

# CARLISLE CITY COUNCIL

Report to:- **COUNCIL**

Date of Meeting:- **2 MAY 2006**

Agenda Item No:-

Public	Operational	Delegated Yes
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Accompanying Comments and Statements	Required	Included
Environmental Impact Statement:	No	No
Corporate Management Team Comments:	No	No
Financial Comments:	Yes	Yes
Legal Comments:	Yes	Yes
Personnel Comments:	No	No
Impact on Customers:	-	-

Title:- **PROPOSAL TO ESTABLISH AN AUDIT COMMITTEE**  
Report of:- **DIRECTOR OF LEGAL AND DEMOCRATIC SERVICES**  
Report reference:- **LDS.11/06 (Amended)**

## Summary:-

The attached Report was submitted to and considered by the Accounts Committee at its meeting on 19 April 2006. The Accounts Committee considered the draft Rules of Governance and suggested a number of amendments. The Audit Committee's Rules of Governance as amended by the Accounts Committee are attached to this Report.

## Recommendation:-

- (1) The Council are recommended to approve the Audit Committee's Rules of Governance (as now circulated) with a view to the Audit Committee being established as part of the Council's Governance arrangements as from the Annual Council Meeting on 22 May 2006.
- (2) The Council needs to determine whether the Audit Committee should be comprised of 5 or 6 Members.

**Contact Officer : Mr Ian Dixon Ext. 7033**

**Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers: None**

# CARLISLE CITY COUNCIL

Report to:- **ACCOUNTS COMMITTEE**

Date of Meeting:- **19 APRIL 2006**

Agenda Item No:-

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Public	Operational	Delegated: No
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Accompanying Comments and Statements	Required	Included
Environmental Impact Statement:	No	No
Corporate Management Team Comments:	No	No
Financial Comments:	Yes	Yes
Legal Comments:	Yes	Yes
Personnel Comments:	No	No
Impact on Customers:		

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Title:- **PROPOSALS TO ESTABLISH AN AUDIT COMMITTEE**

Report of:- **DIRECTOR OF LEGAL AND DEMOCRATIC SERVICES**

Report reference:- **LDS.11/06**

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## Summary:-

Following the decision of the Council on the 7 March last, the report sets out for Members some draft Rules of Governance for them to consider in respect of the establishment of a formal Audit Committee by the Council.

## Recommendation:-

The Committee are asked to:-

- (a) consider the proposed Rules of Governance and if they are happy with them,
- (b) recommend them, together with any appropriate amendments which the Committee may wish to make, to the full Council for approval on the 2 May next with a view to the Audit Committee being established as part of the Council's governance arrangements as from the Annual Council meeting on the 22 May next.

**Contact Officer: J M Egan Ext. 7004**

"Note: in compliance with Section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers : CIPFA publication entitled "Audit Committees – Practical Guidance for Local Authorities".

## 1. **Why have an Audit Committee?**

- 1.1 Although there is no specific statutory duty as yet to set up a free-standing Audit Committee, the Council does have a responsibility under the Accounts and Audit Regulations 2003 to “ensure that its financial management is adequate and effective and that it has a sound system of internal control which facilitates the effective exercise of its functions”. Further, Section 151 of the Local Government Act 1972 requires the Council to “make arrangements for proper administration of its financial affairs”. The authority, therefore, has to be able to demonstrate that it has in place robust governance arrangements to fulfil these responsibilities.
- 1.2 At the end of last year CIPFA produced guidance for local authorities which was consistent with the Audit Commission’s thinking and which encouraged authorities to consider setting up free-standing Audit Committees to demonstrate compliance with the above responsibilities. Although the guidance recognises that many authorities already deal with audit issues through other means (for example through a nominated Overview and Scrutiny Committee, in some cases) it states that there is always the danger either that the audit functions of a generalist Committee may become diluted by the pressure of other business or that the proper functions of these other Committees might become less clear. The CIPFA guidance, therefore, highlighted a number of benefits which might be gained from operating a separate free-standing Audit Committee because such a Committee could:-
- Raise greater awareness of the need for internal control and the implementation of audit recommendations within the authority
  - Increase public confidence in the objectivity and fairness of financial and other reporting
  - Reinforce the importance and independence of internal and external audit and other similar review processes (for example, providing a view on the statement of internal control) from other functions of the Council e.g. Executive and Overview and Scrutiny and
  - Provide additional assurance to the full Council through a process of independence and objective review

For these reasons, the CIPFA guidance encourages Councils to look at setting up free-standing Audit Committee to enable authorities to firmly demonstrate that their statutory responsibilities referred to above are being fulfilled in a focused and independent manner by a body distinct from the Council's Executive and Scrutiny functions.

## **2. The Rules of Governance – what should they contain?**

- 2.1 The CIPFA guidance sets out a clear direction which it recommends authorities to consider in connection with setting up an Audit Committee. Whilst the precise terms and functions of the committee will be a matter for each authority to determine, the guidance advises that the committee's Rules of Governance should address the points set out below.

### **2.2 Statement of Purpose**

The guidance suggests that each authority should formally approve a Statement of Purpose in respect of its Audit Committee to make it clear what it is intended to achieve. The attached draft Rules of Governance do this in Paragraph 1.1 and they follow, verbatim, the recommendations set out in the guidance. It is suggested, therefore, that the Council adopt the Statement as drafted.

### **2.3 Terms of Reference**

The terms of reference proposed for the committee are set out in Paragraphs 2.1, 2.2 and 2.3. Members will see that they are grouped under three broad headings dealing with Audit Activity, Regulatory Framework and Accounts. Again, the terms of reference proposed follow closely those recommended in the guidance, tailored where necessary to meet the specific circumstances of the City Council. The only area which perhaps requires further comment is that relating to the Accounts function in Paragraph 2.3 of the draft Rules of Governance. The committee's powers in this paragraph, and subsequently as set out in Paragraph 9.1 of the Rules, refer to the Audit Committee having power to review the annual Statement of Accounts and pre-suppose that formally signing off the Statement of Accounts would be reserved to the full Council. It is a matter for Members to consider whether they would wish to retain this position or whether they would like to ask the Council to give the Audit Committee delegated powers to sign off the accounts as well, rather than having to refer them to full Council. Referring them to full Council with an appropriate recommendation could be seen as giving the signing off of the Statement of Accounts a high profile and importance, but it is likely to necessitate calling special meetings of the Council if the timetable of ordinary Council meetings does not allow the sign off to take place by the date required.

### **2.4 Independence of the Committee**

The guidance says that, to be effective, the Audit Committee needs to be independent from both Executive and Scrutiny. It believes that, whilst the link with the Scrutiny function can be beneficial in some ways, the ultimate power of the Audit Committee could be compromised by too much cross-membership with the Council's other committees and bodies. The Audit Committee needs to retain the ability to challenge the Executive on issues and to report to it on major matters and contraventions. Therefore, the guidance

recommends that cross-membership should not be the norm but, if it is seen as necessary, it should be restricted to one member from each of Executive and Scrutiny only. In addition, it recommends that the Audit Committee chair should not be a member of the Executive. A non-Executive chair is seen as important in order to promote the objectivity of the Audit Committee and to enhance its' standing in the eyes of the public.

- 2.5 Following this advice the draft Rules, at Paragraph 5.1, provide that only one member of the Executive, Overview and Scrutiny and Regulatory Committees will be eligible to be a member of the Audit Committee. They also provide that the Council will be responsible for appointing the Chair of the Committee in Paragraph 3.2 of the draft Rules, although this is not a requirement as such and the Council could decide to leave it to the Committee to appoint its own Chair in the usual way.

## 2.6 Composition of the Committee

The size of the Audit Committee is relevant although not crucial. Too small a number of members and political balance may be difficult to achieve; too large and meetings may become unwieldy. HM Treasury guidance recommends between three and five members of an Audit Committee and so, in Paragraph 5.1 of the Rules, it is proposed that the Committee consists of five voting members. There is provision for the Council to co-opt other non-voting members, as required, but it is not recommended that this is done from the outset but should only take place (if at all) once the committee has become established and comfortable with its' own operating procedures and practices.

## 2.7 Frequency of Meetings

The frequency and timing of meetings is a matter for each authority to determine, based on its own committee timetable and needs. However, the guidance advises that, from general practice, at least four meetings per year appear to be appropriate. One meeting annually will be taken up with setting the programme, agreeing audit plans and generally preparing for the year ahead, leaving three meetings which are available for monitoring purposes and to fit in with the cycle of statements and financial reporting. Authorities are likely to wish their Audit Committees to meet before approval of the accounts, to review both the financial statements and the draft SIC and after completion of the review of the auditors report to those charged with governance. If responsibility for signing off the Statement of Accounts is formally delegated down to the committee then it will, of course, have to meet to carry out this function as well. Paragraph 7.1 of the draft Rules, therefore, provides for the Audit Committee to meet at least four times per year, with the proviso for other special meetings to be called as required in accordance with the Council's Procedure Rules. A draft timetable for the Audit Committee's work is set out in Appendix A by way of an example, although this would need to be refined in consultation with the Director of Corporate Services and the Head of Audit Services.

## 2.8 Skills, Experience and Training

The guidance indicates that, to be effective, members of the committee will require certain skills and will benefit from having gained experience in some of the key areas to be considered by the committee. Whilst the guidance recognises that financial awareness is essential, particularly for the chair, it sees an accounting background or qualification as less important than a broad understanding of the financial, risk and control and corporate governance issues facing local authorities generally and the Council specifically. It suggests that an ability to question, probe and seek clarification about complex issues is also essential.

2.9 The guidance recognises that identifying sufficient members with appropriate skills and experience may be difficult, if such members could already be serving on other committees and thus may not be eligible for membership of the Audit Committee. It recognises that appropriate and timely training for members will help to overcome this problem and build up on the key attributes of independence, a risk focused attitude and a balanced approach that preferred Members will already possess. It suggests that induction training should be provided for all new Committee Members and should cover :

- The role of the Committee.
- The terms of reference.
- The time input required of Members
- An overview of Council activities and
- The financial and risk environment

Further regular audit committee training should also be provided in:-

- Financial reporting
- Governance
- Understanding financial statements
- The Regulatory Framework
- Role of internal and external audit and
- The importance of Risk Assessment

## 2.10 Administration

The guidance recognises that effective administrative support of the committee will clearly be important if the committee is to take an active part in Council business. The regular attendance of the key senior management figures mentioned in the Rules in Paragraph 6.1 is therefore recommended, both to maintain the credibility of the committee and to ensure that Members are adequately supported by appropriate officers. The Chief Finance Officer will obviously have an important relationship with the committee. This officer's role and that

of the Audit Committee are closely aligned and complementary and CIPFA's guidance states that one of the Chief Finance Officer's key roles is one of "maintaining strong financial management underpinned by effective financial controls". The Chief Finance Officer's role is also seen as "supporting and advising democratically elected representatives" and the Officer will therefore be a key point of contact for Audit Committee Members. The guidance suggests that, as the Committee will need to receive advice from the Officer on most, if not all, of the matters taken to the body, then this Officer or her/his deputy will be required to attend all meetings to fulfil this function and so give the Committee the credibility and support required to carry out its role.

### **3. Recommendation**

- 3.1 Whilst currently some of what could be described as audit committee functions are nominally allocated to the Corporate Resources Overview and Scrutiny Committee, it is clear that this is one of many functions carried on by that Committee. It is recognised that there is a need to give attention to audit matters a much higher profile in the authority and to put in place a structure to allow elected Members to have a closer involvement in such matters and, in particular, in the working up of the Statement of Accounts and SAS 610 reports to the formal approval stage. The CIPFA guidance and the direction it sets out also has strong Audit Commission support and it is right that the Council should be seen demonstrably to be adopting best practice in this area. It is therefore recommended that the Council should establish a free-standing Audit Committee in the light of all these factors.
- 3.2 It is therefore recommended that the Committee:-
- (a) consider the proposed Rules of Governance and if they are happy with them,
  - (b) recommend them, together with any appropriate amendments which the Committee may wish to make, to the full Council for approval on the 2 May next with a view to the Audit Committee being established as part of the Council's governance arrangements as from the Annual Council meeting on the 22 May next.

John Egan  
Director of Legal and Democratic Services

## **AUDIT COMMITTEE**

### **RULES OF GOVERNANCE**

#### **1. STATEMENT OF PURPOSE**

- 1.1 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.

#### **2. TERMS OF REFERENCE**

##### **2.1 Audit Activity**

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.

To consider summaries of specific internal audit reports as requested.

To consider reports dealing with the management and performance of the providers of internal audit services.

To consider a report from internal audit on agreed recommendations not implemented within a reasonable timescale.

To consider the external auditor's annual letter, relevant reports, and the report to those charged with governance.

To consider specific reports as agreed with the external auditor.

To comment on the scope and depth of external audit work and to ensure it gives value for money.

To liaise with the Audit Commission over the appointment of the Council's external auditor.

To commission work from internal and external audit.

##### **2.2 Regulatory Framework**

To maintain an overview of the Council's Constitution in respect of Contract Procedure Rules, Financial Regulations and financial Codes of Conduct and Behaviour.

To review any issue referred to it by the Town Clerk and Chief Executive or a Director, or any Council body.



To monitor the effective development and operation of risk management and corporate governance in the Council.

To monitor Council policies on "Raising Concerns at Work" and the anti-fraud and anti-corruption strategy and the Council's complaints process.

To oversee the production of the authority's Statement on Internal Control and to recommend its adoption.

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

To consider the Council's compliance with its own and other published standards and controls.

## **2.3 Accounts**

To review the Annual Statement of Accounts and to make recommendations to Council in respect of the approval of the 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.

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

## **3. ACCOUNTABILITY**

3.1 The Audit Committee will be a stand alone Committee of the Council. All Audit Committee members will act in the interests of the Council and not on behalf of any political party, constituency, ward, or interest group.

3.2 The Chairman of the Audit Committee will be appointed by the Committee. The Chairman and the Committee will ensure that relevant issues are promptly brought to the attention of the Executive, Overview and Scrutiny and Regulatory Committees or the full Council.

3.3 The Chairman of the Audit Committee will present an Annual Report on the work of the Audit Committee to the full Council.

## **4. AUTHORITY AND ACCESS**

4.1 The Audit Committee has a right to request relevant information from appropriate or relevant Members and Officers of the Council.

4.2 The Audit Committee will not be able to transact the powers, functions and duties reserved to the full Council, the Executive, Overview and Scrutiny and other Regulatory Committees.

4.3 The Audit Committee will have access to in-house financial, legal and any other professional advice necessary to carry out its functions.

4.4 The Chairman of the Audit Committee and the external and internal auditor will meet as necessary and the Council's Head of Audit Services will provide necessary services and support and assistance to the Audit Committee.

4.5 Any Member, Officer or member of the public who has any concern covered by the Terms of Reference of the Audit Committee may raise the matter with the Chairman of the Committee who will obtain, if necessary, relevant advice from the Council's Monitoring Officer or the Section 151 Finance Officer before taking any action with regard to the same.

## **5. MEMBERSHIP**

5.1 Audit Committee members will be appointed by the Council and consist of (5 or 6) members in accordance with the rules governing political balance. No member of the Executive and no chair of the Overview and Scrutiny Committees will be eligible to be a member of the Audit Committee.

5.2 The Audit Committee will be provided with administrative support by the Legal and Democratic Services Department and reports/decisions of the Audit Committee will be recorded and published on CMIS in the usual way. The People, Policy and Performance Directorate will provide technical support to the Committee when required. As the decisions of the Audit Committee will not be of an executive nature, the decisions will not be the subject of a request for call-in. If any Member is concerned about any decision of the Audit Committee, s/he should raise the matter with the Chairman of the Audit Committee, the Monitoring Officer, the Section 151 Finance Officer and/or ask an oral question of the Chairman of the Audit Committee at the Council meeting in accordance with the relevant Council Procedure Rules.

## **6. ATTENDANCE**

6.1 The Audit Committee shall meet on a regular basis as provided for in paragraph 7 below. Officers and others may attend all or part of the meeting at the invitation of the Committee. Attendees will usually include:

- The Leader or Deputy Leader
- The Portfolio Holder for Finance
- Town Clerk and Chief Executive
- Director of Corporate Services (Section 151 Finance Officer)
- Director of Legal and Democratic Services (Monitoring Officer)
- Head of Audit Services
- Other Directors and Managers, as required

6.2 Subject to the relevant meeting complying with the Access to Information paragraphs for the exclusion of members of the public, the Audit Committee will at least annually meet :

- (i) in private, with the external and internal auditors together; and/or
- (ii) in private, with the external auditor.

## **7. MEETINGS**

- 7.1 The Audit Committee will meet at least four times a year in accordance with the schedule of meetings agreed by the Council. The External Auditor or the Head of Audit Services may request a meeting if they consider it necessary and other special meetings may be called in accordance with the Council's Procedure Rules. Appendix A contains an outline Audit Committee timetable.
- 7.2 The members of the Audit Committee will commit to receiving appropriate training and development necessary to fulfil their roles.

## **8. QUORUM**

- 8.1 The quorum for any meeting will be one quarter of the elected members of the Committee, subject to there being not less than two elected members present at any time.

## **9. WORK PROFILE OF THE AUDIT COMMITTEE**

- 9.1 In furtherance of the Terms of Reference and not otherwise, the Audit Committee is likely to receive and advise upon the following areas of work :

- Whether there is an appropriate culture of risk management and related control throughout the Council;
- the annual Statement on Internal Control (SIC);
- the annual Statement of Accounts, including changes in and compliance with accounting policies and practices, major judgemental areas and significant adjustments resulting from the audit;
- significant changes required to Financial Procedure Rules and the Contracts Procedure Rules.
- the framework and processes for risk assessment, analysis and management within the Council;
- the effective co-ordination between internal and external audit;
- the budget needed to resource effective internal and external audit and other responsibilities of the Audit Committee; and
- generally, on how the Audit Committee could add value to the work and operation of the Council.

### **9.2 External Audit and Inspection Agencies**

- To note the fees and terms of engagement of the external auditor.
- To review the planned programme of work with the external auditor.
- To consider the annual statutory audit and to advise the Executive on any response to any audit management letters, reports and investigations, including Value for Money studies and other inspection reports.
- To review whether agreed external or internal audit or inspection recommendations have been implemented by the Executive as timetabled.
- To discuss with the external auditor any problems, reservations or issues arising from the interim or final audit or other investigations.

- To review the external auditor's independence and objectivity and annually appraise the Executive on the effectiveness and value for money of the external audit service.

### 9.3 Corporate Governance Framework

- To review and advise the Executive on the embedding and maintenance of an effective system of corporate governance including internal control and risk management.
- To give an assurance to the Council that there is a sufficient and systematic review of the corporate governance, internal control and risk management arrangements within the Council.
- To review the Statement on Internal Control and make appropriate recommendations to the Council, the Executive, the Overview and Scrutiny and Regulatory Committees.
- To ensure that any significant weaknesses identified are remedied.
- To commission, if necessary, any relevant investigations into matters of particular concern relating to internal control.
- To ensure that the impact of any alleged or fraudulent activity on the Council's framework of internal control is reviewed and, where necessary, to recommend changes to strengthen the control framework.
- To receive reports relating to those aspects of whistle blowing or alleged or actual fraudulent activity which relate to the Terms of Reference of the Audit Committee.

### 9.4 Internal Audit

To review and make recommendations to the Executive regarding :

- The effectiveness of internal audit;
- the internal audit function to ensure it is adequately resourced;
- the internal audit strategy, annual plan and to monitor delivery of the plan;
- any internal audit protocols and policies;
- significant audit findings, together with the response from managers to these reports;
- any difficulties encountered by internal audit including any restrictions on the scope of activities or access to required information;
- agreed internal audit recommendations to ensure they are implemented by management as timetabled; and
- the annual report from the Head of Audit Services.

### 9.5 Other

To consider and make recommendations to the Executive on :

- the selection and terms of appointment of other appropriate advisors and consultants;
- governance issues relating to the operation of the Audit Committee, and
- the proportionality, independence, and appropriateness of any of the Council's policies relating to any audit or governance matters.
- such other matters of an audit, financial or governance nature as fall within the terms of reference of the Committee or as may be referred by the Council.

# APPENDIX A

## DRAFT AUDIT COMMITTEE TIMETABLE

	Agenda Item/Issue	April	July	October	January
1	Review of internal audit annual plan.	X			
2	Review of internal audit progress reports and summary of key findings.	X	X	X	X
3	Review of final accounts timetable and plans.				X
4	Review of annual account progress.	X			
5	Review of Statement on Internal Control to accompany the final accounts.	X			
6	Review of external audit annual plan.	X			
7	Receipt of annual internal audit report.		X		
8	Review of audited final accounts and financial statements.		X		
9	Review of External Audit annual letter.				X
10	Private discussions with internal and external audit			X	
11	Self assessment of Audit Committees' effectiveness				X

12	Briefing/update sessions			X	X
13	Review of other reports and policies as appropriate e.g. changes to Financial Regulations.	X	X	X	X