

AGENDA ITEM: 8

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Meeting	Audit Committee
Date	15 February 2006
Subject	Terms of Reference & Review of Effectiveness of the Audit Committee
Report of	Chief Finance Officer
Summary	To review the terms of reference for the Audit Committee and make recommendations on this to the Constitution Review Committee. To conduct the annual review of effectiveness of the Audit Committee.

Officer Contributors	Chief Finance Officer, Chief Executive, Director of Resources, Head of Corporate Support, Borough Solicitor
Status (public or exempt)	Public
Wards affected	None
Enclosures	Appendix A – Existing terms of reference Appendix B – Model terms of reference Appendix C – Review of effectiveness
For decision by	Audit Committee
Function of	Council
Reason for urgency / exemption from call-in (if appropriate)	None

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1. RECOMMENDATIONS

That the Audit Committee

1.1 recommend to the Constitution Review Committee the following:-

- (i) that the model Statement of Purpose and Terms of Reference for the Audit Committee as set out in recent CIPFA guidance and in Appendix B be adopted within the Council Constitution;**
- (ii) any recommendations in response to paragraphs 8.10 (ix), (xi) and (xii) of this report;**
- (iii) that it be noted that the annual review of effectiveness of the Audit Committee (and its predecessor) is already in accordance with best practice, but the requirement to conduct this review annual now be included in the Terms of Reference, and that this be scheduled within the Committee's work programme in time to make any recommendations each year to the Constitution Review Committee.**

1.2 agree to put in place a programme of training for its members, to be established over a 12 month period commencing as soon as possible after the May 2006 local elections.

1.3 agree a work plan in line with the revised terms of reference for the next municipal year at its first meeting after new terms of reference are approved.

1.4 instruct the Chief Finance Officer to advise the Special Committee (Constitution Review) of this Committee's decision under 1.1 above, and take the necessary action to implement 1.2 and 1.3 above.

2. RELEVANT PREVIOUS DECISIONS

2.1 Council – 12.4.2005 – report of the Constitution Review Committee.

3. CORPORATE PRIORITIES AND POLICY CONSIDERATIONS

3.1 The Audit Committee is part of the corporate governance framework and it is important that its operation is reviewed regularly.

4. RISK MANAGEMENT ISSUES

4.1 None in the context of this report, but the report does mention future arrangements for organising risk management.

5. FINANCIAL, STAFFING, ICT AND PROPERTY IMPLICATIONS

5.1 None.

6. LEGAL ISSUES

6.1 None.

7. CONSTITUTIONAL POWERS

7.1 This report is part of a constitution review process that is governed by the Council Constitution.

8 BACKGROUND INFORMATION

8.1 The Council set up an Audit Committee as part of the 2004/05 constitution review that was reported to Council in April 2005. The current terms of reference for the Audit Committee are set out in Appendix A.

8.2 The External Auditor has commented favourably over the past year on the establishment of the Audit Committee and the level of debate at the meetings on reports presented to it. It is important, however, to regularly review the arrangements of the committee, not least towards the end of its first year of working. A review at this time means it will also be possible to consider recent guidance on audit committees issued by CIPFA (Chartered Institute of Public Finance and Accountancy), which will also be used by the External Audit in the annual Corporate Performance Assessment Use of Resources judgement.

8.3 It is important to appreciate that the Audit Committee is not an overview and scrutiny committee, and can make recommendations to both Council and Cabinet.

8.4 This report also deals with the annual review of the effectiveness of the Audit Committee.

Review of Terms of Reference

8.5 The recent guidance from CIPFA incorporates a 'Statement of Purpose' and set of model terms of reference for Audit Committees – these are both attached at Appendix B.

8.6 Since its inception the Audit Committee has had reports on the following matters:-

Internal Audit:

- Interim/ Annual Internal Audit reports 2004-5
- Swift computer system and adult social services debt
- Audit updates on MCS (Modernising Core Systems) project

CAFT

- Annual report 2004-5

Finance

- Annual Statement of Accounts and SAS 610
- Debt Collection

Chief Executive / Other

- Risk management
- Barnet Homes financial governance arrangements
- Audit Committee work programme 2004-5

External Audit

- External Auditor's Report under Statement of Auditing Standards (SAS) 610 for the year 2004/05
- MCS

8.7 Comparing the model terms of reference to the business conducted over the past year there is a strong correlation. Main areas of 'omission' from the model terms of reference would be:-

- the review of the annual statement of accounts – which, the 2005/06 constitution review will correct;
- liaising with the Audit Commission over the appointment of the external auditor – because the Audit Commission is not currently conducting a review of the appointment;
- commissioning work from internal and external audit;
- maintaining an overview of the constitutional arrangements for contracts procedures, financial regulations and codes of conduct and behaviour;
- considering the Council's arrangements for corporate governance;
- considering the Council's compliance with its own published standards and controls.

8.8 On the other hand, a review of the CIPFA guidance would indicate that the depth in which certain reports from the Chief Internal Auditor over the past year have been reviewed by the Audit Committee goes beyond the strategic role that the guidance envisages.

8.9 It is proposed that the model terms of reference for the Audit Committee be adopted in full, except as noted in paragraph 8.10 (vii), but before commenting further on this it is worth noting some changes in responsibility that have recently been agreed as part of the Resources Directorate restructure. Firstly, the Chief Internal Auditor will in future report to the Chief Executive. Secondly, the Director of Resources will be responsible corporately for risk management.

8.10 If the model terms of reference are to be adopted, the following points should be noted, and the Committee is asked to consider whether they wish to recommend any changes to the Council's constitution or express any views in respect of these points.

- (i) In respect to the Internal Audit function, the Audit Committee would:-
- approve, but not direct, the overall strategy;
 - approve the annual work plan;

- monitor progress against the plan and assess whether adequate skills and resources are available.
- (ii) In reviewing the work of Internal Audit, the Audit Committee would:-
- consider summaries of work done, key findings, issues of concern and action in hand as a result of audit work;
 - receive feedback on the work carried out by Internal Audit.
- (iii) The Chief Internal Auditor should be able to meet privately with the Audit Committee.
- (iv) The External Auditor should be able to meet privately with the Audit Committee.
- (v) The Audit Committee should have access to reports from inspection agencies about the Council's financial management and governance, to provide a source of assurance and to compare with any relevant internal and external audit reports. It would also be expected to monitor executive and management action arising from such reports.
- (vi) The Audit Committee should be aware of the work of overview and scrutiny committees, so that it can take account of issues relevant to its areas of interest.
- (vii) The Audit Committee should take a view on a number of strategies that the Council has in place to regulate its activities and control the actions of employees, elected members and contractors – ensuring these have been properly formatted and remain effective. This could include the following:-
- risk management;
 - assurance framework for producing the Statement of Internal Control;
 - local codes of corporate governance, standards and behaviour;
 - arrangements for delivering value for money;
 - anti-fraud and corruption arrangements.

The third bullet point above cuts across the role of the Standards Committee. If this were included in the terms of reference of the Audit Committee it would undermine the principle that matters of standards and behaviour, including codes and policies, are regulated by that Committee with its independent majority and Chairman. It is proposed, therefore, that this line be removed from the model terms of reference.

- (viii) In reviewing the annual Statement of Accounts and SAS610 report from the External Auditor, the Audit Committee should focus on:-
- the suitability of accounting policies and treatments, including any changes in these from the previous year;
 - major judgemental areas (e.g. provisions);
 - significant adjustments and material weaknesses in internal control reported by the External Auditor.

- (ix) The chairman of the Audit Committee should not be a member of the Executive and preferably a member of an opposition party. Although the guidance does not say this, the committee might want to consider recommending amendments to the constitution to also prevent any member of the executive being a member of the Audit Committee, and to prevent a Chairman of the committee serving for more than one municipal term (4 years)..
- (x) The Audit Committee should meet around four times a year, with one meeting agreeing the annual work plan and the remaining meetings fitting in with the cycle of assurance statements and financial reporting.
- (xi) The Audit Committee should comprise somewhere between three and five members, subject of course to achieving the necessary political balance.
- (xii) Co-option (without voting rights) to the Audit Committee could be considered where it is considered an external view might assist with a specific discussion.
- (xiii) Whilst financial awareness is essential, particularly for the chairman, an accounting background or qualification is less important than a broad understanding of the financial, risk and control and corporate governance issues facing local authorities in general and the Council specifically. This will translate into a training programme for members of the Audit Committee, which will require the members to give a commitment to participating.

8.11 Given that the CIPFA guidance recommends the Audit Committee meeting around four times a year and that the first meeting would be substantially devoted to agreeing the annual work plan, it is clear that the Audit Committee is expected to be fairly strategic in its working and level of debate, and should not be sucked into discussing points of detail in great depth at its meetings.

8.12 To facilitate this, the content and style of reports to the Audit Committee may need to change, and consideration should be given to scheduling a meeting between the Chairman, Vice-Chairman and key officers mid-way between Audit Committee meetings. Such a meeting would certainly be helpful prior to the Audit Committee meeting that agrees the annual work plan, in order to have a clear understanding of the nature and content of the reports to the committee over the year ahead.

Review of Effectiveness

8.13 An initial appraisal of the Audit Committee against the criteria contained in the self-assessment checklist 'Measuring the Effectiveness of the Audit Committee' demonstrates that the Committee currently meets the majority of the requirements. This is consistent with the External Auditor's assessment of the Committee as being very effective.

8.14 The completed self assessment is attached at Appendix C. Areas where there are opportunities to further enhance effectiveness, and compliance with the checklist, are:-

- formal assessment of Members' skills and experiences;

- identification of training to address any gaps in skills and experience;
- induction training for the committee Members;
- reviewing summaries of Internal Audit quality questionnaires completed by service managers.

9 LIST OF BACKGROUND PAPERS

9.1 Audit Committees – practical guidance for local authorities (CIPFA 2005).

Legal: JEL

CFO: CM

Audit Committee – Existing Terms of Reference

1. Ensuring that the Council's financial reports, annual financial statements, Statement of Internal Control and the action taken by the Council to implement fully a risk management system are balanced, fair, conform to accountancy standards and meet prevailing best practice.
2. Reassuring the Council that the scope and depth of external audit work and the annual External Audit Plan are sufficient and conducted competently, including communication with the external auditor on audit findings and material weaknesses in accounting and internal control systems, including endorsing the annual External Auditor's Letter. Meeting independently with the external auditor periodically, ensuring the independence and objectivity of the external auditor and in matters relating to the provision of non-audit services.
3. Satisfying the Council that the internal auditor carries out sufficient systematic reviews of the internal control arrangements, both operational (relating to effectiveness, efficiency and economy) and financial.
4. Reviewing the major findings of any relevant internal council investigations by the Corporate Anti Fraud Team into control weaknesses, fraud, whistle blowing or misconduct and the management's response.
5. Reporting as appropriate to the Council and Cabinet.

Audit Committee – Statement of Purpose

The local authority should formally approve a Statement of Purpose, along the following lines:

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.

Audit Committee – Model Terms of Reference

Audit Activity

1. 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.
2. To consider summaries of specific internal audit reports as requested.
3. To consider reports dealing with the management and performance of the providers of internal audit services.
4. To consider a report from internal audit on agreed recommendations not implemented within a reasonable timescale.
5. To consider the external auditor's annual letter, relevant reports, and the report to those charged with governance.
6. To consider specific reports as agreed with the external auditor.
7. To comment on the scope and depth of external audit work and to ensure it gives value for money.
8. To liaise with the Audit Commission over the appointment of the council's external auditors.
9. To commission work from the internal and external audit.

Regulatory Framework

10. To maintain an overview of the council's constitution in respect of contract procedure rules and financial regulations.

11. To review any issue referred to it by the chief executive or a director, or any council body.
12. To monitor the effective development and operation of risk management and corporate governance in the council.
13. To monitor council policies on 'Raising Concerns at Work' and the anti-fraud and anti-corruption strategy and the council's complaints process.
14. To oversee the production of the authority's Statement on Internal Control and to recommend its adoption.
15. To consider the council's compliance with its own and other published standards and controls.

Accounts

16. 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.
17. To consider the external auditor's report to those charged with governance on issues arising from the audit of the accounts.

The following line has been excluded from the proposed terms of reference – see paragraph 8.10(vii) of the main report:-

- To consider the council's arrangements for corporate governance and agreeing necessary actions to ensure compliance with best practice.

Audit Committees: Practical Guidance for Local Authorities

Self-assessment Checklist - Measuring the Effectiveness of the Audit Committee

ISSUE	YES	NO	N/A	Comment
Terms of Reference				
Have the committee's terms of reference been approved by full council?	✓			
Do the terms of reference follow the CIPFA model?			✓	Will do when this exercise is complete
Internal Audit Process				
Does the committee approve the strategic audit approach and the annual programme?	✓			Annual plan approved in April each year
Is the work of Internal Audit reviewed regularly?	✓			Interim and annual reports as well as regular reporting against Internal Audit PIs
Are summaries of quality questionnaires from managers reviewed?		✓		The Internal Audit PI which monitored this was discontinued but will be re-instated
Is the annual report, from the head of audit, presented to the committee?	✓			
External Audit Process				
Are reports on the work of external audit and other inspection agencies presented to the committee?	✓			Query: should ToR require OFSTED/ CSCI reports also go to Audit Committee for review of any risk/control issues
Does the committee input into the external audit programme?		✓		Ext Audit programme should be presented to the Audit Committee, when it has the opportunity to comment
Does the committee ensure that officers are acting on and monitoring action taken to implement recommendations?	✓			All recommendations are followed up and reported to the Audit Committee

ISSUE	YES	NO	N/A	Comment
Does the committee take a role in overseeing:				
<i>risk management strategies</i>	✓			
<i>internal control statements</i>	✓			
<i>anti-fraud arrangements</i>	✓			
<i>whistle-blowing strategies?</i>	✓			
Membership				
Has the membership of the committee been formally agreed and a quorum set?	✓			
Is the chair free of executive or scrutiny functions?	✓			Chair is presently drawn from an opposition party.
Are members sufficiently independent of the other key committees of the council?	✓			No cabinet members presently sit on the Audit Committee
Have all members' skills and experiences been assessed and training given for identified gaps?		✓		
Can the committee access other committees as necessary?	✓			
Meetings				
Does the committee meet regularly?	✓			
Are separate, private meetings held with the external auditor and the internal auditor?	✓			The right to do this is included in the ToR.
Are meetings free and open without political influences being displayed?	✓			
Are decisions reached promptly?	✓			
Are agenda papers circulated in advance of meetings to allow adequate preparation by members?	✓			
Does the committee have the benefit of attendance of appropriate officers at it's meetings?	✓			

ISSUE	YES	NO	N/A	Comment
Training				
Is induction training provided to members?	✓			
Is more advanced training available as required?		a		
Administration				
Does the authority's 151 officer or deputy attend all meetings?	✓			
Are the key officers available to support the committee?	✓			