible for holding the Chief Constable (and Commissioner for London) of their police force to account for the full range of their responsibilities.
- 1.24. Probation services, which used to be part of Local Government's remit, have been a responsibility of central government since consolidation into the Home Office in 2000-01. The financial results of probation trusts have been consolidated into the National Offender Management Service accounts, which are audited by the Comptroller and Auditor General. We believe, therefore, that probation trusts should in future be audited by the Comptroller and Auditor General.

**Q2: Do you agree that the audit of probation trusts should fall within the Comptroller and Auditor General's regime?**

- 1.25. Pension funds are not statutorily subject to a full audit separate from that of the local authority. However, the Audit Commission has used its regulatory powers to require pension funds to be audited separately. We propose to include pension funds on the list of local public bodies subject to the new local audit framework.
- 1.26. We consider that Joint Committees should remain subject to audit, but it will be for the constituent authorities making up the Joint Committee to decide whether the Joint Committee is audited separately or as part of one of the authorities' own audits.
- 1.27. The abolition of the Audit Commission will also impact on the audit arrangements for local health bodies. Currently, the Strategic Health Authorities, Primary Care Trusts and NHS Trusts are audited under the Audit Commission framework. The Health and Social Care Bill, currently before Parliament, aims to abolish Strategic Health Authorities and Primary Care Trusts and provides for all NHS Trusts to become Foundation Trusts by 2014. The Department of Health is considering the governance and accountability arrangements for the new health landscape and these will help determine the appropriate audit arrangements. The local public bodies referred to in this consultation paper do not therefore include local health bodies. However, health bodies will be included in draft legislation on the proposals for the new local audit framework. The Department of Health will publish a paper summarising its proposals at the same time.

### **Audit Commission functions excluded from this consultation**

- 1.28. There are a number of functions that are or have been carried out by the Audit Commission that are not considered as part of this consultation. The Secretary of State has announced that the Commission's inspection and research activities would cease. In general, local government and others outside of central Government are well-placed to decide when and where research should

be undertaken. In addition, the National Audit Office, following confirmation of its existing powers, will be able, when reporting to Parliament on the activities of central Government departments, to examine the impact of policies administered by local bodies. As well as contributing to parliamentary accountability, this will provide useful insights for local communities by drawing out examples of what works successfully in different circumstances and how barriers to good value for money are being overcome.

1.29. It will also be possible for an auditor to undertake value for money studies connected to audit work, with the agreement of the audited body. In addition, the National Audit Office would be able to identify and report on wider issues of concern about local bodies' use of resources or common themes of interest, should such issues be identified by the audit process. They could do this, in part, by drawing upon the work of local auditors.

1.30. Other functions, such as grant certification, operation of the National Fraud Initiative and the auditor function of reporting on Whole of Government Accounts returns will continue in some form, but are not considered in detail here. These issues will be covered in the forthcoming draft bill and accompanying consultation.

1.31. The Audit Commission appoints auditors to all local public bodies in England. It appoints its own auditors from the in-house practice to 70 per cent of local public bodies, with the remaining 30 per cent of auditors employed by accountancy firms under contract to the Commission. We are considering a range of options for transferring the Commission's in-house audit practice into the private sector. We expect that an announcement on our preferred option for privatisation of the Commission's audit work will be made ahead of publication of a draft audit bill.

### **Timing and how to get involved**

1.32. This initial consultation will run for 12 weeks with responses invited by 30 June. Following this period, we will consider the responses we receive and will publish a summary and a Government response.

1.33. We then propose to publish draft legislation on the proposals for a new local audit framework which will be subject to pre-legislative scrutiny by Parliament and other interested parties. As part of this process, we will consult again on our proposals, and will publish a consultation stage impact assessment. Following pre-legislative scrutiny, we will prepare for final legislation to be introduced at the earliest opportunity.

### **Costs**

1.34. We are developing an impact assessment which will be published alongside the draft Bill. We would therefore be interested in your views on the costs and benefits of the proposals and options set out in this consultation. This evidence will inform the draft bill proposals and help refine the impact assessment.

## Who are we consulting?

1.35. We would welcome comments from organisations affected by the change to the audit of local public bodies, and any other bodies or individuals. This document is available on the Department for Communities and Local Government website ([www.communities.gov.uk](http://www.communities.gov.uk)) and we will be drawing it to the attention of all public bodies currently audited by the Audit Commission, to professional bodies and those involved in regulating audit in England. It is open to all to make representations on the proposed new system of local audit and all submissions will be carefully considered.

## How to respond

1.36. Your response must be received by 30 June 2011 to:

[foia@communities.gsi.gov.uk](mailto:foia@communities.gsi.gov.uk)

Or to:

Luke Scofield  
The Department for Communities and Local Government  
Zone 3/G6  
Eland House  
Bressenden Place  
London SW1E 5DU

1.37. Please use the title 'Response to future of local audit consultation'.

1.38. It would be helpful if you could make clear in your response whether you represent an organisation or group, and in what capacity you are responding.

## Publication of responses – confidentiality and data protection

1.39. Information provided in response to this consultation, including personal information, may be published, or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000, the Data Protection Act 1998 and the Environmental Information Regulations 2004).

1.40. If you want any information you provide to be treated as confidential you should be aware that under the Freedom of Information Act, there is a statutory Code of Practice with which public authorities must comply, and which deals, amongst other things, with obligations of confidence. In view of this, it would be helpful if you could explain to us why you regard the information you have provided as confidential.

1.41. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give any assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer

generated by your IT system will not, of itself, be regarded as binding on the Department.

- 1.42. The Department will process your personal data in accordance with the Data Protection Act and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.



# Section 2

## 2. Regulation of local public audit

2.1. Audit systems in the UK for both the public and private sector follow the International Standards on Auditing. These include the following common elements of regulation:

- **standards** – setting out what comprises the audit and the quality standards that apply
- **registration** – determining who can audit and ensuring that auditors have the necessary skills, expertise and qualifications in order that there can be confidence in the auditors' work
- **monitoring and enforcement** – ensuring that standards are met and that appropriate action is taken in the case of failure

2.2. The Government believes that having a specific regulator for the local government and the local health sectors in England - less than 10% of the audit market – risks duplication. We therefore consider that, to the extent possible, there should be a consistent regulatory regime for audit, covering the private sector and the local government and local health sectors. This local public audit regime should be focused on local accountability, in the way that the commercial sector is tailored to accountability to shareholders.

### Standards and codes of practice

#### CURRENT SYSTEM

2.3. Under the current system the Audit Commission sets audit standards through Codes of audit practice for the local government and health sectors, which are approved by Parliament. These Codes build on the ethical, auditing and other standards issued by the Auditing Practices Board and are therefore broadly consistent with audit standards applied in other sectors.

2.4. However, the Commission's Codes contain additional standards to reflect the principles of public audit and its wider scope, particularly in terms of regularity and propriety and value for money. They specify the approach to audit for areas not already covered by professional audit standards (such as the 'value for money' conclusion). The Commission also publishes guidance and statements of responsibilities of auditors and audited bodies.

#### OTHER SECTORS

2.5. Standards for the audit of companies are set by the Auditing Practices Board (part of the Financial Reporting Council), which sets standards and issues guidance for the performance of external audit and in relation to the independence, objectivity and integrity of external auditors. The Auditing Practices Board is also responsible for setting ethical standards for auditors in the private and public sectors.

### **The Audit Commission's Codes of audit practice**

The Commission has a statutory duty to prepare, keep under review and publish statutory Codes of audit practice. There are currently two Codes: one for local government bodies and one for health bodies. The Codes, which are approved by Parliament and must be reviewed at least every five years, set out best professional practice with respect to the standards, procedures and techniques to be adopted by auditors. The latest versions of the Codes of practice were published in 2010.

The Codes are high level documents, which focus on the Audit Commission's core requirements and aspects of audit specific to its regime. Each Code:

- sets out the general principles to be followed by auditors in delivering their objectives
- outlines auditors' responsibilities regarding the audit of financial statements and use of resources and
- sets out the range of outputs through which the results of audit are reported

### **OUR PROPOSALS**

2.6. Under our proposals, auditors of local public bodies would continue to follow the auditing and ethical standards set by the Auditing Practices Board. We have considered which body would be best placed to produce the audit Codes of practice and supporting guidance. While this is a role that could possibly be undertaken by the Financial Reporting Council or the profession, we believe that the National Audit Office, given its role in providing Parliament with assurance on public spending, would be best placed to develop and maintain the audit Codes, which would continue to be approved by Parliament. The National Audit Office would also produce any supporting guidance.

**Q3: Do you think that the National Audit Office would be best placed to produce the Code of audit practice and the supporting guidance?**

### **Registration of auditors**

#### **CURRENT SYSTEM**

2.7. The Audit Commission Act 1998 stipulates that for an individual or a firm to be appointed as an auditor, the person/s conducting the audit must be a member of one of the specified professional bodies and has such qualifications as may be approved by the Secretary of State (none have been so approved). The Audit Commission regulates the quality of the work of auditors by setting minimum qualifications a public sector auditor must have in conjunction with standards set by the professional bodies for membership.

## **OTHER SECTORS**

- 2.8. As part of the statutory framework for the audit of companies under the Companies Act 2006, the Professional Oversight Board (part of the Financial Reporting Council), essentially acts as the main regulator, with statutory powers delegated to it by Government for the recognition and supervision of those professional accountancy bodies responsible for supervising the work of auditors or offering an audit qualification – recognised qualifying body and recognised supervisory body e.g. Institute of Chartered Accountants in England and Wales.
- 2.9. Recognised supervisory bodies are responsible for putting rules and arrangements in place which their members must fulfil before they can be registered auditors, both as regards eligibility for appointment as a statutory auditor and the conduct of statutory audit work. A list of recognised supervisory bodies and recognised qualifying bodies for the purposes of the Companies Act is at annex C. The Institute of Chartered Accountants for Scotland maintains the list of registered auditors for the whole of the UK on behalf of the recognised supervisory bodies.
- 2.10. People with responsibility for company audit work at the firm must also hold a recognised qualification, awarded by a recognised qualifying body.
- 2.11. Looking elsewhere, in Finland, auditors who are eligible to audit municipal authorities are included in a register of eligible auditors maintained by the Finnish Board of Chartered Public Finance Auditing. In Italy, auditors who can carry out local public audit are included on a register of auditors managed by the Ministry of Justice.

## **OUR PROPOSALS**

- 2.12. We propose that, as under the Companies Act 2006 (“the Companies Act”), an overall regulator would have responsibility for authorising professional accountancy bodies to act as recognised supervisory bodies for local public audit. Any such body would need to comply with the statutory requirements set out in the proposed primary legislation. It would have the roles of registration, monitoring, and discipline in relation to local public audit.
- 2.13. The Financial Reporting Council is the regulator for Companies Act audit and we propose that it takes on a similar role for the local public audit regulatory regime in England, provided that it can assure the Government that it has both the resources and the expertise to undertake the role, and wishes to do so. It is likely that setting up a separate regulator for local public audit would lead to duplication of work as entirely new systems and procedures would need to be developed.
- 2.14. Recognised supervisory bodies for local public audit could include supervisory bodies recognised under the Companies Act 2006 and any other bodies with sufficient expertise and capacity.
- 2.15. A recognised supervisory body for local public audit could have rules and practices covering:

- the eligibility of firms to be appointed as local public auditors and
- the qualifications, experience and other criteria individuals must reach before being permitted to lead a local public audit engagement and/or sign off an audit report

2.16. We propose to set out, in primary legislation, certain high level criteria that specify that the auditor must be:

- a member of a recognised supervisory body and
- eligible for appointment under the rules of that body

2.17. The legislation will include provisions enabling the supervisory body to develop appropriate detailed rules and practices on other criteria.

2.18. The eligibility criteria will be based on those for the audit of companies as we would like to ensure enough flexibility in the criteria to enable new firms to enter the local public audit market. However, there will need to be additional criteria to ensure that auditors have the necessary experience to be able to undertake a robust audit of a local public body.

2.19. We propose that all eligible local public auditors would be placed on a public register. This register could be kept by the recognised supervisory bodies for local public audit, or it could be kept by another body.

**Q4: Do you agree that we should replicate the system for approving and controlling statutory auditors under the Companies Act 2006 for statutory local public auditors?**

**Q5: Who should be responsible for maintaining and reviewing the register of statutory local public auditors?**

**Q6: How can we ensure that the right balance is struck between requiring audit firms eligible for statutory local public audit to have the right level of experience, while allowing new firms to enter the market?**

**Q7: What additional criteria are required to ensure that auditors have the necessary experience to be able to undertake a robust audit of a local public body, without restricting the market?**

## **Monitoring and enforcement**

### **CURRENT SYSTEM**

2.20. The Audit Commission currently monitors the quality of auditors' performance through its annual quality review programme. The Audit Inspection Unit of the Financial Reporting Council reviews the quality of the financial statements audits carried out by the Commission's own audit practice and by private firms on behalf of the Commission.

### **OTHER SECTORS**

2.21. Under the Companies Act, the recognised supervisory bodies are responsible for monitoring the quality of the statutory audits undertaken by their members and for disciplining their members where this is appropriate.

2.22. Some companies that are of public significance because of the nature of their business, their size, or their number of employees can be designated as "public interest entities". In the case of these bodies, the Professional Oversight Board has an additional role in monitoring the quality of the auditing function and the Accountancy and Actuarial Disciplinary Board has a role in investigating significant public interest disciplinary cases and imposing sanctions to those found guilty of misconduct.

### **OUR PROPOSALS**

2.23. We propose that recognised supervisory bodies for local public audit would have responsibility for monitoring the quality of audits undertaken by their members, as they do in the private sector. This work would fall under the monitoring units of these bodies, and would include:

- reviews of individual audit engagements
- reviews of the policies, procedures and internal controls of those firms licensed to carry out the public sector audits
- reporting on the quality of audit to the registration body

2.24. The recognised supervisory bodies for local public audit would investigate complaints or disciplinary cases, as well as issues identified during their monitoring process. They would also be able to stop a firm being eligible for appointment as a statutory local public auditor and remove them from the register of eligible local public auditors.

2.25. We are considering whether the overall regulator (i.e. the body that authorises the recognised supervisory bodies) should have a role in assuring the quality, and undertaking independent investigation of the audit of local public bodies that might be considered analogous to public interest entities for the public sector. The overall regulator would have powers to investigate and discipline in these cases. The process undertaken would be similar to that above, but would provide an additional level of assurance in respect of those bodies.

However, the costs that would fall on the Financial Reporting Council from undertaking this role would be passed on to the audit firms and therefore could be reflected in fees.

**Q8: What should constitute a public interest entity (i.e. a body for which audits are directly monitored by the overall regulator) for the purposes of local audit regulation? How should these be defined?**

**Q9: There is an argument that by their very nature all local public bodies could be categorised as 'public interest entities.' Does the overall regulator need to undertake any additional regulation or monitoring of these bodies? If so, should these bodies be categorised by the key services they perform, or by their income or expenditure? If the latter, what should the threshold be?**

**Q10: What should the role of the regulator be in relation to any local bodies treated in a manner similar to public interest entities?**

# Section 3

## 3. Commissioning local public audit services

- 3.1. The Government believes that a localist approach, without an independent central body having a role in appointing an auditor, is an important element of driving accountability to local people rather than to central government. However, maintaining the independence of the auditor in the new system is central to the principles of public audit. Our proposals therefore need to include measures to safeguard the independence of the auditor.

### **Duty to appoint an auditor**

#### **CURRENT SYSTEM**

- 3.2. Under the current system, all auditors of local public bodies included in Schedule 2 of the Audit Commission Act are appointed by the Audit Commission. Before making appointments of auditors to local government bodies, the Commission has a statutory duty to consult the body. The Commission has voluntarily extended this practice to health bodies.

#### **OTHER SECTORS**

- 3.3. Commissioning takes different forms in different sectors. Under the Companies Act the annual general meeting must agree a resolution on the appointment of the auditor, although this will be based on a recommendation from directors and input from an audit committee.
- 3.4. Looking elsewhere, it is clear that there are different systems for commissioning audit services. However, in the USA local authorities procure their own auditors: an audit committee often appoints 'internal auditors' for their local authority, who then procure the external auditor.

#### **OUR PROPOSALS**

- 3.5. We propose that all larger local public bodies (those with income/expenditure over £6.5m) will be under a duty to appoint an auditor. The auditor would need to be on the register of local public statutory auditors, which should help to ensure that the quality of auditors is maintained.
- 3.6. It is equally important as it is in other sectors that those to whom audit is directed have influence but that the independence of the auditor remains paramount. Therefore, for larger public bodies, we propose an approach whereby appointment is made by full council or equivalent, on the advice of an audit committee with opportunities for the electorate to make an input.
- 3.7. We consider that local public bodies will wish to co-operate to ensure that there is wide competition for external audit contracts, and that local public bodies will want to work together to procure an external auditor. We propose to ensure that legislation provides for both joint procurement and joint audit committees.

**Q11: Do you think the arrangements we set out are sufficiently flexible to allow councils to cooperate and jointly appoint auditors? If not, how would you make the appointment process more flexible, whilst ensuring independence?**

- 3.8. Lord Sharman, in his report, *Holding to Account: the Review of Audit and Accountability in Central Government*, was clear that, to maintain confidence, auditors must be independent to avoid improper influence and allow work to be carried out freely. Independence includes the way auditors are appointed. We consider that, as part of a new local audit regime, each larger local public body should have an audit committee with a majority of members independent of the local public body and, with some elected members to strike a balance between objectivity and in-depth understanding of the issues.
- 3.9. A possible structure is set out below. However, there could be alternative arrangements, for example:
- a) only the chair and perhaps a minority of members are independent of the local public body
  - b) a chair and a majority of members independent of the local public body, as described below
  - c) as for (b), but with independent selection of the members independent of the local authorities
- 3.10. We are keen to ensure that local public bodies have flexibility in the way that they constitute and run audit committees. But we need to balance this with ensuring that the minimum requirements for an audit committee set out in legislation provide for an independent audit appointment. We set out below a possible structure and role for the audit committee, some of which may be prescribed in legislation and some of which we would put forward as best practice.



## **Structure of audit committees**

We envisage that in the new system, an audit committee could be structured in the following way:

- The chair should be independent of the local public body. The vice-chair would also be independent, to allow for the possible absence of the chair.
- The elected members on the audit committee should be non-executive, non-cabinet members, sourced from the audited body and at least one should have recent and relevant financial experience (it is recommended that a third of members have recent and relevant financial experience where possible).
- There would be a majority of members of the committee who were independent of the local public body.

### ***Independent members of the committee***

When choosing an independent member of the committee, a person can only be considered for the position if:

- he or she has not been a member nor an officer of the local authority/public body within five years before the date of the appointment
- is not a member nor an officer of that or any other relevant authority
- is not a relative nor a close friend of a member or an officer of the body/authority
- has applied for the appointment
- has been approved by a majority of the members of the council
- the position has been advertised in at least one newspaper distributed in the local area and in other similar publications or websites that the body/local authority considered appropriate

**Q12: Do you think we have identified the correct criteria to ensure the quality of independent members? If not, what criteria would you suggest?**

**Q13: How do we balance the requirements for independence with the need for skills and experience of independent members? Is it necessary for independent members to have financial expertise?**

**Q14: Do you think that sourcing suitable independent members will be difficult? Will remuneration be necessary and, if so, at what level?**

## **Role of the Audit Committee**

### **CURRENT SYSTEM**

3.11. As auditors are currently appointed by the Audit Commission there is no role for an audit committee in the appointment of auditors, although the Audit Commission always consults local public bodies before it confirms an audit appointment. However, some local public bodies do have Audit Committees (some of which are independent) with roles in relation to both internal and external audit.

3.12. Health bodies currently have their own form of audit committees following the Financial Reporting Council best practice guidance, comprising of independently appointed non-executive directors governed by their own rules and requirements.

### **OTHER SECTORS**

3.13. The Financial Reporting Council currently produces guidance for the establishment of audit committees for companies, stating that they should be made up of at least three, or in the case of smaller companies two, independent non-executive directors.

3.14. The main role and responsibilities of a company's audit committee are set out in written terms of reference and can include a number of roles, including:

- providing advice to the board in relation to the appointment of external auditors
- approving the remuneration and terms of engagement of the external auditor
- reviewing and monitoring the external auditor's independence and objectivity and the effectiveness of the audit process
- developing and implementing policy on the engagement of the external auditor to supply non-audit services

3.15. Looking elsewhere, audit committees are statutory bodies in each municipality in Finland. Their remit includes preparing the choice and appointment of external auditors. In Canada, the local authority's audit committee also commissions audit services.

### **OUR PROPOSALS**

3.16. It is likely that we would want to specify in legislation some responsibilities that the audit committee should have in relation to the engagement of an auditor and monitoring the independence and quality of the external audit. However, we would not wish to limit the scope of an audit committee so that a local body had no flexibility in designing its role.

3.17. The expanded role of the audit committee would include the provision of advice and guidance to the full council or equivalent (the audit committee may wish to have regard to advice from the section 151 officer) on appropriate criteria for engaging an auditor and advice as to how these criteria could be weighted. The audit committee would be given copies of the bids to evaluate in order that they

may advise the full council or equivalent on the selection process and may, if they wish, indicate which auditor, in their view, presents the best choice.

- 3.18. The full council or equivalent would need to have regard to the advice of the audit committee but would not need to follow its advice. The full council or equivalent would be responsible for selecting an auditor and engaging that auditor on a contractual basis.
- 3.19. Advice provided by the audit committee to the full council or equivalent would be published, although consideration will need to be given to the treatment of commercially confidential material.
- 3.20. If the full council or equivalent did not follow the advice of the audit committee, then it would need to publish on its website a statement from the audit committee explaining its advice and a statement from the full council or equivalent setting out the reasons why the council or equivalent has taken a different position.

### **Option 1**

- 3.21. We could specify only one mandatory duty for the local public body's audit committee, i.e. to provide advice to the local public body on the engagement of the auditor and the resignation or removal of an auditor.
- 3.22. It would then be left up to the local public body and the audit committee to decide whether the audit committee should have a wider role in other issues, e.g. setting a policy on the provision of non-audit services by the statutory auditor or reviewing the relationship between the auditor and the audited body.
- 3.23. This option would ensure that the audit committee provided advice to the local public body at crucial moments, but would allow the local public body and the audit committee flexibility to decide on any other functions it may carry out. However, if only the minimum was followed, this may not provide an adequate check on ongoing independence through the auditor's term.

### **Option 2**

- 3.24. We could specify a much more detailed mandatory role for the audit committee which could include, but may not be restricted to the following:
- providing advice to the full council on the procurement and selection of their external auditor
  - setting a policy on the provision of non-audit work by the statutory auditor
  - overseeing issues around the possible resignation or removal of the auditor
  - seeking assurances that action is being taken on issues identified at audit
  - considering auditors' reports
  - ensuring that there is an effective relationship between internal and external audit
  - reviewing the financial statements, external auditor's opinions/conclusions and reports to members and monitor management action in response to the issues raised by external audit
  - providing advice to the full council on the quality of service they are receiving

- reporting annually to the full council on its activities for the previous year

3.25. This option would provide more assurance about the independence of the relationship between the audited body and its auditor, it would also ensure that the audit committee had a wider role in reviewing the financial arrangements of the local public body.

**Q15: Do you think that our proposals for audit committees provide the necessary safeguards to ensure the independence of the auditor appointment? If so, which of the options described in paragraph 3.9 seems most appropriate and proportionate? If not, how would you ensure independence while also ensuring a decentralised approach?**

**Q16: Which option do you consider would strike the best balance between a localist approach and a robust role for the audit committee in ensuring independence of the auditor?**

**Q17: Are these appropriate roles and responsibilities for the Audit Committee? To what extent should the role be specified in legislation?**

**Q18: Should the process for the appointment of an auditor be set out in a statutory code of practice or guidance? If the latter, who should produce and maintain this?**

## **Involvement of the public in the appointment of an auditor**

### **CURRENT SYSTEM**

3.26. There is no involvement of the public in the appointment of auditors by the Audit Commission to audited bodies.

### **OUR PROPOSALS**

3.27. We envisage that the appointment of an auditor by the local public body should be as transparent as possible so that local people are able to hold their local public bodies to account for the appointment.

### ***Pre-appointment***

3.28. The audited body could ask for expressions of interest from audit firms for the audit contract one month prior to the publication of the invitation to tender. The list of those firms that have expressed an interest would then be published on the audited body's website. The public would then be able to make representations to the audited body's audit committee about any of these firms. The audit committee would consider these representations when providing advice to the full council or equivalent.

### **Post - appointment**

3.29. The public would be able to make representations at any time to the local public body's audit committee. If a representation identified a significant, or potentially significant, issue relating to the auditor, then the audit committee would be able to provide advice to the audited body on that issue and investigate as appropriate. If the issue identified was material to the ongoing work of the auditor (such as an undisclosed material conflict of interest) then the audited body would need to take such steps as appeared necessary, in accordance with the terms of the contract with the auditor, to address that issue. We may also wish to specify in legislation some statutory requirements relating to conflicts of interest.

**Q19: Is this a proportionate approach to public involvement in the selection and work of auditors?**

### **Applicability to other sectors**

3.30. The policy of audit committees acting as a safeguard to independent appointment is applicable to all larger local public bodies covered by this framework. The approach may differ depending on the constitution and governance arrangements of those bodies.

3.31. For Police and Crime Commissioners (and Mayor's Office for Policing and Crime) and Chief Constables (and Commissioner for London) we are considering whether the Police and Crime Panel should have a role similar to that of the audit committee. Arrangements for the audit of these policing bodies will be finalised once the Police Reform and Social Responsibility Bill has completed its passage.

**Q20: How can this process be adapted for bodies without elected members?**

### **Failure to appoint an auditor**

#### **CURRENT SYSTEM**

3.32. As the Audit Commission is responsible for appointing the auditors for all audited bodies specified in the Audit Commission Act 1998, the situation where an audited body fails to appoint an auditor does not arise.

#### **OTHER SECTORS**

3.33. The Companies Act 2006 provides a default power for the Secretary of State, so that if a private company fails to appoint an auditor or auditors, the Secretary of State may appoint one or more persons to fill the vacancy. If the company fails to make the necessary appointment, the company is required to give notice to the Secretary of State that his power has become exercisable and if the

company fails to give this notice then the company has committed an offence and can be liable for a fine.

### **OUR PROPOSALS**

3.34. The audited body would be under a duty to appoint an auditor. However, there could be some instances under the new system where a body does not fulfil this duty.

#### **Option 1**

3.35. In these circumstances we propose that the Secretary of State would be able to direct the local public body to appoint an auditor.

#### **Option 2**

3.36. Alternatively, where a local public body does not fulfil its duty to appoint an auditor the Secretary of State could be provided with the power to make the auditor appointment. In addition to meeting the cost of the appointment the local public body could be subject to a sanction for failing to make the appointment.

**Q21: Which option do you consider provides a sufficient safeguard to ensure that local public bodies appoint an auditor? How would you ensure that the audited body fulfils its duty?**

3.37. It would clearly be against our design principles for the new local audit framework for the Secretary of State to make the auditor appointment for local public bodies. However, some form of assurance will be required that local public bodies have fulfilled their duty to appoint an auditor.

**Q22: Should local public bodies be under a duty to inform a body when they have appointed an auditor, or only if they have failed to appoint an auditor by the required date?**

3.38. Given that we envisage that the Recognised Supervisory Bodies will hold the register of eligible local public auditors there is an argument that they should be notified if a local public body has appointed or failed to appoint an auditor. However, this could involve a significant cost.

3.39. As the Secretary of State would be able to direct the local public body to appoint an auditor, or could be provided with the power to make the auditor appointment where a local public body does not fulfil its duty to appoint an auditor, an alternative option would be for the local public body to notify the appropriate government department, or a body that the government department specifies, of the auditor appointment. The cost of doing this could be met by the appropriate department, and would provide an effective route for the Secretary of State to exercise his powers to direct the local public body to appoint an auditor, or to make the auditor appointment where the body did not fulfil its duty to appoint an auditor.

**Q23: If notification of auditor appointment is required, which body should be notified of the auditor appointment/failure to appoint an auditor?**

## **Rotation of audit firms and audit staff**

### **CURRENT SYSTEM**

3.40. The Auditing Practices Board's ethical standards, which apply to the audit of both private and public entities, require an audit firm to establish policies and procedures to monitor the length of time that audit engagement partners and other key staff serve as members of the engagement team for each audit. These procedures are in place to help ensure the independence and objectivity of auditors.

3.41. The Audit Commission appoints audit firms or its own staff for an initial period of five years. The audit engagement partner can then be appointed for an additional period of up to two years in accordance with the Auditing Practices Board's Ethical Standards (i.e. a maximum of seven years, provided there are no threats to the auditor's independence). The audit manager (the second in command to the audit engagement partner) can be appointed for a maximum of ten years. After this period individuals should then have no further direct relationship with or involvement in work relating to the body concerned until a further period of five years has elapsed.

### **OTHER SYSTEMS**

3.42. In the case of listed companies, the audit firm must have policies and procedures so that:

- no-one shall act as audit engagement partner for more than seven years and
- anyone who has acted as the audit engagement partner for a particular entity for a period of seven years, shall not subsequently participate in the audit engagement with that entity until a further period of five years has elapsed

3.43. The audit committee of a company assesses the independence and objectivity of the external auditor annually, taking into consideration regulatory and professional requirements. This assessment involves a consideration of all relationships between the company and the audit firm (including the provision of non-audit services) and any safeguards established by the external auditor. The audit committee seeks from the audit firm, on an annual basis, information about policies and processes for maintaining independence and monitoring compliance with relevant requirements, including current requirements regarding the rotation of audit partners and staff.

### **OUR PROPOSALS**

3.44. We envisage that the new audit framework would be in line with the current ethical standards regarding the rotation of staff within the audit firm.

3.45. The audited body's audit committee would have a role in monitoring the independence and objectivity of the body's external auditor.

- 3.46. In relation to the rotation of the firm, an audit firm would be reappointed annually by the full council on the advice of the audit committee (who may want to provide advice on the quality of service received in the previous year) but the audited body could be required to undertake a competitive appointment process within five years. The audited body would be able to re-appoint the same firm for a second consecutive five year period, following competition.
- 3.47. To preserve independence, we propose that the audited body would need to procure a different audit firm at the end of the second five year period. This will help to ensure that in carrying out their responsibilities auditors are not influenced by their desire to secure re-appointment.

**Q24: Should any firm's term of appointment be limited to a maximum of two consecutive five-year periods?**

**Q25: Do the ethical standards provide sufficient safeguards for the rotation of the engagement lead and the audit team for local public bodies? If not, what additional safeguards are required?**

**Q26: Do the proposals regarding the reappointment of an audit firm strike the right balance between allowing the auditor and audited body to build a relationship based on trust whilst ensuring the correct degree of independence?**

## **Resignation or removal of an auditor**

### **CURRENT SYSTEM**

- 3.48. In the current situation there is not a direct contractual relationship between the auditor and the audited body - the relationship is with the Audit Commission. It is therefore not possible for the audited body to remove the auditor and the auditor does not need to resign because of issues arising with the audit.
- 3.49. In the event that there was a breakdown in the relationship between the auditor and audited body the Audit Commission can consider rotating suppliers.
- 3.50. The audit engagement partner or audit team may change during the appointment and the Audit Commission can and does rotate between firms and its in-house practice undertaking the audit, including if the audited body requests it.



## **OTHER SECTORS**

### ***Resignation***

3.51. In the companies sector, if an auditor ceases for any reason to hold office, he must deposit a statement at the company's registered office which will usually set out the circumstances connected with his ceasing to hold office. If the circumstances are set out in the statement (in the case of a quoted company), the company must send a copy of the statement to all members of the company unless it makes a successful application to the court to stop this.

3.52. If (in the case of an unquoted company) the circumstances are not set out in the statement, the auditor must deposit a statement with the company to that effect but the company does not have to circulate this statement to its members.

3.53. When an external auditor resigns, the audit committee of the company will investigate the issues giving rise to such resignation and consider whether any action is required.

### ***Removal***

3.54. The members of a company may remove an auditor from office at any time during their term of office. They, or the directors, must give 28 days notice of their intention to put to a general meeting a resolution to remove the auditor. The company must send a copy of the notice to the auditor, who then sends it to the company's members. The auditor may speak at the meeting where the resolution is to be considered. Although a company may remove an auditor from office at any time, the auditor may be entitled to compensation or damages for termination of appointment.

## **OUR PROPOSALS**

3.55. We envisage that a body might wish to remove its auditor, or an auditor might wish to resign, only in exceptional circumstances, for example, an auditor being in breach of the ethical standards, or a complete breakdown in the relationship between the auditor and audited body.

3.56. However, we recognise the importance of having stringent safeguards in place for the resignation and removal of an auditor to protect the independence of the auditor and the quality of the audit. These safeguards would broadly mirror those in the Companies Act, but would be adapted to reflect the principles of public audit. The process would be designed to ensure that auditors are not removed, or do not resign, without serious consideration.

### ***Resignation***

3.57. We envisage that in the first instance, the audited body and the auditor should discuss and seek to resolve any concerns. If the auditor still wished to resign he should give 28 days written notice of his intention to the audit committee and the audited body, setting out his intention to resign. The audited body should then make a written response, which it should send with the auditor's written notice, to its members and the audit committee. The auditor will then be required to deposit a statement at the audited body's main office and with the audit committee, which should be published on its website. The statement

would set out the circumstances connected with the resignation of the office that are relevant to the business of the audited body.

3.58. The audited body would need to notify the body responsible for maintaining the register of appointed auditors, and the auditor will need to notify the appropriate regulatory supervisory body. We envisage a role for the audit committee and the regulatory supervisory body in investigating the issues that have led to the resignation and considering whether any action is required.

### **Removal**

3.59. Again, we envisage that in the first instance, the audited body and the auditor should discuss and seek to resolve any concerns. If the audited body still wished to remove its auditor, it should give 28 days written notice of its intention to the audit committee and to the auditor. The audited body should put to a public meeting, or full council meeting, a resolution to remove the auditor. The audited body would also send a copy of this notice to the auditor.

3.60. The auditor would then have the right to make a written response, which the body would need to send to its members and the audit committee, and to speak at the meeting where the resolution is to be considered. A representative from the audit committee should also be able to speak at the meeting. The auditor would be required to deposit a statement at the audited body's main office and with the audit committee, which would need to be published on its website. This statement would set out the circumstances connected with the cessation of their office that are relevant to the business of the audited body.

3.61. The audited body would need to notify the appropriate regulatory supervisory body. We envisage a role for the audit committee and the regulatory supervisory body in investigating the issues that have led to the removal and considering whether any action is required.

3.62. A right of access to the previous auditor's audit working papers (from the previous year and/or current) should be provided to incoming auditors in cases of resignation or removal or any other instances where the audit firm changes. This right should extend to all aspects of the previous auditor's responsibilities and not just to work on the audit of the financial statements.

**Q27: Do you think this proposed process provides sufficient safeguard to ensure that auditors are not removed, or resign, without serious consideration, and to maintain independence and audit quality? If not, what additional safeguards should be in place?**

## **Auditor liability**

3.63. In the private sector, auditors are concerned about the consequences of the risks of litigation, as a result of actual or perceived failing by auditors. These concerns have been fuelled by legal judgments about the extent of auditors' duty of care to third parties, such as potential investors and the banks. They have increasingly caused auditors to caveat their audit opinions by explicitly limiting their duty of care and by seeking to limit their liability. Case law has established that the duty of care of auditors appointed by the Commission is to the audited body itself and not to third parties. Public authorities can sue their auditor for breach of duty.

### **CURRENT SYSTEM**

3.64. There are particular issues in the public sector where auditors may exercise special powers. The Audit Commission currently indemnifies auditors for the costs they incur where they are engaged in litigation arising from the exercise of such powers. This ensures that auditors are able to exercise their functions with the certainty that their costs will be met.

### **OTHER SECTORS**

3.65. In the companies sector, the Companies Act provides that general provisions that protect auditors from liability for negligence, default, breach of duty or breach of trust in relation to the company, or provide an indemnity against liability are void, but:

- does not prevent a company from indemnifying an auditor against any costs incurred by him in defending proceedings in which judgment is given in his favour or in the granting of relief by the court in the case of honest and reasonable conduct
- allows for a "liability limitation agreement" to be put in place if it is authorised by the members of the company, provided it complies with the content permitted in the Companies Act

### **OUR PROPOSALS**

3.66. In the absence of a central body providing indemnity to audit firms, it could be possible for audited bodies and auditors to deal with auditor liability as part of their contractual negotiations. A legislative framework, similar to that in the companies sector, could set out the process for setting and agreeing liability limitation agreements. Without a liability agreement, audit firms may increase their fees to match the increased risk they face in undertaking their work.

**Q28: Do you think the new framework should put in place similar provision as that in place in the companies sector, to prevent auditors from seeking to limit their liability in an unreasonable way?**

# Section 4

## 4. Scope of audit and the work of auditors

4.1. In this chapter, we look at the scope of the audit and the options for the elements of local public bodies' finance and the arrangements that auditors should assess. The duty for the auditor to issue a report in the public interest is also considered. This section asks whether auditors should be able to carry out additional, non-audit, work for the audited body, and considers the various safeguards that could be introduced to ensure that auditor independence is not compromised.

### **Scope of local public audit**

4.2. The starting point is the principles of public audit, in particular the wide scope of the audit covering the audit of financial statements, regularity and propriety and value for money.

### **CURRENT SYSTEM**

4.3. Public sector accounting in the UK has recently moved to adopt International Financial Reporting Standards adapted as necessary for the public sector (for local government audits from 2010-11).

4.4. Currently, the auditor of larger local public bodies is required to:

- give an opinion on whether the accounting statements give a true and fair view of the audited body's financial position and of its income and expenditure
- provide a conclusion as to whether the body has proper arrangements for securing value for money, having regard to specified criteria (such as financial resilience and to regularity and propriety) and in accordance with guidance issued by the Commission
- review and report on as appropriate, other information published with the financial statements, including the statement on internal control/annual governance statement and the remuneration report and
- (for local government) review and report on the Whole of Government Accounts return

4.5. Smaller local public bodies are currently subject to a limited assurance regime. We believe that it is important for smaller bodies to continue to be dealt with proportionately under the new framework and discuss this in more detail at Section 5.

### **OTHER SECTORS**

#### ***Companies***

4.6. The scope of audit for companies is based around the financial statements produced by the company and a report that the directors are required to produce which must describe the company's principal activities, a review of the business and an indication of future developments.

4.7. Statutory auditors of companies include in their report, statements as to whether, in their opinion:

- the accounts have been prepared in accordance with the Companies Act 2006
- the accounts give a “true and fair “ view of the company’s financial statements
- the director’s report is consistent with the accounts
- the remuneration report is properly prepared

### **Charities**

4.8. Any charity which has income above the audit threshold in the financial year must have an audit of its financial statements undertaken by a registered auditor. This is in line with the treatment of companies.

4.9. The Charities Act 1993 also requires all registered charities to prepare a Trustees’ Annual Report. The length of the report and the amount of detail included in it can be in proportion to the charity’s size so for small charities it can be a very simple report.

### **Central government**

4.10. The Comptroller and Auditor General, with the support of the National Audit Office, is responsible for auditing the financial statements of all central Government departments, executive agencies and a wide range of other public sector bodies.

4.11. When certifying the accounts of central government departments, the Comptroller and Auditor General states whether, in his opinion:

- the financial statements give a “true and fair” view of the financial position of the body
- the financial statements have been properly prepared in accordance with underpinning legislation
- in all material respects the transactions recorded in the financial statements are in accordance with Parliamentary or other authority (regularity)
- information given in the Management Commentary/Annual Report is consistent with the financial statements
- the audited part of the Remuneration Report has been properly prepared in accordance with relevant guidance

4.12. The Comptroller and Auditor General also has statutory authority to report to Parliament on the economy, efficiency and effectiveness with which departments and other bodies have used their resources.

### **OUR PROPOSALS**

4.13. When looking at the future scope of audit for local public bodies we have considered whether we should move to a more transparent model, such as that followed by companies and charities which must produce a director or trustee’s report. Central Government departments are also required to prepare an Annual Report along similar lines. However, we recognise that public money

must be accounted for in a certain way, including assuring regularity and propriety and with the necessary focus on value for money. With this in mind, for larger public bodies we have identified the following three options to deliver effective audit that conforms to the principles of public audit.

### **Option 1**

4.14. The scope of audit could be reduced to be more in line with that for companies, with no assessment of value for money. The auditor would:

- give an **opinion** on whether the financial statements give a true and fair view of the audited body's financial position and of its income and expenditure and
- review, and report on as appropriate, other information published with the financial statements, including the statement on internal control/annual governance statement, the remuneration report and the whole of government accounting summarisation schedules

4.15. This option would reduce the information available to local citizens on how local bodies are spending their money or on whether bodies are securing value for money.

### **Option 2**

4.16. As under the current system, the auditor would:

- give an **opinion** on whether the financial statements give a true and fair view of the audited body's financial position and of its income and expenditure; and
- provide a **conclusion** as to whether it has the proper arrangements in place to secure value for money (based on locally defined policy priorities) having regard to specified criteria (including financial resilience and regulatory and propriety)
- review, and report on as appropriate, other information published with the financial statements, including the statement on internal control/annual governance statement, the remuneration report and the whole of government accounting summarisation schedules

4.17. This option would maintain the current scope of audit. However, this option would not provide any additional information to local citizens on how local public bodies are spending their money or on whether bodies are securing value for money.

### **Option 3**

4.18. New arrangements could provide stronger assurances on the way local public bodies spend money. Under this option, the auditor would still give an **opinion** on the financial statements, but would provide **conclusions** on:

- regularity and propriety – a conclusion on compliance with relevant laws and regulations and the audited body's governance and control regime

- financial resilience – a conclusion about the future financial sustainability of the audited body and
- value for money – in addition to proper arrangements in place to secure value for money, a conclusion about the achievement of economy, efficiency and effectiveness within the audited body

4.19. We will need to consider carefully how a stronger value for money element to the audit would fit with other sectors, such as policing, who already have alternative systems for examining and reporting value for money publicly.

4.20. We believe that, compared to option 1 and 2, option 3 could lead to greater transparency for local citizens, and would help deliver the wide scope of public audit. It would also require a separate conclusion on regularity and propriety and financial resilience, rather than having regard to these aspects within a conclusion on value for money (as in option 2). However, the volume of work undertaken by the auditor would be significantly greater than for option 1. It is also possible that auditors would have difficulties in reaching a robust conclusion on value for money, regularity and propriety. We expect that reaching a conclusion on the achievement for value for money would involve more work for auditors, particularly in the case of complex organisations such as principal local authorities.

#### ***Option 4***

4.21. Local public spending should be transparent so that citizens can hold bodies to account. Companies are required, by law, to produce and publish an annual report, including the principal activities of the company during the year, and a business review which includes risks and uncertainties. Most public bodies also produce such a report, although local authorities are not currently required to do so.

4.22. Under this option, all local public bodies would be required to produce an annual report and to publish this report on their website. The report would set out the arrangements the audited body had put in place to secure value for money, whether they had achieved economy, efficiency and effectiveness, regularity and propriety and financial resilience.

4.23. The auditor would be required to:

- give an opinion on the financial statements
- review the audited body's annual report and
- provide reasonable assurance on the annual report

4.24. The annual report could be written in an accessible way and would be published. This option could therefore substantially increase the transparency of the local public bodies, compared to options 1 and 2. Citizens' increased knowledge of the local public body's financial performance could help drive greater local accountability. We would need to consider whether producing an annual report in an appropriate format would be a new burden for local authorities that do not currently produce an annual report in an appropriate format.

4.25. Another possible benefit of this option, is that it brings the format of audit for local public bodies (financial statements and reviewing a report) more in-line with that of other sectors.

**Q29: Which option would provide the best balance between costs for local public bodies, a robust assessment of value for money for the local taxpayer and provide sufficient assurance and transparency to the electorate? Are there other options?**

**Q30: Do you think local public bodies should be required to set out their performance and plans in an annual report? If so, why?**

**Q31: Would an annual report be a useful basis for reporting on financial resilience, regularity and propriety, as well as value for money, provided by local public bodies?**

**Q32: Should the assurance provided by the auditor on the annual report be 'limited' or 'reasonable'?**

**Q33: What guidance would be required for local public bodies to produce an annual report? Who should produce and maintain the guidance?**

## **Public interest reporting**

### **CURRENT SYSTEM**

4.26. Under Section 8 of the Audit Commission Act 1998, the auditor is currently required to consider whether to issue a report in the public interest on any significant matter coming to his or her notice in the course of an audit, and to bring it to the attention of the audited body and the public. The auditor can also make written recommendations to the audited body as part of this report. The audited body has a corresponding duty to consider and respond to these reports and any recommendations that might be made. The costs of the report fall on the audited body.

4.27. Appointed auditors have issued 131 public interest reports since 2002, of which 13 have related to principal local authorities, 85 to parish councils, 30 to health bodies and one each to a passenger transport authority (now an integrated transport authority), a passenger transport executive, and an internal drainage board.

4.28. In addition to the auditor's duties to report in the public interest, they also have the power to make a recommendation requiring a public response and can issue an advisory notice to the body if they have reason to believe the body is about to or has made a decision involving the unlawful incurring of expenditure.



## **OTHER SECTORS**

4.29. Although public interest reporting is a consequence of the principles of public audit, there are some similarities with processes in place in other sectors.

4.30. The auditor of a regulated entity generally has special reporting responsibilities in addition to the responsibility to report on financial statements. One of these special reporting responsibilities is a statutory duty to report certain information, relevant to the regulators' functions that come to the auditor's attention in the course of the audit work. This form of report is derivative in nature and is initiated by the auditor on discovery of a reportable matter.

## **OUR PROPOSALS**

4.31. We consider it is important that the duty on an auditor to consider whether to make a report in the public interest should be retained. Public interest reports are a key part of the current audit system and provide a vehicle through which the public are made aware of issues of significant interest to them. This is consistent with the design principles of localism and transparency.

4.32. We envisage that the current publication requirements for public interest reports would be retained, as would the audited body's responsibilities to consider the report at a meeting within one month of receipt and to publish a summary of the meeting's decision.

4.33. The costs of public interest reports will fall on the audited body. It has been suggested that the new direct contractual relationship between the audited bodies and their auditors could have, if unchecked, an impact on the ability or willingness of the auditor to issue a public interest report. However, we believe that if suitable safeguards are put in place for the resignation or removal of auditors, this will mitigate the risk.

4.34. We also propose to retain the power of an auditor to make a recommendation requiring a public response and to issue an advisory notice to the body if they have reason to believe the body is about to or has made a decision involving the unlawful incurring of expenditure.

**Q34: Do these safeguards also allow the auditor to carry out a public interest report without his independence or the quality of the public interest report being compromised?**

## **Provision of non-audit services**

### **CURRENT SYSTEM**

4.35. The auditor may be best placed to carry out certain types of additional work for the audited body. Therefore, the Audit Commission allows additional work to be undertaken without prior approval from the Commission, if the auditor is satisfied that:

- performance of such work will not compromise, nor be reasonably perceived by the public to compromise, his independence and
- the value of the work in total, in any audit year, does not exceed a de minimis amount (set by the Audit Commission as the higher of £30,000 or 20 per cent of the total audit fee, excluding fees for the certification of grant claims and returns)

4.36. Auditors are required to establish procedures to identify and address any potential breaches of these requirements.

4.37. All such work must be:

- agreed in advance with the audited body, on the understanding that such work is discretionary and is not required to meet the auditors' statutory responsibilities and
- billed separately from the audit work

The Commission requires applications for approval to carry out work exceeding the de minimis threshold at least ten days before the start of the work.

#### **OTHER SECTORS**

4.38. In other sectors, such as the companies sector, statutory auditors are allowed to provide other non-audit services to the company.

4.39. However, the audit committee of the company has a role in considering all relationships between the company and the audit firm, including the provision of non-audit services and whether, taken as a whole and having regard to the views, as appropriate, of the external auditor, management and internal audit, those relationships appear to impair the auditor's independence and objectivity.

4.40. The audit committee should also develop and recommend to the board the company's policy in relation to the provision of non-audit services by the auditor, and keep the policy under review. The audit committee's objective should be to ensure that the provision of such services does not impair the external auditor's independence or objectivity.

#### **OUR PROPOSALS**

4.41. We propose that auditors will be able to provide non-audit services to the audited body, but safeguards will be built into the system to prevent any actual or perceived threats to the auditor's independence. We recognise that by adding a number of safeguards into the system we could reduce the number of auditors eligible for appointment to an audited body, which would in turn affect competition.

4.42. We propose that auditors should continue to adhere to the ethical standards produced by the Auditing Practices Board and permission should be sought from the audit committee who would provide advice to the body on whether non-audit work should be undertaken as well as continuing to monitor the relationship between the auditor and the audited body.

**Q35: Do you agree that auditors appointed to a local public body should also be able to provide additional audit-related or other services to that body?**

**Q36: Have we identified the correct balance between safeguarding auditor independence and increasing competition? If not, what safeguards do you think would be appropriate?**

## **Public interest disclosure**

### **CURRENT SYSTEM**

4.43. Under the current framework, the Audit Commission and appointed auditors are prescribed persons under the Public Interest Disclosure Act 1998 for disclosures relating to “the proper conduct of public business, value for money, fraud and corruption in local government and health service bodies”. The Audit Commission and appointed auditors consider information they receive as a result of a disclosure and determine what action, if any, to take in the context of their existing statutory and professional powers and duties.

4.44. We recognise the importance of the roles undertaken by prescribed persons including the Audit Commission and appointed auditors. It provides reassurance to workers that it is safe and acceptable for them to raise concerns internally and sets out the circumstances where the disclosure of the malpractice outside of the organisation is in the public interest and should be protected.

### **The Audit Commission’s role in public interest disclosure**

The Audit Commission is a ‘prescribed person’ as set out in the Schedule to the Public Interest Disclosure Act. It exercises this role by:

- receiving the facts of a disclosure
- supporting the discloser by referring them to Public Concern at Work for further advice and guidance if subjected to victimisation or harassment;
- acknowledging receipt of the disclosure and stating in general terms what the procedures are
- forwarding information to the auditor and inform the discloser

#### *The current role of the appointed auditor*

The auditor’s role includes:

- evaluating the information provided by the Commission
- acknowledging receipt to the discloser, and providing an indication of the likely response, with an explanation for the decision
- undertaking appropriate audit work in response to the disclosure
- reporting the outcome of any work to the discloser and the Commission

## **OTHER SECTORS**

4.45. The Financial Reporting Council's guidance for the audit committees of companies sets out a role for the audit committee in reviewing arrangements under which staff of the company may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters. The audit committee's objective is to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.

## **OUR PROPOSALS**

4.46. We believe it is important that a similar system operates in the new framework. We propose that the Audit Commission's role (receiving, acknowledging receipt of and forwarding the facts of disclosure) should be broadly transferred to the audit committee of the local public body. The audit committee may choose to designate one of its independent members as a point of contact. As this role is an administrative role, which involves no need to consider the issue they are transferring, we do not see this as an additional burden on audit committees.

4.47. We envisage that the statutory auditor of the local public body would continue to be a prescribed person and would continue with his/her role with no change from the current system.

**Q37: Do you agree that it would be sensible for the auditor and the audit committee of the local public body to be designated prescribed persons under the Public Interest Disclosure Act? If not, who do you think would be best placed to undertake this role?**

## **Transparency**

### **CURRENT SYSTEM**

4.48. Members of the public currently have rights to question the auditor of an audited body about its accounts and raise objections, if the audited body is not a health body, in respect of unlawful items of account or matters on which the auditor can make a report in the public interest. The auditor may also apply for a declaration to the Court. Objectors have the right to appeal to the Courts about an auditor's decision.

4.49. Auditors have only limited discretion to refuse to investigate objections, but the costs of investigating objections, which are recovered from the local public body and, therefore, funded by council taxpayers, can be disproportionate to the sums involved in the complaint, or to the normal audit costs of the local public body.

4.50. The right to object to the accounts was first introduced more than 150 years ago, at a time when the auditor was the only individual to whom an elector could raise issues of concern.

## **OUR PROPOSALS**

- 4.51. The public can now raise concerns through a wide variety of appropriate avenues for redress, including the Local Government Ombudsman (in relation to maladministration) and the Information Commissioner (on matters concerning the rights that individuals have under the Freedom of Information and Data Protection Acts). Publication of all expenditure over £500 also makes spending more transparent and more readily available to the public.
- 4.52. With this in mind, we consider that the rights for local government electors to object to the accounts are both outdated and over-burdensome on auditors, local public bodies and council tax payers.
- 4.53. Under the new local audit framework, members of the public would retain the right to make representations to the auditor, raise issues with the auditor and to ask the auditor questions about the accounts.
- 4.54. While the right to make formal objections would be removed, the local public body would still be required to advertise that its accounts had been prepared and there will be increased publicity requirements for audited bodies. The auditor would still be open and transparent about the audit, and would consider any relevant representations from the public. The auditor would have discretion to decide whether to follow-up any issues raised by local citizens, having regard to the significance of the issue, the amounts of public money involved and the wider public interest. If the auditor decided not to consider a representation further, the decision would be amenable to judicial review, should the citizen who made the representation be dissatisfied with the decision.
- 4.55. We propose that auditors should also be brought within the remit of the Freedom of Information Act to the extent that they are carrying out their functions as public office holders. Therefore, only information in connection with a public audit would be within the remit of a freedom of information request. However, we recognise that there are costs associated with responding to freedom of information requests which could have an impact on audit fees. We would also need to consider whether this could be detrimental to the auditor and audited body's relationship.
- 4.56. We also envisage that local public bodies should be required to publish their accounts and the auditor's report on the website.
- 4.57. We consider that these proposals would provide a balance between transparency and disproportionate cost.

**Q38: Do you agree that we should modernise the right to object to the accounts? If not, why?**

**Q39: Is the process set out above the most effective way for modernising the procedures for objections to accounts? If not, what system would you introduce?**

**Q40: Do you think it is sensible for auditors to be brought within the remit of the Freedom of Information Act to the extent of their functions as public office holders? If not, why?**

**Q41: What will be the impact on (i) the auditor/audited body relationship, and (ii) audit fees by bringing auditors within the remit of the Freedom of Information Act (to the extent of their functions as public office holders only)?**

# Section 5

## 5. Arrangements for smaller bodies

### Current system

#### **The limited assurance audit regime**

The limited assurance audit regime was first introduced in 2001-02 for local councils (parish meetings and parish and town councils) where neither income nor expenditure exceeded £500,000. This threshold was increased to £1m in 2006.

The regime is designed specifically to minimise the audit requirement upon, and cost to, these small bodies. The audits are based on the submission by the body to the auditor of an annual return that is subject to a desk review. The audit report provides a limited level of assurance to the body commensurate with the amount of work undertaken.

The basic audit approach is common to all smaller bodies. However, for those bodies with annual income or expenditure over £200,000, auditors are required to carry out additional testing as part of their audit approach to reflect the higher risk to public funds; this is referred to as the intermediate audit. In addition, on a random sample basis, 5 per cent of those bodies operating below the £200,000 threshold will also be selected annually for intermediate audit at no extra cost.

- 5.1. Under the current legislation, the statutory audit requirements for smaller bodies are the same as those for larger bodies. However, since 2002, the Audit Commission has ensured that these are met proportionately through a separate “limited assurance” framework for bodies with an income or expenditure less than £1m. The smallest bodies currently do not pay any fees for their annual audit.
- 5.2. To bring this into line with the framework under the Companies Act the £1m threshold for local public bodies is being increased to not more than £6.5m.

#### **OTHER SECTORS**

- 5.3. The companies and charities sector, both have arrangements in place to ensure a more proportionate level of audit for smaller bodies.

#### **Charities**

- 5.4. The Charities Act 1993 put in place a system by which some small charities could be subject to independent examination rather than a full audit.

## Independent Examination v Audit (Charity Sector)

The two main differences between independent examination and audit relate to:

- Who can act
- The nature of the report.

	Who can act	The nature of the Report
<b>Independent Examination</b>	An independent person who is reasonably believed by the body to have the requisite knowledge and practical experience to carry out a competent examination of the accounts. No specific qualification is necessarily required but the person must have a good understanding of accounts.	Provides a "negative assurance" on the accounts. The independent examiner declares that no evidence was found of lack of accounting records, of accounts failing to comply with the records, nor of other matters that need to be disclosed.
<b>Audit</b>	Must be a registered auditor	An audit report will need to provide an opinion on the financial statements

5.5. The level of independent examination is dictated by the level of gross income of the charity.

Level of Gross Income	External scrutiny	Annual Report
Not exceeding £10,000	There is no requirement to have the accounts independently examined or audited	The trustees must prepare an annual report but it may be simplified.
Over £10,000 but not exceeding £100,000	Accounts must be subject to outside scrutiny but trustees may choose either independent examination or audit by a registered auditor	An Annual Report must be prepared but it may be simplified
Over £100,000 but not exceeding £500,000 (total assets not exceeding £2.8m)	Accounts must be subject to outside scrutiny but trustees may choose either independent examination or audit by a registered auditor.  If an independent examination is chosen and gross income exceeds £250,000 then the independent examiner appointed must be a member of a body specified under the 2006 Act.	An Annual Report must be prepared but it may be simplified
Exceeds £500,000 (or a charity whose gross assets exceed £2.8m and gross income exceeds £100,000)	A statutory audit is required (subject to specified exceptions) and the accounts must be audited by a registered auditor.	A full Annual Report must be prepared



- 5.6. Company charities used to be dealt with under the Companies Act 2006 system. However, from the financial year beginning on or after 1 April 2008 all charities (including company charities) are subject to the Charities Act 1993 system. The purpose of this change was to ensure that the scrutiny of small company charities was consistent with charity law requirements and in particular allowed for the independent examination of eligible small company charities.
- 5.7. Company charities which meet the Companies Act definition of a small company may elect for exemption from audit under the Companies Act and opt to have their accounts audited or independently examined under the Charities Act 1993.
- 5.8. Independent examination offers a lower cost alternative to charities that do not require the higher level of assurance that audit can provide. Changes effective from this date also result in new requirements for the audit of small groups when their accounts are prepared by parent company charities.

### **Companies**

- 5.9. The Companies Act 2006 sets out the thresholds which must be met for a company to be deemed a small company. These are, at least two of the following three conditions:
- annual income or expenditure (gross income for charities) not exceeding - £6,500,000
  - balance sheet total not exceeding - £3,260,000
  - average numbers of employers not exceeding – 50
- 5.10. These thresholds are subject to periodic amendment.
- 5.11. There is exemption from audit for **certain** small companies if they are eligible and wish to take advantage of it. To qualify for audit exemption, a company must:
- qualify as small (per paragraph 5.9) **and**
  - have an income or expenditure of not more than £6.5m **and**
  - have a balance sheet total of not more than £3.26m
- 5.12. Even if a small company meets these criteria, it must still have its accounts audited if this is demanded by a member or members holding at least 10 per cent of the nominal value of issued share capital or holding 10 per cent of any class of shares. Public companies are not eligible for exemption.

### **OUR PROPOSALS**

- 5.13. Both the limited assurance and independent examination regimes outlined above provide a simpler, more proportionate, form of external scrutiny than a full audit, but still provide assurance that the accounts of the bodies involved have been reviewed by an independent person.

- 5.14. We aim to bring arrangements for smaller local public bodies into line with other sectors. We are therefore considering a process under which the income and expenditure of a body determines what 'level' of audit or scrutiny is required; the greater the income/expenditure, the more scrutiny is required.
- 5.15. We propose that the 1,200 or so bodies with income or expenditure less than £1,000 would not be subject to an external examination or audit, as the risk to public funds is low and any external examination or audit fees would be disproportionate to their income or expenditure. These bodies do not currently pay a fee for an audit or examination, and requiring them to now do so would clearly increase their costs.
- 5.16. Bodies with an income or expenditure between £1,000 and the upper threshold of £6.5m would be subject to an independent examination rather than a full audit.
- 5.17. Examiners of small bodies should act for a maximum period of 10 years (which is in line with the current practices of the Audit Commission).
- 5.18. We propose that the independent examination of smaller bodies should be similar to that followed in the charities sector. As we have set out above, the charities sector provides for a reduced audit for bodies with income or expenditure below £500,000. However, the Audit Commission has provided limited assurance to all bodies with income or expenditure under £1m recently raised to not more than £6.5m. We are keen to ensure that smaller bodies are not disproportionately affected by our proposals. Therefore we propose a staged model such as the model followed in the charities sector, where the level of examination and the qualifications that the independent examiner must have are based on the income or expenditure of the body. However, this staged model would reflect the current £6.5m threshold used by the Audit Commission for their limited assurance regime. The independent examination of smaller bodies might therefore look as follows:

	Number	% small bodies market	Income/Expenditure	Scrutiny
<b>Level 1</b>	1,200	12%	Public bodies with expenditure less than £1,000	<ul style="list-style-type: none"> <li>Existing governance and accounting arrangements</li> <li>Annual accounts published</li> <li>Positive confirmation that annual accounts have been produced and published via the precept request (or equivalent)</li> <li>No external audit/scrutiny</li> </ul>
<b>Level 2</b>	Approx 6,400 bodies	64%	Public bodies with expenditure between £1,000 and £50,000	<p>As level 1, but</p> <ul style="list-style-type: none"> <li>(Under option 1 below) the county or unitary council to appoint an independent examiner (no specific qualifications needed, but County or unitary council should assure itself that the relevant person has the requisite experience and expertise) to assess its accounts. In practice the Section 151 officer or full council, having regard to advice provided by the audit committee, would make this appointment. The independent examiner might be an officer of the county or unitary council.</li> <li>The body must also publish the details of the examiner.</li> </ul>
<b>Level 3</b>	Approx 1,625 bodies	16%	Public bodies with expenditure between £50,000 and £250,000	<p>As level 2, but:</p> <ul style="list-style-type: none"> <li>Existing internal audit arrangements</li> <li>Independent examiner must hold a professional qualification to assess its accounts.</li> </ul>
<b>Level 4</b>	Approx 675 bodies	7%	Public bodies with expenditure between £250,000 and £6.5m	<p>As level 3, but</p> <ul style="list-style-type: none"> <li>Independent examiner must hold a professional qualification and be registered as a public auditor.</li> </ul>

## Appointing the examiner

### OPTION 1

5.19. We consider that the appointment process for the independent examiner should be proportionate. An audit committee could be a significant cost for a smaller body. Instead, where an independent examiner is required, we propose that the county or unitary authority should be responsible for appointing the independent examiner (see table above). If smaller bodies were responsible for appointing their own examiner in the absence of an audit committee there would be a lack of independence in the appointment process. In addition, they may not achieve a good price for this service.

5.20. If the county or unitary authority was responsible for the appointment this would provide a degree of independence to the appointment process for smaller bodies, and they would have the ability to appoint independent examiners for all of the smaller bodies in their areas, providing the opportunity to make savings through economies of scale.

### OPTION 2

5.21. The small body would be required to make arrangements for the appointment of the independent examiner, **including** the involvement of an audit committee. This would give the body the freedom to make the necessary arrangements which might include joining up with other small bodies, either locally or providing similar services. The smaller bodies would be able to arrange a joint audit committee, with safeguards to provide for independence. Alternatively, the small body would be able to join with a larger local public body and utilise their audit committee. Under this option the scope of the examination would still be as set out in the table above.

**Q42: Which option provides the most proportionate approach for smaller bodies? What could happen to the fees for smaller bodies under our proposals?**

**Q43: Do you think the county or unitary authority should have the role of commissioner for the independent examiners for smaller bodies in their areas? Should this be the section 151 officer, or the full council having regard to advice provided by the audit committee? What additional costs could this mean for county or unitary authorities?**

**Q44: What guidance would be required to enable county/unitary authorities to:**

- a.) Appoint independent examiners for the smaller bodies in their areas?**
- b.) Outline the annual return requirements for independent examiners?**

**Who should produce and maintain this guidance?**

**Q45: Would option 2 ensure that smaller bodies appoint an external examiner, whilst maintaining independence in the appointment?**

**Q46: Are there other options given the need to ensure independence in the appointment process? How would this work where the smaller body, e.g. a port health authority, straddles more than one county/unitary authority?**

**Q47: Is the four-level approach for the scope of the examination too complex? If so, how would you simplify it? Should the threshold for smaller bodies be not more than £6.5m or £500,000? Are there other ways of dealing with small bodies, e.g. a narrower scope of audit?**

### **Public interest reporting for smaller bodies**

5.22. There would be no auditor to receive queries or objections from the public, and there would be no public interest reporting. However, if the examiner identified issues giving cause for concern we propose that these could be raised with the audited body, or the county or unitary authority. The county or unitary authority could be given the power to appoint an auditor to then carry out a public interest report on the matters raised with the audited body. Sanctions could include a power to make the next precept (partly or wholly) conditional on the matters raised being addressed.

**Q48: Does this provide a proportionate, but appropriate method for addressing issues that give cause for concern in the independent examination of smaller bodies? How would this work where the county council is not the precepting authority?**

### **Objections to accounts of smaller bodies**

5.23. For bodies with an income or expenditure greater than £6.5 million we are proposing to modernise the system for dealing with objections to accounts.

5.24. In the case of smaller bodies, we propose that the independent examiner would be able to consider whether to refer issues raised by citizens to the proper officer (possibly the s151 officer) of the county or unitary authority. That authority would be provided with powers to take action, which might include appointing an auditor to consider those issues and report in public to the examined body. The costs for dealing with the representation would fall to the smaller body.

**Q49: Is the process set out above the most appropriate way to deal with issues raised in relation to accounts for smaller bodies? If not, what system would you propose?**

### **Regulatory regime for smaller bodies**

5.25. For smaller bodies the more proportionate approach described of independent examination would not give rise to the same level of scrutiny as an external audit.

5.26. However, if appointing the independent examiner to the smaller body, or if provided with powers to take action, which might include appointing an auditor to carry out a public interest report, the county or unitary council would, essentially, be the regulator for this sector.

**Q50: Does this provide a proportionate but appropriate system of regulation for smaller bodies? If not, how should the audit for this market be regulated?**

# Section 6

## 6. List of consultation questions

1. Have we identified the correct design principles? If not what other principles should be considered? Do the proposals in this document meet these design principles?
2. Do you agree that the audit probation trusts should fall within the Comptroller and Auditor General's regime?
3. Do you think that the National Audit Office would be best placed to produce the Code of audit practice and the supporting guidance?
4. Do you agree that we should replicate the system for approving and controlling statutory auditors under the Companies Act 2006 for statutory local public auditors?
5. Who should be responsible for maintaining and reviewing the register of statutory local public auditors?
6. How can we ensure that the right balance is struck between requiring audit firms eligible for statutory local public audit to have the right level of experience, while allowing new firms to enter the market?
7. What additional criteria are required to ensure that auditors have the necessary experience to be able to undertake a robust audit of a local public body, without restricting the market?
8. What should constitute a public interest entity (i.e. a body for which audits are directly monitored by the overall regulator) for the purposes of local audit regulation? How should these be defined?
9. There is an argument that by their very nature all local public bodies could be categorised as 'public interest entities.' Does the overall regulator need to undertake any additional regulation or monitoring of these bodies? If so, should these bodies be categorised by the key services they perform, or by their income or expenditure? If the latter, what should the threshold be?
10. What should the role of the regulator be in relation to any local bodies treated in a manner similar to public interest entities?
11. Do you think the arrangements we set out are sufficiently flexible to allow councils to cooperate and jointly appoint auditors? If not, how would you make the appointment process more flexible, whilst ensuring independence?
12. Do you think we have identified the correct criteria to ensure the quality of independent members? If not, what criteria would you suggest?

13. How do we balance the requirements for independence with the need for skills and experience of independent members? Is it necessary for independent members to have financial expertise?
14. Do you think that sourcing suitable independent members will be difficult? Will remuneration be necessary and, if so, at what level?
15. Do you think that our proposals for audit committees provide the necessary safeguards to ensure the independence of the auditor appointment? If so, which of the options described in paragraph 3.9 seems most appropriate and proportionate? If not, how would you ensure independence while also ensuring a decentralised approach?
16. Which option do you consider would strike the best balance between a localist approach and a robust role for the audit committee in ensuring independence of the auditor?
17. Are these appropriate roles and responsibilities for the Audit Committee? To what extent should the role be specified in legislation?
18. Should the process for the appointment of an auditor be set out in a statutory code of practice or guidance? If the latter, who should produce and maintain this?
19. Is this a proportionate approach to public involvement in the selection and work of auditors?
20. How can this process be adapted for bodies without elected members?
21. Which option do you consider provides a sufficient safeguard to ensure that local public bodies appoint an auditor? How would you ensure that the audited body fulfils its duty?
22. Should local public bodies be under a duty to inform a body when they have appointed an auditor, or only if they have failed to appoint an auditor by the required date?
23. If notification of auditor appointment is required, which body should be notified of the auditor appointment/failure to appoint an auditor?
24. Should any firm's term of appointment be limited to a maximum of two consecutive five-year periods?
25. Do the ethical standards provide sufficient safeguards for the rotation of the engagement lead and the audit team for local public bodies? If not, what additional safeguards are required?



26. Do the proposals regarding the reappointment of an audit firm strike the right balance between allowing the auditor and audited body to build a relationship based on trust whilst ensuring the correct degree of independence?
27. Do you think this proposed process provides sufficient safeguard to ensure that auditors are not removed, or resign, without serious consideration, and to maintain independence and audit quality? If not, what additional safeguards should be in place?
28. Do you think the new framework should put in place similar provision as that in place in the Companies sector, to prevent auditors from seeking to limit their liability in an unreasonable way?
29. Which option would provide the best balance between costs for local public bodies, a robust assessment of value for money for the local taxpayer and provides sufficient assurance and transparency to the electorate? Are there other options?
30. Do you think local public bodies should be required to set out their performance and plans in an annual report? If so, why?
31. Would an annual report be a useful basis for reporting on financial resilience, regularity and propriety, as well as value for money, provided by local public bodies?
32. Should the assurance provided by the auditor on the annual report be 'limited' or 'reasonable'?
33. What guidance would be required for local public bodies to produce an annual report? Who should produce and maintain the guidance?
34. Do these safeguards also allow the auditor to carry out a public interest report without his independence or the quality of the public interest report being compromised?
35. Do you agree that auditors appointed to a local public body should also be able to provide additional audit-related or other services to that body?
36. Have we identified the correct balance between safeguarding auditor independence and increasing competition? If not, what safeguards do you think would be appropriate?
37. Do you agree that it would be sensible for the auditor and the audit committee of the local public body to be designated prescribed persons under the Public Interest Disclosure Act? If not, who do you think would be best placed to undertake this role?
38. Do you agree that we should modernise the right to object to the accounts? If not, why?

39. Is the process set out above the most effective way for modernising the procedures for objections to accounts? If not, what system would you introduce?
40. Do you think it is sensible for auditors to be brought within the remit of the Freedom of Information Act to the extent of their functions as public office holders? If not, why?
41. What will be the impact on (i) the auditor/audited body relationship, and (ii) audit fees by bringing auditors within the remit of the Freedom of Information Act (to the extent of their functions as public office holders only)?
42. Which option provides the most proportionate approach for smaller bodies? What could happen to the fees for smaller bodies under our proposals?
43. Do you think the county or unitary authority should have the role of commissioner for the independent examiners for smaller bodies in their areas? Should this be the section 151 officer, or the full council having regard to advice provided by the audit committee? What additional costs could this mean for county or unitary authorities?
44. What guidance would be required to enable county/unitary authorities to:
- a.) Appoint independent examiners for the smaller bodies in their areas?
  - b.) Outline the annual return requirements for independent examiners?
- Who should produce and maintain this guidance?
45. Would option 2 ensure that smaller bodies appoint an external examiner, whilst maintaining independence in the appointment?
46. Are there other options given the need to ensure independence in the appointment process? How would this work where the smaller body, e.g. a port health authority, straddles more than one county/unitary authority?
47. Is the four-level approach for the scope of the examination too complex? If so, how would you simplify it? Should the threshold for smaller bodies be not more than £6.5m or £500,000? Are there other ways of dealing with small bodies, e.g. a narrower scope of audit?
48. Does this provide a proportionate, but appropriate method for addressing issues that give cause for concern in the independent examination of smaller bodies? How would this work where the county council is not the precepting authority?
49. Is the process set out above the most appropriate way to deal with issues raised in relation to accounts for smaller bodies? If not, what system would you propose?
50. Does this provide a proportionate but appropriate system of regulation for smaller bodies? If not, how should the audit for this market be regulated?

# Appendix A

## **Audited bodies' published accounts – current arrangements**

The annual accounting statements that audited bodies, other than NHS bodies and probation bodies, are currently required to publish are prescribed in Accounts and Audit Regulations made under section 27 of the Audit Commission Act 1998. A new consolidated set of the regulations has recently been issued. The accounting statements for all the bodies must cover the year ending on 31 March.

The larger bodies (broadly those with annual income or expenditure of more than £6.5m) must produce a “statement of accounts”, based, as from the 2010-11 financial year, on International Financial Reporting Standards as those standards are applied by the *Code of Practice on Local Authority Accounting in the United Kingdom*, published by CIPFA/LASAAC. The statement must also conform to specific requirements set out in the Accounts and Audit Regulations and other legislation. A statement of accounts includes all the elements that would be expected in a comprehensive set of accounts, including:

- movement in reserves statement
- comprehensive income and expenditure account
- balance sheet
- cash flow statement, and
- supporting notes, including a summary of significant accounting policies

Where the body has significant subsidiaries or associates Group Accounts must also be included. The statement of accounts is accompanied by a statement of internal control or annual governance statement, setting out the body's annual assessment of how it is managing and controlling the risks it faces in achieving its aims and legal obligations.

The smaller bodies are given a choice on the form of their annual accounting statements. They can prepare either:

- a statement of accounts on the same basis as a larger body or
- an income and expenditure account and statement of balances or
- where the body's annual income or expenditure is no more than £200,000, a record of receipts and payments

For the second and third options the requirements are specified in an Annual Return that the body is required to present to the auditor and publish. The form of the Annual Return is laid out in *Governance and Accountability for Local Councils, a Practitioners' Guide*, available from the National Association of Local Councils.

The accounting statements for both the larger and smaller bodies must be audited (for smaller bodies the audit is a 'limited assurance' - a simpler, more proportionate, form of external scrutiny than a full audit). The statements, together with the auditor's opinion on them, must then be published, and this should be done by 30 September following the financial year end. The larger bodies are required to publish the statements on their websites, and the smaller bodies by displaying them within their area, though both are free to use other means of publication in addition.

## Appendix B

### List of bodies to which the Audit Commission appoints auditors in England

The audit bodies which are specified in primary legislation are<sup>3</sup>:

- A local authority (meaning a county council, district council, London borough council and a parish council).
- A joint authority (which means an authority established by Part 4 of the Local Government Act 1985, includes metropolitan county fire and rescue authorities).
- The Greater London Authority.
- Passenger Transport Executive.
- A functional body (meaning Transport for London, the London Development Agency, the Metropolitan Police Authority and the London Fire and Emergency Planning Authority).
- The London Pensions Fund Authority.
- The London Waste and Recycling Board.
- A parish meeting of a parish not having a separate parish council.
- A committee of a local authority, including a joint committee of two or more such authorities.
- The Council of the Isles of Scilly.
- Any Charter Trustees constituted under section 246 of the Local Government Act 1972.
- A Health Service Body prepared under paragraph 3(1) of Schedule 15 to the National Health Service Act 2006.
- A Port Health Authority constituted under section 2 of the Public Health (Control of Disease) Act 1984.
- The Broads Authority.
- A national park authority.
- A conservation board established by order under section 86 of the Countryside and Rights of Way Act 2000.
- A police authority established under section 3 of the Police Act 1996.
- A fire and rescue authority constituted by a scheme under Section 2 of the Fire and Rescue Services Act 2004 or a scheme to which section 4 of that Act applies.
- An authority established for an area in England by an order under section 207 of the Local Government and Public Involvement in Health Act 2007 (joint waste authorities).
- A licensing planning committee.
- An internal drainage board.
- A local probation board established under section 4 of the Criminal Justice and Court Services Act.

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<sup>3</sup> It is proposed through the Police Reform and Social Responsibility Bill that police and crime commissioners and chief constables will be added to schedule 2 of the Audit Commission Act 1998 and thereby become a body for which the Audit Commission will appoint auditors to. In addition, the Health Bill refers to GP Consortia being brought within the Audit Commission Act 1998.

- A probation trust.
- An economic prosperity board established under section 88 of the Local Democracy, Economic Development and Construction Act 2009.
- A combined authority established under section 103 of that Act.
- The accounts of the collection fund of the Common Council and the accounts of the City fund.
- The accounts relating to the superannuation fund maintained and administered by the Common Council under the Local Government Pension Scheme Regulations 1995.

## Appendix C

### **Recognised supervisory bodies and recognised qualifying bodies in England**

In the companies sector, audit firms must be registered with, and subject to supervision by a recognised supervisory body and persons responsible for company audit work at a firm must hold a recognised qualification awarded by a recognised qualifying body.

There are currently five recognised supervisory bodies:

- Association of Authorised Public Accountants
- Association of Chartered Certified Accountants
- Institute of Chartered Accountants in England and Wales
- Institute of Chartered Accountants in Ireland
- Institute of Chartered Accountants in Scotland

and six recognised qualifying bodies:

- Association of Chartered Certified Accountants
- Association of International Accountants
- Chartered Institute of Public Finance and Accountancy
- Institute of Chartered Accountants in England and Wales
- Institute of Chartered Accountants in Ireland
- Institute of Chartered Accountants in Scotland



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