

CABINET

28 SEPTEMBER 2010

REPORT OF THE CABINET MEMBER FOR FINANCE

Title: Internal Audit and Anti-Fraud Service Contract	For Decision
<p data-bbox="150 488 309 521">Summary:</p> <p data-bbox="150 557 1433 701">Since 2001 the Council has procured a proportion of its Annual Audit Plan requirements from an external provider. Initially this was with Deloitte and from April 2009 with Croydon Council under its “Croydon Framework Contract”, also known as the London Audit and Anti Fraud Partnership, or LAAP for short.</p> <p data-bbox="150 741 1437 1104">Joining Croydon’s framework has allowed the Council to buy-in audit reviews including those related to the adequacy of the Council’s key financial systems, computer audit and those aimed to provide assurance at individual schools. The contract also provides for advice on audit and control issues and time to follow up audit recommendations. Deloitte, one of the major audit suppliers in the UK, provides services under the Framework at a significantly lower cost, afforded by the large volume offered by a number of councils opting to join and securing Value For Money (VFM) from economies of scale. The Council is only required to procure the number of days it needs to supplement in-house resources to deliver the annual Audit Plan, and is not precluded from buying-in specialist resource from other providers should there be a VFM case to do so.</p> <p data-bbox="150 1144 1437 1395">The Council joined the framework for an initial 12 month period (extendable to 18 months - 1 April 2009 to 30 September 2010), with the intention of reviewing the quality of the arrangement before deciding if it was in the Council’s best interest to renew, after considering a number of existing and new options that were on the horizon. The previous Head of Audit and Risk indicated that a full options appraisal be undertaken ahead of any decision to ensure the most advantageous way forward for the Council would be identified and recommended.</p> <p data-bbox="150 1435 1437 1653">Aligned to this, the Chief Executive requested a review of the service be undertaken with a view as to whether it should be re-tendered or delivered via another option. This was reported back to CMT on 21 October 2009. All options were considered, against CIPFA benchmarked data, and the outcome was that CMT agreed to “maintain existing mixed economy arrangement, with improved contract monitoring, and to rationalise and reduce management arrangements, adopting a generic Anti-Fraud and Audit Service”.</p> <p data-bbox="150 1693 1422 1836">Since then other options have arisen and been considered, including a geographical shared service option (NELSS), however this did not develop, due to several of the councils involved joining the Croydon Framework and a lack of appetite for formal shared working arrangements.</p> <p data-bbox="150 1877 1437 2051">Recent soft market-testing undertaken (including Office for Government Commerce information), supports the recommendation that the Croydon Framework offers best value for the Council, combining economies of scale, flexibility and high levels of customer satisfaction (over 80% satisfaction levels achieved in key audit assignments). Additionally, the Council saves money from not undertaking a full tender procurement process, as this</p>	

has already been addressed by Croydon Council. Furthermore, there would be no disruption to the service from any transitional arrangements being required.

The Council currently has a small audit and anti-fraud programme (1400 days), approximately two thirds of the service is delivered by experienced in-house staff, the remainder is provided by specialist external staff, in areas as required where skill sets need to change to meet new technology and requirements e.g. Carbon Reduction Scheme. This arrangement ensures the Council benefits from a wide range of professionals, ensuring its audit and anti-fraud needs are well catered for. The latest CIPFA benchmarking (July 2010) indicates that 18 out of 22 London councils “buy-in” some or all of their audit service.

It would not be in the Council’s best interest to bring the specialist audits in-house, given difficulties in recruiting / retaining specialist staff and fully utilising them within a small team.

The Croydon Framework contract affords the Council continued value for money and will allow the Council to call upon highly qualified and experience specialists as it requires them. There are also soft benefits from an extensive network, where learning and resources can be shared to the advantage of each council in the partnership.

Wards Affected: None

Recommendation(s)

The Cabinet is recommended to agree:

- (i) In accordance with Constitution Contract Rules 3.6, to approve the procurement of the Council’s Internal Audit and Fraud services by way of entering into a contract with Croydon Council for the provision of these services under a contract that will operate from 1 October 2010 to 31 March 2015. The value of the contract, when aggregated with the value of the existing 18 month contract with Croydon, is above £400,000 and therefore requires the approval of the Cabinet.
- (ii) To note that under Constitution Contract Rules 4.1.3 that the Council is exempted from undergoing a separate tendering process under which tenders are invited for the service because the Council will be purchasing services “from a public purchasing body which has already completed a tender process in accordance with EU procedures” for those services.
- (iii) To agree that, in the event that Croydon’s contract with the service provider is extended beyond its existing contract term, the term of our contract with Croydon may also be extended for any such further extension period without need for further Cabinet approval.
- (iv) To agree that the contract shall contain a no-fault break clause in the Council’s favour allowing the Council an opportunity (in September of each year) to terminate the agreement should it wish to do so.

Reason(s)

The Council is recommended to agree to join Croydon’s existing framework agreement as

it

- Provides best value for money for the Council
- Offers maximum flexibility, having a “call down contract”
- Supports the delivery of the Council’s Audit and Anti-Fraud Strategies and Audit Plan
- Ensures the Councils Assurance Function is delivered by a tailored mixed economy approach

Comments of the Chief Financial Officer

The Croydon Framework offers significant reductions on daily rates for internal audit services as a result of the economies of scale produced with the number of boroughs involved and therefore this contract provides value for money. It is likely that given the Council’s constrained finances, there will be a greater need for internal audit compliance reviews to ensure compliance with core processes in the organisation and the reduced rates offered through the framework will provide future value.

Comments of the Legal Partner

The Council may procure services, including its internal audit and anti-fraud services, by joining ‘Framework Agreements’ that are operated by other local authorities or by other public bodies. By joining such a Framework Agreement, the Council will not be required to undertake its own tendering process for the procurement of the service, as it would normally be required to under the Council’s Contract Standing Orders. Where the Council joins another body’s framework agreement, it is also exempted from the requirements of EU procurement regulations.

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1. Background

- 1.1 The original Deloitte contract commenced in 2001 for a period of five years and was extended in February 2006, to operate until 31 March 2009. An options paper outlining various ways forward for procuring the audit service was provided to the Director of Corporate Resources and the Divisional Director of Corporate Finance in September 2008.
- 1.2 In early 2009, in discussion with the previous Head of Audit and Risk, Deloitte agreed to retain the same average day rate applying at that time for a further 12 months from April 2009 (extendable to 18 months) if the Council joined with Croydon Council under its “Croydon Framework Contract”, also known as the London Audit and Anti Fraud Partnership or LAAP for short. This was taken up in the knowledge that the Council would be unable to achieve similar rates if it went out to tender on its own (due to the small volume of audit days required). Accordingly, on 29 March 2009, the previous Head of Audit and Risk recommended that this option was agreed by Chief Officer, as it represented the best VFM and

flexibility for the council, and additionally saved the Council in the region of £24,315 per annum.

- 1.3 LAAP is a partnership / Framework Contract between Deloitte, who provides services to local authorities under the Framework, and London Borough of Croydon which allows for other local authorities to join. The framework was tendered under EU procurement rules and provides for 15,000 audit days in total. LAAP provides for discounts to apply on the average framework daily rate depending on the number of authorities joining the framework. The maximum discount was a 15% reduction on the starting average day rate, if the full 15,000 days are procured. Councils now within or considering joining the Croydon LAAP contract are set out in **Appendix A**.
- 1.4 At present, approximately one third of the Council's internal audit and anti-fraud services, including those audit reviews related to the adequacy of the Council's key financial systems and computer audit, as well as advice on audit and control issues and follow up of audit recommendations, are delivered via the contract with Croydon LAAP. Deloitte also provides services to LBBB for its schools audits. The Croydon LAAP operates effectively on a 'call off' basis – the Council specifies the audits it requires to be undertaken and Deloitte provides them.
- 1.5 At the time the contract with the Croydon LAAP was entered into, the previous Head of Audit and Risk recommended the Council join for a period of 12 months, extendable to 18 months, which would give the Council sufficient time for the value and quality of the contract to be assessed. He also recommended a full option appraisal be completed before the end of the final six months of the contract – the Council could then decide either to enter into a longer contract period or seek other options; for example shared service solutions, full tendering or other framework contracts. The options appraisal was to include market testing given the length of time since the previous full tender exercise.
- 1.6 Aligned to this, part way through the first year of operation, the previous Chief Executive requested a full review of the audit service be undertaken, including the:
 - Overview of the current service arrangements and findings
 - Options Appraisal for improvement in service configuration
- 1.7 A thorough review of the options were looked at, and the outcome was:
 - CMT agreed to “maintain existing mixed economy arrangement, with improved contract monitoring, and to rationalise and reduce management arrangements, adopting a generic Anti-Fraud and Audit Service”.
 - That emerging options including Strategic Partnering and alternative shared services under development are considered at a future date.
- 1.8 The detailed analysis undertaken at the time is set out in **Appendix B**.

2. Proposal

- 2.1 The current contract extension will end on the 30 September 2010. It is deemed not financially beneficial to undertake a full market-testing exercise, given the Audit Plan was reduced by 300 days in 2009/10, essentially making it highly unlikely that

the council would achieve lower rates than the Croydon LAAP due to no economies of scale being available on the number of days for an external supplier. Additionally, the Council saves money from not undertaking a full tender procurement process. Neither shared services nor the Joint Venture options are viable at this stage.

- 2.2 In addition to the option appraisal and market testing undertaken previously, additional soft market testing still indicates that the most advantageous option is to join the Croydon LAAP, when considering economies of scale, flexibility and quality. Details of this are shown in **Appendix C**.
- 2.3 The Audit and Risk Controller proposes that the most advantageous option for the Council is to re-join the Croydon Framework contract from 1 October to 31 March 2015, with the option to extend for up to a further three years. This will be on a call-down basis and subject to annual renewal to remain with the framework.
- 2.4 Cabinet are asked to agree to enter into a contact with LB Croydon under which Croydon will be responsible for providing the internal audit and anti-fraud services to the Council. The contract will specify that the services are provided pursuant to the framework agreement that Croydon has entered into with Deloitte, and that Deloitte will be used to provide the actual services to the Council.

3. Financial Issues

- 3.1 There are no financial implications associated with the recommendations, the annual cost estimated as £86,000 is funded within existing resources.

4. Legal Issues

- 4.1 The new contract with LB Croydon will in effect be a continuation of the existing contract and for this reason Constitution Contract Rules 3.3 is applicable. This provision requires that aggregation of the values of such contracts should take place when applying the tendering requirements of the Constitution Contract Rules. When the value of the existing 18 month contract is combined with the expected value of the new contract (should it run its full length), the value exceeds £400,000. It is for this reason that Constitution Contract Rules 3.6 applies whereby the procurement of a contract of this value must be approved by the Cabinet.
- 4.2 Croydon's framework agreement with Deloitte was procured under a full EU procurement process, and this will allow Constitution Contract Rules 4.1.3 to apply. This provision is an exemption from the normal requirement to follow the tendering procedures contained in the Constitution Contract Rules where the Council purchases services "from a public purchasing body which has already completed a tender process in accordance with EU procedures" for those services. The Council will in effect be taking advantage of an existing framework agreement rather than conducting a formal tendering exercise. EU procurement regulations, which are contained in the Public Contracts Regulations 2006, will not apply in accordance with section 22 of the Regulations.
- 4.3 The Council's legal staff will produce the agreement with LB Croydon under which the Council will access the services for the four and a half year period. Although the Council will be entering into an agreement with Croydon (rather than directly

with Deloitte), the agreement will state that Croydon will arrange for Deloitte to provide the services to the Council, in effect as sub-contractors. The daily rates that will be payable will be subject to an annual inflation based adjustment. The agreement will contain a no-fault break clause in the Council's favour which may be exercised annually in September of each year.

5. Other Implications

- 5.1 **Risk Management**, although there is no requirement to do so, soft-market testing has been undertaken to support the recommendation.
- 5.2 **Contractual Issues** A contract in-line with Contract Rules 3.6 and 4.2.1 has been constructed. The procurement option recommended is in-line with this.
- 5.3 **Staffing Issues** There are no changes to the current staffing levels as a consequence to the recommendation put forward.

6. Options appraisal

- 6.1 In-line with the previous decision to join the LAAP framework, a number of options have been investigated to establish what offers best VFM, flexibility and quality for LBB. These are set out in the table below

Option	Positives	Negatives	Score (1Low-4High)
Undertake service in-house	Strengthen in-house permanent knowledge	Difficulty recruiting appropriately experienced staff. Difficult to fully utilise specialist staff within small team	2
Undertake a full tender exercise	Full test of the potential Market	Costs incurred Small volume of service, won't attract economies of scale	1
Join the Croydon Framework	VFM Flexibility Shared practise Established network Shared risk Shared knowledge & skills transference No service disruption		4
East London Shared Services	Established network. Shared knowledge	Lack of appetite Others joined Croydon framework Competition for similar audits i.e. financial audits	1

		at same time	
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7. Background Papers Used in the Preparation of the Report:

No public reports used, only non-public reports

Head of Audit and Risk Chief Officer report 29 March 2009

CIPFA Benchmarking report 2009

Interim Audit and Risk Controller CMT review paper 21 October 2009

CIPFA Benchmarking report 2010

8. List of appendices:

Appendix A - List of Boroughs within Croydon LAAP Framework Contract

Appendix B - October 2009 CMT review options (this appendix is private and confidential)

Appendix C - Soft' Market testing September 2010 (this appendix is private and confidential)