

Date: 4 October 2012

Item 12: Draft Local Audit Bill

This paper will be considered in public

1 Summary

1.1 The purpose of this paper is to inform the Audit and Assurance Committee about the Department for Communities and Local Government's (DCLG's) publication of the draft Local Audit Bill and of TfL's response to the consultation on the draft Bill.

2 Recommendation

2.1 The Committee is asked to note the paper.

3 Background

3.1 On 6 July 2012, the DCLG published its draft Local Audit Bill for consultation and pre-legislative scrutiny.

3.2 In summary, the principal effects of the Bill will be to:

- (a) abolish the Audit Commission;
- (b) require local public bodies to appoint an external and independent auditor on the advice of an independent 'auditor panel';
- (c) create a new regulatory framework for local public audit with the Financial Report Council and professional accountancy bodies regulating these services; and
- (d) give the National Audit Office (NAO) new responsibilities in relation to the Code of Audit Practice and studies of thematic value for money issues relating to local government.

3.3 The attached Appendix 1 provides further detail on the draft Bill and its anticipated implications for TfL.

3.4 The only element of the draft Bill that is likely to have any significant impact on TfL is the requirement for an independent auditor panel. Although TfL could nominate the Audit and Assurance Committee to be the auditor panel, the Committee would have to have a majority of non TfL Board members and an independent chair to meet the independence requirements set out in the Bill. Therefore, the most likely approach would be sharing a panel with other appropriate bodies (eg GLA and functional bodies) or to jointly procure an auditor.

3.5 TfL previously responded to a DCLG consultation, in June 2011, in relation to this issue and argued that the requirement for additional independent members of the Audit Committee should not apply to TfL in view of the TfL Board being non-

Executive and appointed by the Mayor. We have now responded to the consultation on the draft Bill, again making the point that TfL does not believe that the requirement for additional 'independent' members of its Audit and Assurance Committee would add any value to its governance arrangements, but would certainly add cost due to the need to pay these members.

List of appendices to this report:

Appendix 1 – Draft Local Audit Bill and Implications for TfL.

List of Background Papers:

None

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Draft Local Audit Bill and Implications for TfL

Introduction

1. The Draft Local Audit Bill (“the draft Bill”), which currently is the subject of consultation¹, disbands the Audit Commission and creates a new regulatory framework to allow local public bodies to appoint their own auditors in accordance with its provisions. Local public bodies are specified in Schedule 2 to the draft Bill and include the GLA (paragraph 7), TfL and the other functional bodies (paragraph 8) and MOPAC (paragraph 20).

Abolition of existing audit regime

2. Part 1 of the draft Bill abolishes the Audit Commission and repeals the Audit Commission Act 1998, although many of the substantive obligations for audits themselves are retained. The draft Bill introduces a new framework for the appointment of auditors by local public bodies, and for the eligibility and regulation of auditors.

Basic requirements

3. Part 2 of the draft Bill sets out the general accounting and audit requirements for local public bodies. These requirements have been recast (in line with the Companies Act 2006 and Charities Act 2011) to provide a clear distinction between the accounting records that must be maintained during the year and the annual statement of accounts that must be published after the year end.

Appointment of auditors

4. A local public body must appoint and take into consideration the advice of an ‘auditor panel’² before making the appointment of an auditor.
5. The panel must consist³ of a majority of independent members and have an independent chair. To be independent, a panel member must not have been a member or officer of the local public body within the last five years and must not at the time be a relative or close friend of an officer or member of the local public body. An existing Audit Committee may be nominated as the panel as long as it meets the ‘independence’ requirements. In addition, separate local public bodies may share a panel and may also make joint procurement arrangements.

¹ Until 31 August 2012; see <http://www.communities.gov.uk/publications/localgovernment/draftlocalauditbill>.

² Clause 8(3) of the draft Bill provides that the appointment of the independent audit panel for the GLA must be made jointly by the Mayor and the London Assembly. Clauses 9(6) to (8) impose a requirement that the Commissioner of the Metropolitan Police must have the same auditor as MOPAC. The draft Bill does not impose any specific or additional requirements on TfL or any other functional bodies.

³ It is proposed that the Secretary of State may make regulations and guidance regarding the constitution of panels.

6. The panel's role⁴ is chiefly to advise on:
 - (a) the appointment of an auditor;
 - (b) the maintenance of an independent relationship with the auditor; and
 - (c) the impacts of public interest report,although a local public body can delegate further functions as it sees fit.
7. Appointments to the independent audit panel and the advice of the panel (together with, if the advice has not been followed, the reasons why) will be required to be published.
8. **Impact on TfL: Options:**
 - (a) Although TfL could nominate the Audit and Assurance Committee to be the auditor panel, the Committee would have to have a majority of non TfL Board members and an independent chair to meet the independence requirements outlined above.
 - (b) TfL could share an auditor panel with other local public bodies (most obviously the GLA and/or other functional bodies, subject to any specific requirements such as those placed on GLA and policing authorities).
 - (c) TfL could jointly procure an auditor with other local public bodies (also as above).

Eligibility and regulation of auditors

9. As with private audit under the Companies Act 2006, it is proposed that the Financial Reporting Council (FRC) will be responsible for the oversight⁵ of the regulation of local public audit. The FRC will be able to authorise professional accounting bodies to be recognised 'supervisory bodies' for the purposes of local public audit and delegate functions to them. Those bodies will then be responsible for a number of matters including determining eligibility of firms and individuals, maintaining a register, and monitoring and reporting on the quality of audits. A core element of eligibility will be an independence requirement; auditors will not be able to act for local public bodies if they are a member or officer of the body or a connected entity⁶, or a partner of a member or officer of the body or a connected entity.
10. There is also an additional level of oversight and monitoring for audits of significant local public bodies ("major local audits", paragraph 15(10) of Schedule 3). The FRC will publish the scope of its inspections of these audits after consultation with Government departments and professional accounting bodies; the Government is also exploring which bodies would be subject to these audits, which will be specified in regulations along with further details about the process.

⁴ It is proposed that the Secretary of State may make regulations and guidance regarding the functions of panels.

⁵ The FRC may authorise existing and additional professional accounting bodies to be recognised supervisory bodies for the purposes of local public audit, and delegate functions to supervisory bodies.

⁶ I.e. those entities whose financial transactions, under proper accounting practices, consolidate into the group accounts of the relevant authority.

11. **Impact on TfL:** It is unclear whether TfL will be listed a significant local public body, however, it is not currently anticipated that a 'major local audit' will be more onerous than the current audit arrangements.

Conduct of audit

12. The draft Bill provides that the National Audit Office (NAO) will set a statutory code of audit practice that sets out the audit outputs and the scope of audit. It is expected that these matters will broadly be the same as the current regime and in summary the auditor must, by examination of the accounts and otherwise, be satisfied that⁷:
 - (a) the accounts comply with relevant legislative requirements;
 - (b) proper practices have been observed in the preparation of the statement of accounts; and
 - (c) the local public body has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.
13. The draft Bill retains the following key features of the current regime:
 - (a) access to documents and information from the local public body and connected entities;
 - (b) making reports and recommendations in the public interest (which must be published and discussed within specified time frames);
 - (c) public interest reports for GLA or entities connected to TfL must be considered by the London Assembly with the Mayor in attendance;
 - (d) the right of local electors and interested persons to inspect accounting records and audited documents; and
 - (e) the Secretary of State will make Accounts and Audit Regulations as under the current regime.
14. **Impact on TfL:** The statutory code (which it is stated will take a risk based and proportionate approach) may result in an increase in the level of audit work. In addition, there are specific requirements in relation to public interest reports for entities connected to TfL.

Other matters

15. The draft Bill transfers the Audit Commission's current powers to require local public bodies to submit data for the purposes of data matching (ie part of a National Fraud Initiative to provide potential fraud matches for further investigation) and carry out inspections to the Secretary of State.
16. Similarly the Audit Commission's powers in relation to carrying out studies, and accessing information to carry out studies, are transferred to the NAO.

⁷ Clause 60(1).