Summary
There is a requirement under the Accounts & Audit Regulations 2015 (England & Wales) for local authorities to have an internal audit function and effective internal control is also a responsibility of the Council’s Section 151 Officer. Regulations do not define how the service should be organised or delivered with many shared or joint arrangements in place across London supported by a number of private sector audit firms.

Finance Directors across east London are exploring the potential for a shared internal audit service with four boroughs supportive of taking the proposal on. As a result of having corporate governance and assurance oversight within its remit, this committee is offered the opportunity to identify any issues it would want Cabinet to consider ahead of making a decision.

Recommendation(s)
PAASC is recommended to:

i. Note the proposal to pursue a shared internal audit service with other east London boroughs;

ii. Note the interim management arrangements with London Borough of Redbridge for the service pending the development of a business case for shared services; and

iii. Identify any issues it wishes to be considered by Cabinet when considering any report on the progression of the proposals for shared internal audit.

1. Introduction and Background

1.1 Section 151 of the Local Government Act 1972 – England and Wales requires that every local authority should “make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs”.

1.2 This section of the Act also implies that external financial arrangements should be checked to ensure that council’s financial affairs are properly administered.
1.2 One of the mechanisms by which the S151 Officer responsibilities are discharged is via the internal audit service undertaking reviews and assessments of the control environment. Additionally, the Accounts & Audit Regulations 2015 (England & Wales) features the requirement for internal audit and requires that a “relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control”.

1.3 At Barking & Dagenham, the relatively small internal audit plan, which is agreed annually by PAASC, is delivered by a mixed economy of an in house team complemented by bought in resources from Mazars via the Croydon led framework contract.

1.4 As part of the Council’s voluntary redundancy scheme, the Group Manager, Assurance & Counter Fraud has decided to take the opportunity to leave the Council on 3rd July providing a stimulus to consider how the service is provided. In addition to Internal Audit, the Counter Fraud team, which covers both corporate and housing related fraud, reports in to the Group Manager.

2. Emerging proposal for shared service

2.1 Over recent months, Section 151 Officers across east London have discussed the scope for sharing finance and corporate services across two or more boroughs. Internal Audit was identified at an early stage as a potential service that could be progressed more quickly due to a variety of circumstances across the region including excess and under capacity, recruitment challenges and imminent departures. It was also highlighted as a service currently shared, to some degree, in approximately half of all London boroughs.

2.2 As a result of the discussions, four boroughs, Waltham Forest, Redbridge, Tower Hamlets and Barking & Dagenham, are interested in progressing the business case for a shared service. An initial high level scoping exercise has been completed indicating how the service could be operated and the potential benefits from a shared service:

- Service resilience – a larger shared resource will add capacity and resilience to the service than currently from such a small team.
- Best practice – combining teams into a single resource will enable the sharing of both best practice in internal audit itself and control improvements from undertaking the same audits in each authority. The ambition will be to develop a centre of excellence for internal audit across East London.
- Financial savings – bringing together the management levels across the participating councils will enable financial savings. Given the relatively small size of the team and the audit plan, these are not expected to be significant for Barking & Dagenham.
- Skills shortages – the role of internal audit has evolved in recent years in to a more advisory capacity rather than the focus on controls based testing. This broader skill set, and wider learning opportunities, is more easily delivered within a larger team.
- Career opportunities – internal audit at Barking & Dagenham is a small team with limited career opportunities. By bringing together four teams, the service will be of a size and will deliver a wider range of audit to enable the development of a career path for members of the team.
- Recruitment challenges – specialist internal auditors are at a premium and all councils have experienced challenges in filling vacant roles, often competing for a very small number of candidates. A larger shared service would be better placed to manage these issues and would also be of a scale that could consider the employment of specialist roles that are not justified for an individual authority, e.g. IT audit, contract audit.

- Retender of Mazars contract – the Croydon contract with Mazars expires in March 2018 and authorities are operating in a different environment to when it was originally let five years ago. Whilst Croydon have indicated a willingness to lead on a re-tender, a shared service would be large enough to consider letting its own contract to reflect the specific needs of the partner boroughs.

2.5 The four Councils have agreed to jointly fund the development of a full business case by an individual or organisation independent of all participating authorities and such proposals are currently being sought. It is expected that this will be delivered by the end of the summer and will, assuming it reaches a positive recommendation, form the basis of a recommendation to the Cabinet (or equivalent) of each authority. The Cabinet Member for Finance, Growth & Investment has been regularly briefed on the scope and is supportive of the development of a full business case.

2.6 In the event of the shared service being successful, there is the potential to expand to include additional councils and for any arrangements to incorporate Counter Fraud. It has been decided, partly due to the different arrangements in place at each authority, to keep fraud as a phase two option and to focus attention on internal audit initially.

2.7 Whilst PAASC is not a decision making body, due to its remit on corporate governance and assurance oversight, and the role internal audit plays in fulfilling that, the committee is being invited to comment on the proposal for the shared service. It is then intended to incorporate those comments into the report to Cabinet in the event the business case recommends progression of the shared service, so they are considered as part of any decision making process.

3. **Short term management arrangements**

3.1 As noted in the introduction, the Group Manager – Assurance & Counter Fraud expressed an interest in leaving the Council under the voluntary redundancy initiative. In light of the proposal being explored for shared services, this application was accepted with a final day of service of 3 July 2016.

3.2 Due to the exploration of shared services, the Strategic Director, Finance & Investment, in consultation with the Cabinet Member for Finance, Growth & Investment, has decided on an interim management arrangement for the service with the London Borough of Redbridge.

3.3 Redbridge operate a larger audit plan than Barking & Dagenham and therefore have a larger in house internal audit team. As a result, given the emerging plans, Redbridge are freeing up capacity at Head of Audit and Audit Manager level to support the Barking & Dagenham team. This will provide the team with sufficient management capacity in the interim and will, along with extra audit delivery support from Mazars, will ensure the continued delivery of the audit plan. It is anticipated
that this arrangement will continue to the end of the year while the shared service proposals are being developed.

3.4 To enable this to operate effectively, Legal officers are drafting a Section 113 agreement to support the part time secondments and the Council will be reimbursing Redbridge for the proportion of time spent by their staff working at Barking & Dagenham.

3.5 In the event that the shared service does not progress, the Council will review the service needs for Assurance & Counter Fraud and recruit to the required roles.

4. **Financial Implications** – **Completed by Kathy Freeman, Finance Director**

4.1 The annual budget for the internal audit service is £607k reflecting the relatively small size of the annual audit plan. Since 2012/13, the service has contributed £102k to meeting the Council's budget gap. As noted above, the development of a shared service could deliver some financial savings though, given the size of the current plan and budget, these are expected to be small with greater non financial benefits for the authority. The potential financial saving will be part of the business case to be considered by Cabinet.

4.2 The cost of the interim management arrangement will be contained within the costs of the vacant Group Manager and Assurance Manager roles. Any loss of capacity to deliver the audit plan will be met from the Mazars contract and this cost will also be contained within the overall budget for the service.

5. **Legal Implications**: **Completed by Fiona Taylor, Director of Law & Governance**

5.1 Section 101 of the Local Government Act 1972 permits two or more authorities to discharge their functions jointly as envisaged in this arrangement for the Internal Audit Service. S1(1)b of the Local Authorities (Goods and Services) Act 1970 also permits the provision jointly of any administrative, professional or technical services.

5.2 It is envisaged here that officers will work under s.113 agreements under the 1972 Act which allows an authority to enter into an agreement to place at the disposal of another authority for the purposes of their functions, on such terms as may be provided under the agreement, officers of that authority. Legal Services have been consulted on the agreements and will advise accordingly.

6. **Other Implications**

6.1 **Risk Management** – internal audit is one of the key mechanisms for the management of risk in the Council. As such, it will be essential that there is no loss in the quality or capacity of the service to the Council as part of a shared arrangement and this will need to be considered as part of the assessment of the business case.

6.2 **Staffing Issues** – in the event the participating councils agree to progress a shared service, there will need to be a full consultation with all affected staff in line with the relevant policies for each authority. Additionally, the relevant agreements will need
to be put in place between the councils to enable staff in the shared service to work effectively in each borough.

6.3 **Contractual Issues** – if the shared service is progressed, a clear agreement will be needed between the councils to ensure effective governance of the arrangement.

6.4 **Asset Management Issues** – the shared service will need to consider its accommodation needs and working style to enable it to effectively deliver the requirements of each council. It is anticipated that there would be a small accommodation saving from the development of the shared arrangement unless Barking & Dagenham acts as the host borough.

6.5 **Customer Impact** – internal audit is an internal service working with council departments and it is not anticipated that the end recipients of the service will be impacted by the proposal.

6.6 **Safeguarding Children** – no specific implications.

6.7 **Health Issues** – no specific implications.

6.8 **Crime & Disorder Issues** – no specific implications.

7. **Public Background Papers Used in the Preparation of the Report:** None

8. **List of appendices:** None