



**AUDIT SCRUTINY OF**

**ASSEMBLY-SPONSORED**

**PUBLIC BODIES**

Memorandum by the Auditor General for Wales

July 2005

**Audit Scrutiny of Assembly-Sponsored Public Bodies**

**Summary**

1. The planned merger of a number of Assembly-sponsored public bodies into the Welsh Assembly Government will result in changes to the existing accountability framework. The ability of the Audit Committee to hold public officials to account will, however, remain unchanged.
2. The Welsh Assembly Government intends to put in place a range of measures to ensure that oversight of the expenditure formerly managed by the sponsored bodies will continue to be effective. These arrangements will, however, need to be reinforced by continuing

improvements in the Assembly's financial management systems to ensure that an increasingly complex business structure can be managed in the most efficient manner.

3. Arrangements will be put in place to ensure that an adequate level of audit scrutiny is retained over the merged functions. My core audit of the accounts prepared by the National Assembly of Wales will also be supplemented by additional risk-based reviews. These steps will help to address any 'expectation gap' that might otherwise arise in respect of the level of audit scrutiny that will be given to important areas of the Assembly's responsibilities that were previously managed by the sponsored bodies.

### Purpose and scope of this paper

4. At the Audit Committee meeting held on 2 December 2004, members considered the audit implications of the Welsh Assembly Government's white paper 'Making the Connections: delivering better services for Wales'. During discussion of that agenda item, my predecessor undertook to provide a memorandum to the Committee setting out the existing and proposed arrangements for audit scrutiny in light of the Assembly Government's restructuring plans for certain of its sponsored bodies.
5. On 1 April 2006, four Assembly-sponsored public bodies: the Welsh Development Agency; the National Council for Education and Training for Wales; the Wales Tourist Board; and the Qualifications, Curriculum and Assessment Authority for Wales, will all be merged with the Welsh Assembly Government. The functions of a fifth sponsored body, Health Professions Wales, will be subsumed in a new NHS body to be established for 1 April 2006 or brought into the Assembly. In addition, a sixth sponsored body, the Welsh Language Board, is due to be merged with the Assembly Government at a future

date to be determined.

6. The annual expenditure of these six bodies is around £900 million, representing almost two-thirds of the total spending by all 14 of the present Assembly-sponsored public bodies.
7. This paper:
  - summarises the existing arrangements for audit scrutiny of the public bodies which are currently sponsored by the Welsh Assembly Government;
  - describes how the impending reforms of certain of those sponsored bodies by the Welsh Assembly Government will impact on the existing audit and accountability arrangements; and
  - sets out the measures that are in hand in order to ensure that there is no risk of any reduction in the present ability of the Audit Committee of the National Assembly for Wales to hold public officials to account for the regularity, propriety and value for money of public funds.

## The existing arrangements for audit scrutiny of Assembly-Sponsored Public Bodies

### Financial audit of accounts

1. I act as the appointed external auditor of all of the Welsh Assembly Government's sponsored public bodies. Each body is required to prepare an annual set of financial statements which must provide a 'true and fair' picture of its financial affairs and of its assets and liabilities at the year end. I audit each set of accounts in accordance with professional auditing standards, which include a requirement to confirm that each body has spent public funds only for the purposes intended by the National Assembly for Wales (my 'regularity opinion'). For the vast majority of sponsored bodies, their governing legislation requires me to address my audit opinions to the members of the National Assembly for Wales, and for the accounts to be laid in the Table Office. This in turn brings them within the remit of the Audit Committee.
2. As it would, of course, not be practical for my staff to audit every single transaction

undertaken in a financial year by a public body, my examination follows best professional auditing practice and is instead undertaken on a sample basis linked to an assessment of the strength of the body's internal controls. This approach is also linked to the concept of audit 'materiality', whereby the auditor makes a judgement on what degree of error the reader of the financial statements may reasonably consider acceptable. The less the degree of error is considered to be acceptable, the more work the auditor has to carry out.

3. As well as certifying the annual accounts, I may choose to append to them a substantive report. I will always do this when my opinion is qualified, to explain to readers of those accounts the basis of my qualification. I can also report without qualifying my audit opinion in respect of any matter that I wish to bring to the attention of users of the accounts, including concerns relating to propriety or the proper conduct of public business.
4. Examples of these two types of report in recent years include my qualification of the 2001-02 accounts of the National Council for Education and Training for Wales (in respect of material level of irregular procurement contracts), and my report without qualification on that body's 2002-03 accounts. In those cases where I issue a substantive report on accounts to the Members of the National Assembly of Wales, the Assembly's Audit Committee has the power, if it so wishes, to take evidence from the Accounting Officer of the relevant body and other appropriate officials.

#### Additional Assurance reports

5. At the request of the Welsh Assembly Government, I also carry out an annual 'additional assurance review' at each sponsored body in parallel with my audit of the financial statements. This work, which is currently unique in the UK central government sector, is designed to provide assurance on the body's financial affairs over and above the level required by the external audit of the annual financial statements.
6. The additional assurance review looks at whether the body has complied during the year with the requirements of its Management Statement and Financial Memorandum issued by the Welsh Assembly Government. These can cover, for example, whether the body has operated proper tendering procedures, and maintained its expenditure within the limits set by the Welsh Assembly Government. The review also examines the body's internal control arrangements, including procedures for corporate governance and risk management, and a range of other issues including whether adequate arrangements for provision of an internal

audit service have been put in place.

## Value for Money audit

7. I also take account of the views of the Assembly Audit Committee each autumn in formulating my annual value for money work programme, which includes studies relating to expenditure areas managed by one or more Assembly-sponsored public bodies. My value for money work examines the economy, efficiency and effectiveness with which public bodies use their resources. My audit findings are published, and these form the basis of the Assembly Audit Committee's evidence sessions. A recent example is my published report on the management of sickness absence in further education institutions in Wales, on which the Audit Committee took evidence from the Accounting Officer of the National Council for Education and Training in Wales, along with the Principals of two further education institutions.

## The role of audit and corporate governance committees

8. Each sponsored body is additionally subject to scrutiny by its own audit or corporate governance committee. This operates in accordance with standards set by HM Treasury and contains one or more members who are independent of the body itself. Each audit committee is able to question senior management on the results of internal and external audit work and also to review the sufficiency and adequacy of the work undertaken. It plays a key role within the overall corporate governance arrangements of the body and can help ensure that sufficient prominence is given to the audit role by senior management. My staff attend the audit committee meetings of every sponsored body, and also those of the Corporate Governance Committee which fulfils an equivalent purpose within the Welsh Assembly Government. There is a separate corporate governance committee for the Assembly Parliamentary Services.

## The scrutiny role of governing bodies

9. Whilst not part of the formal internal or external audit arrangements, another relevant aspect is the role played by the appointed governing body (a 'Board', 'Council' or 'Authority', as prescribed in the relevant legislation) of each Assembly-sponsored public body. Subject to the parameters set out in the annual Ministerial

‘remit letter’, the senior management of each sponsored body are generally responsible for policy development within the organisation. However, the governing bodies scrutinise and approve policy decisions, and they thus play an important oversight role in the overall direction and shape of the organisation, acting as an integral part of its corporate governance arrangements. There are also often in place sub-committees of the governing body, each focussing on specific aspects of the body’s performance, for example in scrutinising the body’s budgetary and financial management arrangements.

## Impact of the impending reforms on audit and accountability arrangements

10. There will be three main direct impacts on audit and accountability arrangements arising from the impending reforms:
  - i. the loss of the oversight role played by the appointed governing bodies and related scrutiny functions such as those provided by each body’s audit committee;
  - ii. the income and expenditure of all of the various bodies will be subsumed within the single set of annual financial statements prepared by the National Assembly for Wales (NB: under existing legislation, there is no requirement for the Welsh Assembly Government to produce accounts separate from those of the Assembly as a whole). The separate sets of accounts prepared by the sponsored bodies for the 2005-06 financial year will therefore be the last; and
  - iii. audit scrutiny of the activities previously undertaken by the various sponsored bodies will now fall within my examination of the accounts of the National Assembly for Wales as a whole. The relative materiality of those bodies’ income and expenditure to my audit opinions will thus change, resulting in both a requirement and an opportunity, to re-evaluate the audit approach in this area.

## Measures in hand

11. The effective accountability and robust independent audit scrutiny of the functions being transferred into the Welsh Assembly Government will be safeguarded in three main ways:
  - i. arrangements being put in place by the Welsh Assembly Government and the Wales Audit Office in the run-up to the merger;

- ii. accountability arrangements proposed by the Welsh Assembly Government post-merger; and
- iii. future audit arrangements that I propose to introduce in relation to my examination of the expenditure and activities of the National Assembly for Wales.

#### Arrangements being introduced prior to 1 April 2006

12. There exists a range of important transitional risks to be managed by both the sponsored bodies and the Welsh Assembly Government in the period leading up to and beyond the merger date of 1 April 2006. This includes the potential loss of key staff in the sponsored bodies, senior management overload, and a risk that this may weaken the focus within each body on maintaining sound financial management, and ensuring propriety and regularity of expenditure. During this period the sponsored bodies will also still have to continue to deliver their normal programmed objectives and account properly for their finances.
13. To help manage these risks, the Welsh Assembly Government has established a structure of project teams and boards to oversee the key elements involved in the merger process. Staff of the sponsored bodies are participating alongside Assembly Government officials in these project management arrangements and the bodies have also incorporated the merger process within their risk management procedures. My staff are also playing an active part in this process through attendance at project team meetings and in advising on risk management issues.
14. I welcome also the fact that, as part of their management of the merger project, Assembly Government officials are making use of good-practice criteria issued by the Audit Committee in November 2000 following their examination of the merger of the Land Authority for Wales and the Development Board for Rural Wales into the Welsh Development Agency.
15. I remain alert, however, to the potential risks in terms of costs and business stability during the period in which the sponsored bodies will be merged with the Welsh Assembly Government. In managing these risks it will be important that the Assembly Government is able to ascertain and control the costs involved in the merger process itself.
16. In accordance with my predecessor's practice, I intend to report on the closure of each of the sponsored bodies to confirm that closing assets and liabilities are complete and fairly stated at the date of their transfer to the Welsh Assembly Government. As the bodies themselves will have ceased to exist by the time these

accounts are prepared, the legal duty for the preparation of the 2005-06 accounts will pass to the Welsh Assembly Government. Appropriate arrangements will need to be put in place to manage this process adequately, for example through maintaining continuity of key staff.

### Accountability arrangements proposed by the Welsh Assembly Government

17. The absorption of additional functions by the Welsh Assembly Government will place significant extra pressures on its management and operational structure. It will be important to integrate the new functions within the Assembly Government's operating and control framework and to ensure an appropriate continuing level of internal and external accountability.
  18. Accordingly, and to support him in managing the larger Welsh Assembly Government structure that will come into place in 2006, the Assembly's Permanent Secretary (as the Principal Accounting Officer) has delegated responsibility to five sub-Accounting Officers with effect from 1 April this year. These new sub-accounting officers are the Heads of Departments responsible for budgets within the following administrative areas of the Welsh Assembly Government:
    - Social Justice and Regeneration;
    - Training and Education;
    - Environment, Planning and Countryside;
    - Economic Development and Transport; and
    - Local Government, Public Services and Culture.
1. In addition to its existing ability to question the Principal Accounting Officer on the activities of the Welsh Assembly Government (and the Director of Health and Social Care as Accounting Officer for NHS Wales), the Assembly Audit Committee will be able also to take evidence from these new sub-accounting officers on any matters of concern. The existing Corporate Governance Committee of the Welsh Assembly Government will be augmented by governance committees operating at the sub-accounting officer level which will scrutinise the financial and other affairs of the delegated areas. It is possible, as is currently the case with the Corporate Governance Committee, that these new governance committees will also include independent members.
  2. I welcome these proposals and believe that they will be of considerable assistance in the continuing process of strengthening corporate governance and financial



management arrangements within and across the Assembly Government's various areas of business. The Welsh Assembly Government will need to consider what additional financial management arrangements it may be necessary to put in place to support each sub-accounting officer. This could extend also to a review of internal and external financial reporting arrangements, to ensure not least the continuing visibility of the financial performance of the merged areas.

### Future external audit arrangements

3. At the core of future external audit arrangements will remain my statutory financial audit of the annual resource account of the National Assembly for Wales. In planning their work on this account each year, my auditors will ensure that full attention is given to the significance and potential risks relating to the areas which were formerly the responsibility of the sponsored bodies.
4. I also envisage some specific benefits to the way in which I shall be able to conduct my audit work arising from the structural reforms. For example, in future my audit will be able to focus on a single, overall control framework within the Welsh Assembly Government in respect of the merging bodies, whereas to date my auditors have had to consider each of the differing internal control systems that are in place within each sponsored body. This unified control framework will include a common accounting and financial management system, which will also cover European-funded projects; many of which were previously managed by the individual sponsored bodies.
5. The above changes, whilst aiding the overall efficiency of my audit approach, will also provide more opportunities for me to make 'added value' recommendations to management in respect of the Assembly's internal control arrangements. There may, in addition, be scope for me to place increased reliance on the work of internal audit, for example in the examination of central systems such as payroll, thereby generating further cost efficiencies.
6. In the light of the announced structural changes, I also intend to enhance my core audit of the Assembly's accounts by considering opportunities to carry out focused 'investigative' reviews of particular areas of expenditure that are assessed to be of higher risk or greater public interest. This will also help to ensure that there is no reduction in my scrutiny of systems of internal control arising from the discontinuation of the additional assurance reviews on the former sponsored bodies. I would intend such investigative reviews to complement both my statutory financial audit work and my continuing programme of value for money examinations. This

will ensure that the overall audit approach in place is both fully integrated and also focused on the widest range of potential risks to regularity, propriety and value for money across the entire spectrum of Welsh Assembly Government activities and expenditure.

7. My value for money programme will continue to be based on risk assessment that covers the full range of the Assembly's spending portfolios. The activities currently undertaken by each of the sponsored bodies will not, therefore, 'disappear from the radar'. Indeed, the increased risk to value for money that inevitably accompanies change will mean that my programme is more likely to include examinations of the activities of the former sponsored bodies.
8. Both my financial audit work and my value for money examinations are also informed by my correspondence work. Each year I receive 60 or more enquiries and expressions of concern regarding financial management, value for money and the proper conduct of public business. Such correspondence comes from a variety of sources, including Assembly members, the public and businesses, and all concerns raised are examined fully and objectively. Recently, for example, concerns raised in correspondence led me to examine the adequacy of the arrangements of both the Welsh Development Agency and the National Council for safeguarding the public funds each had provided to the liquidated enterprise company, Antur Dwyryd Llyn Ltd.
9. The Public Audit (Wales) Act 2004 has given me a new power to prepare and publish reports in the public interest at any time. I envisage that the risk-based 'investigative' reviews described above could occasionally generate such published reports, as well as reports to management. There may also be the case for me to publish a substantive report on the Assembly's annual accounts, covering issues of current public interest, but I intend to give further consideration to this once the new structural arrangements are in place. As is currently the case, all published reports would be laid in the Table Office and be available for the Audit Committee if it wishes to take evidence from the appropriate Accounting Officers.
10. Taken together, the above measures will help to ensure that my work continues to build upon the minimum level of audit necessary simply for me to place an opinion on the Assembly's accounts each year. I consider that this will be increasingly important to both the Audit Committee and the people of Wales to ensure proper scrutiny of what is an ever-larger and more complex range of public expenditure. I look forward to working with the Audit Committee and with Assembly Government officials in enhancing the framework of public audit in a manner that aims to meet the needs of all stakeholders.

Jeremy Colman

5 July 2005

Auditor General for Wales