

**Meeting of:** AUDIT COMMITTEE

**Date:** 25 January 2006

**Report of:** INTERNAL AUDIT MANAGER

**Reference:** aud/audcomm/250106

**Title:** CIPFA GUIDANCE ON AUDIT COMMITTEES IN LOCAL GOVERNMENT

## **PUBLIC/EXEMPT ITEM**

This item is for consideration in the public part of the meeting.

## **PURPOSE OF THE REPORT**

To assess the Audit Committee's current arrangements against the CIPFA Guidance and in relation to the Audit Commission's criteria for evaluating the Council's "Use of Resources".

## **RECOMMENDATIONS**

- 1. That the content of the CIPFA (Chartered Institute of Public Finance and Accountancy) Publication is noted.**
- 2. That officers undertake a review of the Committee's terms of reference , to be reported to the next meeting of the Audit Committee in April 2006, with a view to recommending changes to Council in May 2006 if required. Also that this review consider issues relating to the separate roles and responsibilities of the Audit Committee, the Standards Committee and Overview and Scrutiny.**
- 3. That Members consider whether, and in what circumstances they would wish to hold private meetings with the Internal Auditor or External Auditor.**
- 4. That consideration is given to the need for, and format of further Member training.**

## **REPORT**

### **Introduction**

#### **CIPFA Publication – "Audit Committees; Practical Guidance For Local Authorities"**

- 1. In November 2005, CIPFA published guidance for local authorities on the roles, functions and operation of audit committees. A copy of the Executive Summary of that guidance is attached as Appendix A.**
- 2. The Audit Committee's current terms of reference are reproduced at Appendix B.**
- 3. Suggested terms of reference for an Audit Committee (per the CIPFA Guidance) are reproduced at Appendix C.**
- 4. A self-assessment checklist (included in the CIPFA guidance) aimed at measuring the effectiveness of the Audit Committee has been completed and is reproduced at Appendix D. It is pleasing to note that a positive response has been given to 17 out of the 24 questions.**

5. Of the seven questions where a “No” response has been given, four areas are considered to be of greater significance and these are explored in greater detail below.

**Question 2 - Do the terms of reference follow the CIPFA Model?**

6. The following omissions have been identified:

Omission	Suggested Response
To liaise with the Audit Commission over the appointment of the council's external auditor	That this be considered in a review of the Committee's Terms of Reference prior to the next meeting of the Committee.
To commission work from internal and external audit	Given that both audit plans are presented to the Audit Committee, it is considered that any member concerns can be adequately discussed under current arrangements with the potential to amend plans, subject to resource constraints.
To maintain an overview of the council's constitution in respect of contract procedure rules, financial regulations and codes of conduct and behaviour; AND To monitor council policies on “Raising Concerns at Work “ and the anti-fraud and corruption strategy and the council's complaints process	Monitoring and advising the Council about the operation of its Code of Conduct for Members are currently set out as terms of reference of the Standards Committee, as are monitoring and reviewing the operation of the Council's Whistleblowing Policy. Response to the CIPFA guidance has included cautionary comments from some quarters about confusing and/or duplicating the roles of the Audit Committee, Standards Committee and Overview & Scrutiny.  In such circumstances, any change to the existing terms of reference of the Audit Committee must be considered within the wider context of the overall governance framework.  That said, where practicable, the Audit Committee is and should continue to be “consulted” on key governance documents and processes.
To review any issue referred to it by the chief executive or a director, or any council body	Such an omission does not warrant an immediate change to the existing terms of reference
To approve a Statement of Purpose	Such an omission does not warrant immediate action

7. Given that the suggested terms of reference could encroach on those of other Committees, it is recommended that a review is undertaken and reported to the next meeting of the Audit Committee in April 2006, with a view to recommending changes to Council in May 2006 as necessary.

**Question 13 - Are members sufficiently independent of the other key committees of the council?**

8. The CIPFA guidance stipulates that the Audit Committee should include not more than one from each of the Executive and Overview & Scrutiny. The current membership includes two members of Cabinet and two members of the Budget & Performance Panel. With a membership of seven, the Committee is relatively large for the type of organization.
9. At a CIPFA Seminar in December 2005, following up the publication of the guidance, it was stressed that in terms of the workings of the Audit Committee “independence of attitude” was as important a feature as independence from other responsibility. There are practical benefits in having the Cabinet member with responsibility for finance on the Committee as well as the Chairman of the Budget & Performance Panel.
10. Members may wish to consider the CIPFA guidance on this matter. In practical terms, the independence expected of the Audit Committee may be most efficiently promoted through the provision of training on Members’ roles and responsibilities (see the following paragraphs).

**Question 14 – Have all members’ skills and experience been assessed and training given for identified gaps (also related to questions 21 and 22)**

11. The CIPFA document places great emphasis on Member training and suggests the following topics are covered:

<b>Induction Training</b>	<b>Advanced Training</b>
The role of the committee	Financial reporting
The terms of reference	Governance (including the Statement on Internal Control)
The time input required of members	Understanding financial statements
An overview of council activities	The regularity framework
The financial and risk environment	The role of internal and external audit
	The importance of risk management

12. Members may wish to reflect on this matrix. Further training could be provided in a variety of ways to suit the subject matter and Members’ personal needs.

**Question 16 – Are separate, private meetings held with the external auditor and the internal auditor?**

13. The CIPFA Guidance suggests that there should be the opportunity for both the Internal Auditor and External Auditor to meet privately with the Committee. Whilst there is nothing in the Committee’s terms of reference to either allow or preclude such meetings, they have not, to date, taken place. Under Financial Regulations, the Internal Audit Manager does have the right of access to elected Members.
14. Aside from providing the auditors with the opportunity to report any significant concerns directly to members of the Committee, a key purpose of such meetings would be to enable Members to develop their own programmes and priorities, review and influence audit activity and explore ways of obtaining assurance in areas of particular importance to the Committee.
15. Members are asked to consider whether, and in what circumstances they might wish to meet privately with the Internal Auditor or External Auditor.

## **FINANCIAL IMPLICATIONS**

None arising from this report.

## **LEGAL IMPLICATIONS**

Legal Services have been consulted and have no further comments.

## **MONITORING OFFICER'S COMMENTS**

The Terms of Reference of each Council Committee are very clearly set out in the Constitution. If members believe a review is necessary, the scope of the review needs very careful consideration. Whilst the Audit Committee has overall responsibility for Corporate Governance within the Council, each of the Personnel Committee, Standards Committee, and Overview and Scrutiny Committee has a role to play in governance arrangements. At present, as Monitoring Officer I haven't received any concerns regarding the functioning of these committees.

With regard to Member training, each individual Member is currently being canvassed to assess their specific training needs. It is anticipated that the outcome of this exercise will be a member training programme for 2006/7 that accommodates both individual and corporate training needs.

## **SECTION 151 OFFICER'S COMMENTS**

The Section 151 Officer has been consulted and has no further comments.

## **BACKGROUND PAPERS**

CIPFA Publication entitled "Audit Committees – Practical Guidance for Local Authorities"  
Council Constitution

## **APPENDIX A**

### **CIPFA Publication – Audit Committees – Practical Guidance for Local Authorities**

#### **Executive Summary**

Although audit committees have been a feature of the public sector for some time, there has been a lack of clarity about how they should operate in local government. Audit committees are not just the concern of auditors; they are about the governance, financial reporting and performance of the whole authority. Yet the fact that local government is not required to establish them is unique in the public sector – less than half of all local authorities have audit committees.

Good corporate governance requires independent, effective assurance about the adequacy of financial management and reporting. These functions are best delivered by an audit committee, independent from the executive and scrutiny functions.

Effective audit committees help raise the profile of internal control, risk management and financial reporting issues within an organisation, as well as providing a forum for the discussion of issues raised by internal and external auditors. And they enhance public trust and confidence in the financial governance of an authority.

Now Comprehensive Performance Assessment sets a challenge to local authorities (in England) to ensure that their audit committees work effectively.

This guidance has been written to help those authorities that do not already have an audit committee to implement one effectively, and to help those authorities that have audit committee arrangements in place to assess whether they are as effective as they need to be to contribute to good governance.

CIPFA seeks to address the key issues in a discursive manner, without being prescriptive, as the variety of types, styles and sizes of local authorities mitigates against a single model for all.

This guidance therefore seeks to consider the key issues for all authorities to help them address the principles.

CIPFA stresses that audit committees have a key role in corporate governance. They should therefore be clearly integrated into an authority's governance framework.

This guidance explores the main purpose of an audit committee and concludes that these include giving independent assurance to members and the public, scrutinising financial management and reporting, and providing challenge across the council.

In addition to internal and external audit, the functions overseen by the committee should include a number of control strategies such as risk management, the authority's governance and assurance statements, and anti-fraud and anti-corruption arrangements.

This guidance identified a range of benefits to an authority from operation of an effective audit committee. These include increasing public confidence, highlighting the independence of audit, and raising awareness of the importance of internal controls. Consultees have assisted in highlighting a range of characteristics and success factors that help to identify when a committee is effective.

In terms of structure, CIPFA believes that the audit committee must be independent of the executive and scrutiny functions and that it must have a clear right of access to full council, other council groups and committees. The number of members and the frequency of meetings are not prescribed, but this publication gives guidance to allow authorities to determine their own approach.

This guidance stresses the importance of the audit committee's relationship with the authority's chief finance officer. The audit committee helps the officer to discharge his or her statutory functions. In turn, this officer is a key source of expert advice and guidance for the audit committee.

Audit committees exist in a number of councils, although not necessarily in name. What is important is the operation of the function of an effective audit committee. Status and independence are important, but being effective also means having well informed people able to confirm to the council that the right processes are in place to give confidence that the authority's financial stewardship and overall governance arrangements can be relied upon.

Everyone charged with the responsibility for governance in their authority will want to familiarize themselves with the issues covered by this guidance to enable their audit committees to work effectively.

## Appendix B

### SECTION 8 – AUDIT COMMITTEE

**Composition: 7 Members of the Council on a PR basis, Chairman and Members of the Committee appointed by Council annually. Changes can be made by Council during the course of the year.**

#### Terms of Reference

- 1 To review all matters relating to Internal and External Audit. It will have the right of access to all the information it considers necessary and can consult directly with Internal and External Auditors.
- 2 To monitor arrangements for discharging the Council's responsibilities for efficient and effective financial and operational resource management. In pursuing this aim, it will consider:-
  - the soundness, adequacy and application of controls;
  - compliance with policies, procedures and statutory requirements;
  - arrangements for safeguarding the Council's assets and interests;
  - the integrity and reliability of management information and financial records;
  - the economic, efficient and effective use of resources.
- 3 To approve the annual Statement of Accounts, income and expenditure and balance sheet or record of payments and receipts under the Account and Audit Regulations 1996.
- 4 To approve the Audit Plan of the External Auditor.
- 5 To monitor the External Auditor's progress with the Annual Plan, including his comments on the Best Value Performance Plan and the production of agreed outputs.
- 6 To approve Internal Audit strategic plans and the Annual Internal Audit Plan.
- 7 To monitor Internal Audits progress with the Annual Audit Plan, evaluating the effectiveness of Internal Audit and the use of Audit resources and recommending adjustments to the Audit Plan.
- 8 To review and comment upon liaison arrangements between Internal and External Audit with a view to optimising the effective deployment of Audit resources.
- 9 To evaluate the adequacy and effectiveness of the Council's financial and operational policies and procedures including financial and accounting management through discussions with the External Auditors, Internal Auditors and appropriate officers.
- 10 To receive and review the findings of both Internal and External Audit examinations and to ensure that management takes appropriate action to implement agreed recommendations and to remedy any internal accounting, organisational or operational control weaknesses identified.
- 11 To receive the annual Internal Audit Report and annual controls assurance statement.
- 12 To monitor the effectiveness of the Code of Corporate Governance.
- 13 To refer to Council any matters it shall see fit.
- 14 To consider any matters referred to it by the Monitoring Officer in accordance with Overview and Scrutiny Procedure Rule 12.
- 15 With the Monitoring Officer to monitor and review the operation of the Constitution to ensure the aims and principles of the Constitution are given full effect.
- 16 To consider and approve amendments to the Council's Financial Regulations and

Contract Procedure Rules.

- 17 To consider and propose to Council any other amendments to the Constitution as necessary.
- 17 To act as the mechanism for Members of the Council to liaise with the Independent Remuneration Panel on the Members' Allowances Scheme.

## **DELEGATIONS TO OFFICERS**

### **To the Chief Executive**

To sanction emergency action, as set out in the rules of procedure for urgent business.



## **APPENDIX C**

### **CIPFA GUIDANCE – SUGGESTED AUDIT COMMITTEE TERMS OF REFERENCE**

#### **Audit Activity**

- (a) To consider the head of internal audit's annual report and opinion, and a summary of internal audit activity (actual and proposed) and the level of assurance it can give over the council's corporate governance arrangements.
- (b) To consider summaries of specific internal audit reports as requested.
- (c) To consider reports dealing with the management and performance of the providers of internal audit services.
- (d) To consider a report from internal audit on agreed recommendations not implemented within a reasonable timescale.
- (e) To consider the external auditor's annual letter, relevant reports, and the report to those charged with governance.
- (f) To consider specific reports as agreed with the external auditor.
- (g) To comment on the scope and depth of external audit work and to ensure it gives value for money.
- (h) To liaise with the Audit Commission over the appointment of the council's external auditor.
- (i) To commission work from internal and external audit.

#### **Regulatory Framework**

- (j) To maintain an overview of the council's constitution in respect of contract procedures rules, financial regulations and codes of conduct and behaviour.
- (k) To review any issue referred to it by the chief executive or a director, or any council body.
- (l) To monitor the effective development and operation of risk management and corporate governance in the council.
- (m) To monitor council policies on "Raising Concerns at Work" and the anti-fraud and corruption strategy and the council's complaints process.
- (n) To oversee the council's arrangements for corporate governance and agreeing necessary actions to ensure compliance with best practice.
- (o) To consider the council's compliance with its own and other published standards and controls.

#### **Accounts**

- (p) To review the annual statement of accounts. Specifically, to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements or from the audit that need to be brought to the attention of the council.
- (q) To consider the external auditor's report to those charged with governance on issues arising from the audit of accounts.

## APPENDIX D

### CIPFA SELF ASSESSMENT CHECKLIST – MEASURING THE EFFECTIVENESS OF THE AUDIT COMMITTEE

Issue	Ref	Yes	No	Comment
<b>Terms of Reference</b>				
Have the committee's terms of reference been approved by full council?	1	Yes		
<p>Do the terms of reference follow the CIPFA model?</p> <p>Note: CIPFA also recommends that a local authority should formally approve a Statement of Purpose, along the following lines:</p> <p><i>“The purpose of an audit committee is to provide independent assurance of the adequacy of the risk management framework and the associated control environment, independent scrutiny of the authority's financial and non-financial performance to the extent that it affects the authority's exposure to risk and weakens the control environment, and to oversee the financial reporting process”</i></p>	2		No	<p>In the main, the terms of reference do follow the CIPFA model. The following areas set out in the CIPFA model are not explicitly defined within the Council's terms of reference:</p> <p><b><u>Audit Activity</u></b></p> <ul style="list-style-type: none"> <li>To liaise with the Audit Commission over the appointment of the council's external auditor</li> <li>To commission work from internal and external audit</li> </ul> <p><b><u>Regulatory Framework</u></b></p> <ul style="list-style-type: none"> <li>To review any issue referred to it by the chief executive or a director, or any council body</li> <li>To monitor council policies on “Raising Concerns at Work” and the anti-fraud and corruption strategy and the council's complaints process</li> <li>To oversee the council's arrangements for corporate governance and agreeing necessary actions to ensure compliance with best practice.</li> </ul> <p>Note: A Statement of Purpose has not been approved</p>

Issue	Ref	Yes	No	Comment
<b>Internal Audit Process</b>				
Does the committee approve the strategic audit approach and the annual programme?	3	Yes		Strategic approach and Annual Plan 2004/05 approved at meeting on 27 July 2005
Is the work of internal audit reviewed regularly?	4	Yes		Internal Audit monitoring reports are submitted to meetings during the year.
Are summaries of quality questionnaires from managers reviewed?	5		No	Quality questionnaires are obtained from managers following the completion of each audit. This information will be included in future monitoring reports.
Is the annual report, from the head of audit, presented to the committee?	6	Yes		Annual report and Controls Assurance Statement was presented to committee on 19 October 2005.
<b>External Audit Process</b>				
Are reports on the work of external audit and other inspection agencies presented to the committee?	7	Yes		
Does the committee input into the external audit programme?	8	Yes		2005/06 Audit and Inspection Plan presented by the Relationship Manager to Audit Committee on 27 July 2005
<b>General</b>				
Does the committee ensure that officers are acting on and monitoring action to implement (audit) recommendations?	9	Yes		<p>Results of Internal Audit work to follow up agreed actions are reported to the committee.</p> <p>Observation: There is an opportunity to link this function more closely to risk management arrangements and provide the committee with a more active role in monitoring and reviewing action.</p>

Issue	Ref	Yes	No	Comment
<p>Does the committee take a role in overseeing:</p> <ul style="list-style-type: none"> <li>• Risk Management Strategies</li> <li>• Internal Control Statements</li> <li>• Anti-Fraud Arrangements</li> <li>• Whistle-Blowing Strategies?</li> </ul>	10	Yes		<ul style="list-style-type: none"> <li>• Revised Risk Management Policy and Strategy approved by the Audit Committee on 27<sup>th</sup> July 2005</li> <li>• Statement on Internal Control reported to Audit Committee on 19<sup>th</sup> October 2005.</li> <li>• Anti-Fraud and Corruption Policies are reviewed by the Committee (due in early 2006)</li> </ul> <p>Exception:</p> <ul style="list-style-type: none"> <li>• To monitor and review as necessary the operation of the Council's Whistleblowing Policy is included in the terms of reference of the Standards Committee.</li> </ul>
<b>Membership</b>				
<p>Has the membership of the committee been formally agreed and a quorum set?</p>	11	Yes		<p>Membership approved at the annual Council meeting on 12<sup>th</sup> May 2005. The quorum for all Committees is prescribed in the Constitution (Council Procedure Rules) and for the Audit Committee it is currently 3 out of 7.</p>
<p>Is the chair free of executive or scrutiny functions?</p>	12	Yes		<p>The Chairman of the Committee is also a member of the Licensing Act Committee but has no executive or scrutiny responsibilities.</p>
<p>Are members sufficiently independent of the other key committees of the council?</p> <p>Note: CIPFA guidance stipulates not more than one from each of the Executive and O&amp;S</p>	13		No	<p>The Committee membership comprises 7 members of the Council, including two members of Cabinet and one member of the Budget and Performance Panel. The inclusion of the Cabinet Member with special responsibility for financial affairs is currently required.</p>

Issue	Ref	Yes	No	Comment
Have all members' skills and experiences been assessed and training given for identified gaps?	14		No	No training programme for individual members has been produced (See also response at 22)
<b>Meetings</b>				
Does the committee meet regularly?	15	Yes		There are currently four scheduled meetings and other meetings are held as necessary.
Are separate, private meetings held with the external auditor and the internal auditor?	16		No	Under Financial Regulations, the Internal Audit Manager has right of access directly to members. Otherwise, private meetings are not set out in the Terms of Reference and have not been held to date.
Are meetings free and open without political influences being displayed?	17	Yes		
Are decisions reached promptly?	18	Yes		
Are agenda papers circulated in advance of meetings to allow adequate preparation by members?	19	Yes		Papers are dispatched at least five clear days before each meeting in accordance with the provisions of the access to information rules set out in Part 4 of the Constitution  Observation – potential to review arrangements for submitting/publishing IA reports and format of report to the Audit Committee.
Does the committee have the benefit of attendance of appropriate officers at its meetings?	20	Yes		The meetings are routinely attended by the following officers: <ul style="list-style-type: none"> <li>• Corporate Director (Central Services)</li> <li>• Head of Financial Services</li> <li>• Risk &amp; Insurance Manager</li> <li>• Internal Audit Manager</li> </ul> External Audit Relationship Manager and/or Audit Manager when relevant.

<b>Issue</b>	<b>Ref</b>	<b>Yes</b>	<b>No</b>	<b>Comment</b>
<b>Training</b>				
Is induction training provided to members?	21		No	Limited training has been provided so far by means of presentation to the Audit Committee in formal meeting
Is more advanced training available as required?	22		No	Whilst advanced training is available none has thus far been undertaken.
<b>Administration</b>				
Does the s151 officer or deputy attend all meetings?	23	Yes		See response at 20
Are the key officers available to support the committee?	24	Yes		See response at 20