

## **Annual Report of the LG Group Audit and Scrutiny Panel**

### **Purpose of report**

For review and consideration.

### **Summary**

1. New audit committee arrangements were introduced in 2010/11 to support the integration of operations across the Group, with the functions previously covered by the separate audit committees of the LGA and the LG Group companies, now being covered by one audit and scrutiny panel.
2. The Panel has met quarterly since its first meeting in September 2010 where it agreed a programme of work for the year to enable it to meet its responsibilities.
3. This is therefore the LG Group Audit and Scrutiny Panel's first annual report, to both the LG Group Executive and the LGA General Assembly.

### **Recommendation**

To review the first annual report of the Group Audit and Scrutiny Panel.

### **Action**

The LG Group Audit and Scrutiny Panel to develop a programme of work for 2011/12, building on the progress made in 2010/11.

**Contact officer:** Helen Platts

**Position:** Strategic Business Adviser

**Phone no:** 020 7296 6819

**E-mail:** helen.platts@local.gov.uk

## **Annual Report of the LG Group Audit and Scrutiny Panel**

### **Introduction**

1. New audit committee arrangements were introduced for the LG Group in 2010/11, with the result that the functions previously covered by the separate audit committees of the LGA and the LG Group companies, have been covered by one audit and scrutiny panel for the LG Group.
2. A list showing the membership of the Audit & Scrutiny Panel is attached
3. The new arrangements have been introduced as part of the Getting Closer programme to support the development of fully integrated operations for the Group including a consistent set of business processes.
4. The responsibilities of the Panel are to:
  - 4.1 Review the financial statements of the organisations in the LG Group
  - 4.2 Monitor the processes for managing financial risks and internal control
  - 4.3 Monitor the operation of internal and external processes for the organisations in the Group
  - 4.4 Monitor delivery of the LG Group Business Plan
  - 4.5 Report back on specific issues, commissioned by the LG Group Executive
  - 4.6 Monitor the use of resources, including the effective use of top-slice funds
  - 4.7 Consider issues of probity and conduct.
5. The Panel has met quarterly since its first meeting in September 2010 where it agreed a programme of work for the year to enable it to meet its responsibilities.
6. This is therefore the LG Group Audit and Scrutiny Panel's first annual report, to both the LG Group Executive and the LGA General Assembly.

### **Executive Summary**

7. The main focus of the Panel's work in 2010/11 has been to review the internal audit programme for the Group. This has confirmed that progress has been made in developing a consistent set of business processes for the Group, particularly with governance and risk management.

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8. The Panel recognises the need for further work to strengthen internal controls within the Group, especially in the key areas of income and debtor management, the procurement of goods and services and a number of other financial procedures identified by the internal auditors. Progress with these will be kept under review by the Panel as part the 2011/12 internal audit programme.
9. The Panel will also focus on ensuring that internal audit recommendations from 2010/11 are fully implemented. While the internal auditors reported adequate progress in implementing previous internal audit recommendations, the Panel recognises the opportunity for faster progress now to be made with the creation of one business support function for the LG Group from June 2011.
10. The Panel has reviewed the audited financial statements for 2010/11 for the LGA, the Local Government International Bureau and the LGA property companies which have received an unqualified audit opinion; and is due to review the audited accounts of LG Improvement and Development, LG Employers and LG Regulation at its next meeting in July.
11. The Panel has reviewed progress in delivering the 2010/11 business plan but notes that so far its scrutiny role has been limited. As part of the governance review, due to take place in September 2011, Executive is asked to consider whether the current scrutiny arrangements are adequate.

**Financial statements and external audit**

12. For the last three years, the LGA and the LG Group companies (with the exception of the Leadership Centre) have commissioned one external auditor, KPMG, to act on behalf of the Group, reflecting the fact that much of the audit focuses on the shared finance service. The Panel considered KPMG's planned approach to the 2010/11 audits at its February meeting.
13. At its meeting on 1 June 2011, the Audit and Scrutiny Panel reviewed the 2010/11 audited accounts for the LGA, prior to these being adopted by the LGA Resources Panel, and also the 2010/11 audited accounts for the Local Government International Bureau and the LGA property companies, LGA Properties and LGMB.
14. The LGA financial statements for 2011/12 received an unqualified audit by KPMG. The accounts show that the LGA made a profit of £86k before exceptional items and pension adjustments for the 2010-11 financial year. This was in line with the forecasts previously provided. There was, in addition, a one-off receipt of £0.5m related to the transactions under which Local Partnerships was formed. Significant changes made by the actuaries to the assumptions on which pension liabilities are calculated, including in particular

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the change from RPI to CPI indexation of pensions, mean that, overall, the net pension deficit reduced considerably. The most significant audit recommendation related to improving controls over reconciliation of intra-group balances. This recommendation was accepted.

15. The audited accounts for LG Improvement and Development, Local Government Information House, LG Employers and LG Regulation are due to be reviewed at the next meeting of the Panel in July, prior to these being adopted by the relevant company boards.
16. It is standard practice for issues identified in the course of the external audit to be raised by the auditors with management and for these to be reported to the board members as "Performance Improvement Observations" in what is commonly known as the "Management Letter". The Panel has monitored progress with implementing the Performance Improvement recommendations made in 2008/09 and 2009/10, and found that good progress had been made. The Panel will also monitor progress with the recommendations arising from the 2010/11 external audit.

**Internal audit**

17. The Panel is responsible for agreeing the annual internal audit programme for the Group at the start of each financial year, taking account of the key risks identified in the Group risk register. In 2010/11 the different strands of internal audit activity across the Group - which until then had been separately commissioned by each of the organisations in the Group - were brought together for the first time in one integrated internal audit programme for the Group.
18. Internal audit for the LG Group is carried out by RSM Tenon, and the internal audit programme for 2010/11 is now nearly complete. RSM Tenon's annual report was presented to the June meeting of the Panel. Based on the work undertaken in 2010/11, the internal auditor's opinion regarding the adequacy and effectiveness of the LG Group's arrangements for governance, risk management and control was as follows:

**Governance and Risk Management** – an Amber-Green assurance opinion with three medium priority recommendations. The internal auditors recognised that the LG Group has undergone significant governance changes in 2010/11 as part of the "Getting Closer" programme

**Control** – eight assurance and two advisory reviews were carried out. One Red assurance opinion was provided in relation to income and debtors, four Amber-Red opinions and two Amber-Green opinions (with Data Protection – HR self service still to be reported on). The Follow-Up review concluded that adequate

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progress had been made in implementing previous internal audit recommendations.

19. All of the internal auditors' 12 high priority and 35 medium priority recommendations have been accepted by management, apart from five recommendations where the internal auditors have confirmed they are satisfied with management's response and that they have understood the risks identified.
20. The full reports from RSM Tenon for each internal audit assignment have been considered by the Panel and the audit opinions are summarised below:

<b>Internal audit assignment</b>	<b>Internal audit opinion</b>
Health and Safety	Amber-Red
Value for money – printing arrangements	N/A - advisory
Compliance with ICT policies	N/A - advisory
Conference facilities	Amber-Red
Business Continuity	Amber-Green
Income and debtors	Red
Bidding and management of grants	Amber-Green
Data Protection – HR self-service	to be presented in July
Key financial controls	Amber-Red
Governance and Risk	Amber-Green
Procurement	Amber-Red
Follow-up of previous internal audit recommendations	Adequate progress

21. The key issues addressed by the Panel in reviewing the internal auditor's finding were:
  - 21.1 That further work is done to strengthen the Group's debtor management, with a full report on progress to the Panel in September 2011.
  - 21.2 That procedures are strengthened to ensure in-house printing services are being used
  - 21.3 That steps are taken to ensure with regard to ICT security that the LG Group is ISO certified
  - 21.4 That managers sign off against the Business Continuity policy to ensure they fully understand their responsibilities in relation to it
22. The internal auditors have acted as internal auditors to the LGA and the LG Group companies since 2007/08. The Panel has agreed to this service now being re-tendered, and this exercise is now underway.

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**Risk management and internal control**

23. During 2010/11 significant progress was made in developing a coherent risk management framework for the LG Group. For the first time a strategic risk register was developed which was kept under review by the Group Strategic Management Team and also regularly reported to the Panel. The Panel has made suggestions for improving the presentation of the Risk Register, to ensure that risks are appropriately assessed and managed.
24. In the course of the year, the Panel focused on two particular areas of risk for the Group: managing the pension deficit for the Group; and the approach to Treasury Management.
25. With regard to managing the Group Pension Risk, the Panel noted the potential mitigations of risk around the future level of employer pension contributions and noted that an agreement on any approach beyond standard arrangements would be sought from the Resources Panel and the respective company boards. A steer has since been provided by the Resources Panel and the individual company boards have agreed to increase pension contributions through a combination of an additional one-off payment and additional annual payments for ten years from 2011/12.
26. With regard to the Treasury Management policy, Panel members expressed concern about the risk/returns ratio of the current investment portfolio and that the portfolio should include the potential to invest in Treasury bills. These recommendations have now been pursued with the LGA Resources Panel which oversees the LG Group's investment strategy.

**Performance monitoring**

27. The Panel reviewed progress at the half year stage in delivering the priorities in the 2010/11 business plan for the LG Group. A six month "traffic light" report was presented on the objectives and deliverables included in the 2010/11 business plan.
28. A consistent set of corporate health indicators was also agreed for the LG Group for the first time in 2010/11, covering collection of LGA subscriptions, financial management including debtors, a number of HR indicators (including the number of employees, learning and development activities and sickness absence), satisfaction with the Liberata service, and the LG Group's environmental performance. Members received a six month report on these showing a generally positive direction of travel.

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29. The full performance report for 2010/11 will be reviewed by the Panel at its July meeting, prior to being presented to the LG Group Executive and the Councillors Forum.
30. The Panel will have oversight of the performance framework for 2011/12 which is currently being developed. The Panel has emphasised the importance of developing tangible, quantitative outcomes in developing the performance framework while recognising the difficulties of measuring the impact of the Group's lobbying work in particular.

**Use of resources**

31. At its first meeting the Panel reviewed the LG Group's use of resources and the application of top-slice funds in 2009/10. The Panel asked for future reviews of the LG Group's use of resources to focus on the effectiveness of shared services, and also how resources are applied to priority areas.

**Probitiy and conduct**

32. The Panel has reviewed the LG Group's approach to managing probity and conduct. Officers are due to report back to the Panel in July with an annual update on this. No instances of fraud or corruption have been reported to the Panel in the course of the year.