

Future Audit Arrangements for Community and Town Councils in Wales

Audit year: 2020-21 onwards

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This document summarises the responses to my recent consultation on future audit arrangements for town and community councils and sets out the future audit arrangements to apply for the audit of the 2020-21 accounts and in future years.

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Summary report

Introduction

Community councils in Wales are required to prepare accounts and have them audited by the Auditor General for Wales

- 1 The requirement for community councils to prepare accounts and to have those accounts audited is set out in law.
- 2 Section 13 of the Public Audit (Wales) Act 2004 (the 2004 Act) states that all local government bodies must make up their accounts to 31 March each year and ensure that the accounts are audited by the Auditor General for Wales (the Auditor General). Section 13 also states that the Auditor General must audit the accounts.

Audit is important as it provides assurance on the effective management and safeguarding of public money

- 3 As well as meeting the legal requirements for the audit of community council accounting statements, the audit work provides assurance on how councils have managed their finances.
- 4 An audit of the financial statements results in the publication of an independent opinion on how the statements have been prepared and whether they give a proper presentation of the body's finances as required by the relevant accounting framework.
- 5 The audit of public bodies plays a key role in ensuring that those responsible for handling public money are held accountable for the use of that money. Public audit strengthens accountability, both upwards to the elected or appointed members who make decisions about the allocation of resources, and outwards to the service users and beneficiaries, taxpayers and the wider community. Robust public audit also provides assurance on bodies' arrangements for managing their finances properly, including their arrangements for value for money and to safeguard public money.

My audit responsibilities as Auditor General set out in the 2004 Act apply to all community councils

- 6 The 2004 Act sets out my responsibilities as Auditor General for the audit of community council accounts. These include:
 - Sections 17 and 23: general duties to ensure that the accounts have been properly prepared, to provide an opinion on the accounts and to satisfy myself that the council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources;

- Section 22: duty to consider whether, in the public interest, I should make a report on any matter which comes to the Auditor General's notice in the course of the audit; and
 - Sections 30 and 31: duty to make arrangements for electors to ask questions or make objections to the accounts.
- 7 The audit arrangements must be sufficient to enable me to discharge my statutory duties.

Since 2008, I have identified significant and systemic failings in financial management and governance across the sector that are not identified at audit until more detailed audit work is undertaken leading me to conclude that the audit arrangements need to be changed

- 8 Since 2008, I have published a series of national reports highlighting common governance failures identified during the audit of community and town councils. These reports highlighted systemic weaknesses across the sector and that too many councils are failing to meet the minimum standards expected of them. Although there has been improvement in some areas, there remains significant scope for improvement across the sector.
- 9 More detailed audit work has been undertaken at individual councils where auditors have identified significant concerns. As a consequence of this work, I have published 18 reports in the public interest during 2018 and 2019. Links to the reports can be found in **Appendix 1**.
- 10 The issues identified in these public interest reports include:
- Lack of or inaccurate/incomplete accounting records and improperly prepared accounts
 - Poor internal control and financial management including failure to follow councils' proper expenditure authorisation processes
 - Failure to account for PAYE, leading to additional costs being incurred by councils
 - Poor budget setting and inadequate financial monitoring
 - Failure to comply with councils' own Standing Orders, leading to defective procurement of services and failure to ensure proper arrangements are in place to secure value for money
 - Overpayments to clerks
 - Poor governance and decision-making leading to unlawful expenditure

- 11 The audit issues reported are often longstanding issues. However, the limited scope of the current audit arrangements means that they were not identified, and could not have been identified, in a timely way. A more detailed and rigorous audit is needed for early identification of emerging problems. This will also assist councils to improve their arrangements at an early stage rather than issues continuing and potentially escalating for a prolonged period of time.

From 2020-21 onwards, my audit arrangements for community and town councils in Wales will include a three-year audit programme, designed to meet my statutory responsibilities while providing a sufficient level of audit assurance at a reasonable cost to individual councils

- 12 In January 2020, I consulted on proposals to change the way in which the audit of community and town councils in Wales is carried out. The consultation asked a series of eight questions.
- 13 I received a total of 136 responses to the consultation: 83% (113) of the responses were made on behalf of councils. This represents 15% of all councils in Wales. Individual responses were received from clerks, individual councillors, local residents, internal auditors and professional accountants acting for a number of councils across Wales.
- 14 A summary of the responses to each of the consultation questions is set out in **Appendix 2**. Overall, the responses received were supportive of the proposed audit arrangements. Respondents did however identify some recurring concerns. **Appendix 3** sets out these concerns and my response to them.
- 15 Following this consultation, I have decided that from the audit of the 2020-21 accounts onwards, my audit arrangements will involve an element of transaction-based audit testing. A transaction-based approach to the audit will involve auditors examining an individual council's accounts and tracing transactions through to source records, confirming the completeness and accuracy of the accounts. This approach would provide a significantly higher level of assurance over councils' accounts than that provided at present and address many of the significant issues that have been identified over the last few years.
- 16 Adopting such an approach across all councils each year would require a significant amount of time to be input to each audit and, given the small scale of many councils, would be disproportionate to undertake.
- 17 In order to ensure the arrangement, as a whole, is proportionate, for councils with income and expenditure of less than £2.5 million, transaction-based audits will be interspersed with more limited audit procedures on a three-year, cyclical basis. A three-year cycle will allow for identification of issues within a relatively short

timescale. Councils will also be aware that they would be subject to more detailed scrutiny on a regular basis.

- 18 This cyclical approach is not without risk. It is likely that some issues may not be uncovered until a transaction-based audit is undertaken. I consider that a three-year cycle balances these risks with the overall risk to the public purse and the cost of audit.
- 19 Therefore, the audit arrangements I have determined for community and town councils to be applied from the audit of the 2020-21 accounts incorporates a three-year cycle of two limited procedure audits and a transaction-based audit for each council. The introduction of the transaction-based audits will be staggered across the first three years of the new arrangements.
- 20 A summary of the audit approach is provided in **Appendix 4**.
- 21 In addition to undertaking a transaction-based audit once every three years, auditors would still undertake additional audit work where it is considered necessary. Examples of situations where additional work may be required include (but are not limited to):
- When matters come to the auditor's attention during the course of a limited procedure audit, e.g. through correspondence, objections or matters arising during the audit
 - When transaction testing highlights areas of audit concern
 - When councils fail to co-operate with the audit team
 - When significant problems have been highlighted in previous years
 - When a council fails to prepare accounts on a timely basis

Next steps

- 22 In November 2020, I will host a webinar to provide further detail to councils on how the new arrangements will work in practice. Audit Wales staff are discussing the arrangements with representatives of One Voice Wales and the Society of Local Council Clerks so that these organisations are equipped to support you as the new arrangements are rolled out.
- 23 Audit Wales is also considering how the audits will be delivered. Further information will be provided to all councils by January 2021.
- 24 The audit of the 2020-21 accounts will be undertaken in the late summer of 2021. We expect that fees for two years of the three-year cycle will be broadly in line with current audit fees. For the audit year in which more detailed work is undertaken, we anticipate that there will be a modest increase in the audit fee. Audit Wales is currently developing a fee model to support this approach.

Appendix 1

Reports issued by the Auditor General for Wales

Exhibit 1: Auditor General's annual reports

Annual financial management and governance reports
Financial Management and Governance – Town and Community Councils 2017-18
Internal Audit Arrangements at Town and Community Councils in Wales
Financial Management and Governance in Local Councils 2016-17
Financial Management and Governance in Community Councils 2015-16
Financial Management and Governance in Local Councils 2014-15

Exhibit 2: Reports in the public interest

Public interest reports issued in 2018	Public interest reports issued in 2019
Whitford Community Council	Bodorgan Community Council
Cadfarch Community Council	Buckley Town Council
Tirymynach Community Council	Connah's Quay Town Council
Llanwnnen Community Council	Cynwyd Community Council
Penally Community Council	Glynneath Town Council
Glantymyn Community Council	Llanfairpwll Community Council
Llanbrynmaur Community Council	Llanfrothen Community Council
	Llangristiolus and Cerrigceinwen Community Council
	Maenclochog Community Council
	Mumbles Community Council
	Penmaenmawr Town Council
	Rhosyr Community Council

Appendix 2

Responses to the consultation questions

Exhibit 3: responses to the consultation questions

Consultation questions	Agree	Disagree	Don't know
Current arrangements and the need for change			
Q1 I believe that the current community council audit arrangements can lead to too late identification of the type of audit issues highlighted in recent WAO reports in the public interest: Do you agree?	60%	25%	15%
Proposals for a new system of audit			
Q2 Have I identified the correct design principles for the proposed community council audit arrangements?	83%	17%	
Q3 Do the proposed community council audit arrangements meet the design principles I have identified?	83%	17%	
Q4 Do you agree that the proposed community council audit arrangements should incorporate detailed testing of transactions?	64%	36%	
Q5 Are there any alternative procedures that should be considered for inclusion in the proposed community council audit arrangements?	63%	37%	
Q6 Do you agree that the proposed community council audit arrangements should be a cyclical programme over a three-year period?	73%	27%	
Q7 Do you agree that the publication of annual reports and occasional national studies would be of benefit to the sector?	94%	6%	
Q8 Are there any specific areas of concern you consider it would be helpful for the Auditor General to undertake a national study, or to provide a Good Practice Exchange event (such as a webinar) on?	55% ¹	45%	

¹ Audit Wales is currently examining areas suggested by respondents to identify those that would be suitable for a national study or GPX event.

Appendix 3

Issues raised during the consultation

Small councils will be disproportionately affected by the new arrangements

A large proportion of community councils in Wales are small councils spending less than £10,000 to £15,000 each year. The risk of losses in these small councils is small and there is a case for exempting these councils from audit or for the audit to be conducted by the local unitary authority.

The audit arrangements set out in the consultation paper will place an undue burden on these councils. The audit arrangements should be tailored based upon the precept raised by individual councils with alternative audit cycles depending on the size of the council and outcomes from previous audits.

Some councils expressed concern over the increase in audit fees since 2014-15 and whether the revised arrangements would add a further burden.

Response

The Public Audit (Wales) Act 2004 requires all councils in Wales to prepare their accounts to 31 March each year and to have those accounts audited by the Auditor General for Wales. The Auditor General is not able to exempt such councils from the statutory audit requirement.

The Auditor General's annual reports on Financial Management and Governance have highlighted that many smaller councils do not have appropriate financial management and governance arrangements in place. This includes arrangements to prevent and detect fraud and other losses.

For many smaller councils, there is little scope for segregation of duties to minimise the risk of losses due to fraud, and previous reports in the public interest have highlighted some of the deficiencies identified by auditors. There is a higher risk of deficiency at these smaller bodies.

The revised arrangements are designed to be relatively straightforward and understandable. Introducing a complex arrangement with multiple tiers of audit and alternate audit cycles would not only present an administrative burden but also increase the risk of confusion for councils.

Audit fees are charged in accordance with the Wales Audit Office's Fee Scheme. The Fee Scheme is published annually. The Public Audit (Wales) Act 2013 sets out that audit fees cannot exceed the full cost of undertaking the audit. Since 2014-15, audit fees have been charged on this basis. The new arrangements may mean an increase in audit fees for each year when transaction-based audit testing occurs. However, auditors will consider the size of the council when considering the extent of audit work to be undertaken.

Audit Wales is developing a suite of audit tools and procedures to ensure that all audit work is carried out as efficiently as possible. Councils can also help to maximise the efficiency of the audit process by ensuring that information and documents required for the audit are provided on a timely basis and that proper accounting and other records are kept.

Councils should have an internal audit that undertakes much of the work proposed for the external audit

An annual internal audit that incorporates testing of transactions is sufficient to address the concerns raised by external auditors and removes the need for transaction testing by external auditors. Some respondents considered that such an internal audit should be mandated.

Some respondents queried if the proposed external audit approach would result in a duplication of effort by carrying out work already undertaken by the internal auditor.

Response

The Accounts and Audit (Wales) Regulations 2014 require all councils to maintain an adequate and effective system of internal audit of their accounting records and of their system of internal control.

The Auditor General's report on internal audit in the sector identified that not all councils make arrangements for internal audit. The Auditor General's Financial Management and Governance reports comment on the discrepancies between the internal auditor's findings and the external auditor's findings that result in qualified audit opinions. This is particularly apparent at some councils where the Auditor General has issued a report in the public interest. In some cases, even though the internal auditor has provided positive assurances to individual councils, it is clear that the internal audit process was not adequate and effective.

The issues highlighted in public interest reports are not common across the sector

The number of public interest reports is small and the problems identified are not common across all councils. A more proportionate response would be to target those councils that have issues rather than increasing audit measures across the sector.

Response

Audit work is normally undertaken by firms engaged by Audit Wales. However, when significant issues arise at individual councils, Audit Wales undertakes additional work in-house. As a result of this additional work, since 2008, public interest reports have been issued to 25 councils across Wales. At present, the Auditor General is considering

whether or not to issue public interest reports at another 14 councils. Audit Wales is currently undertaking additional audit work at a further 30 councils.

This represents almost 10% of all councils in Wales. Furthermore, the matters identified in the public interest reports are also identified in qualified audit reports at other councils.

Additional training is needed for clerks and councillors

Many councils employ only a part-time clerk. There is limited training and other support available. Training should be free of charge and available to all clerks to ensure they understand the basic requirements that are relevant to all councils.

Response

One Voice Wales and the Society of Local Council Clerks have area committees across Wales. These meet on a regular basis to discuss current issues.

One Voice Wales offers a training programme for councils to access. Courses are held across Wales and cover a variety of topics including financial procedures.

Audit Wales staff attend sector conferences throughout the year providing updates on developments and explaining how councils can address the issues raised by external auditors.

The Welsh Government has a bursary scheme for training in the sector and is currently considering how this scheme can be extended.

Transaction-based testing should be carried out locally rather than sending large volumes of documents to Audit Wales' offices

This work should be carried out at council premises to avoid the need to collate and submit detailed and voluminous working papers to an external body.

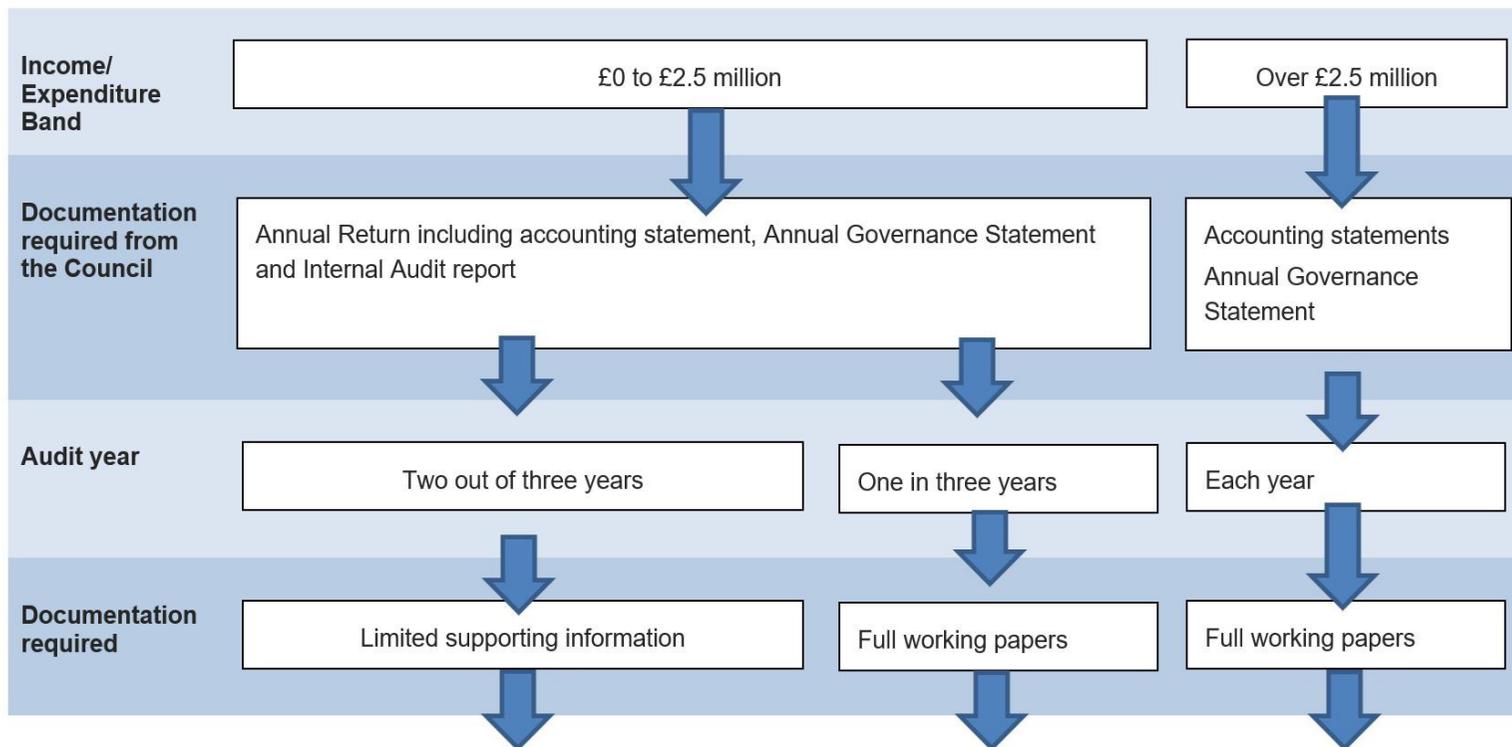
Response

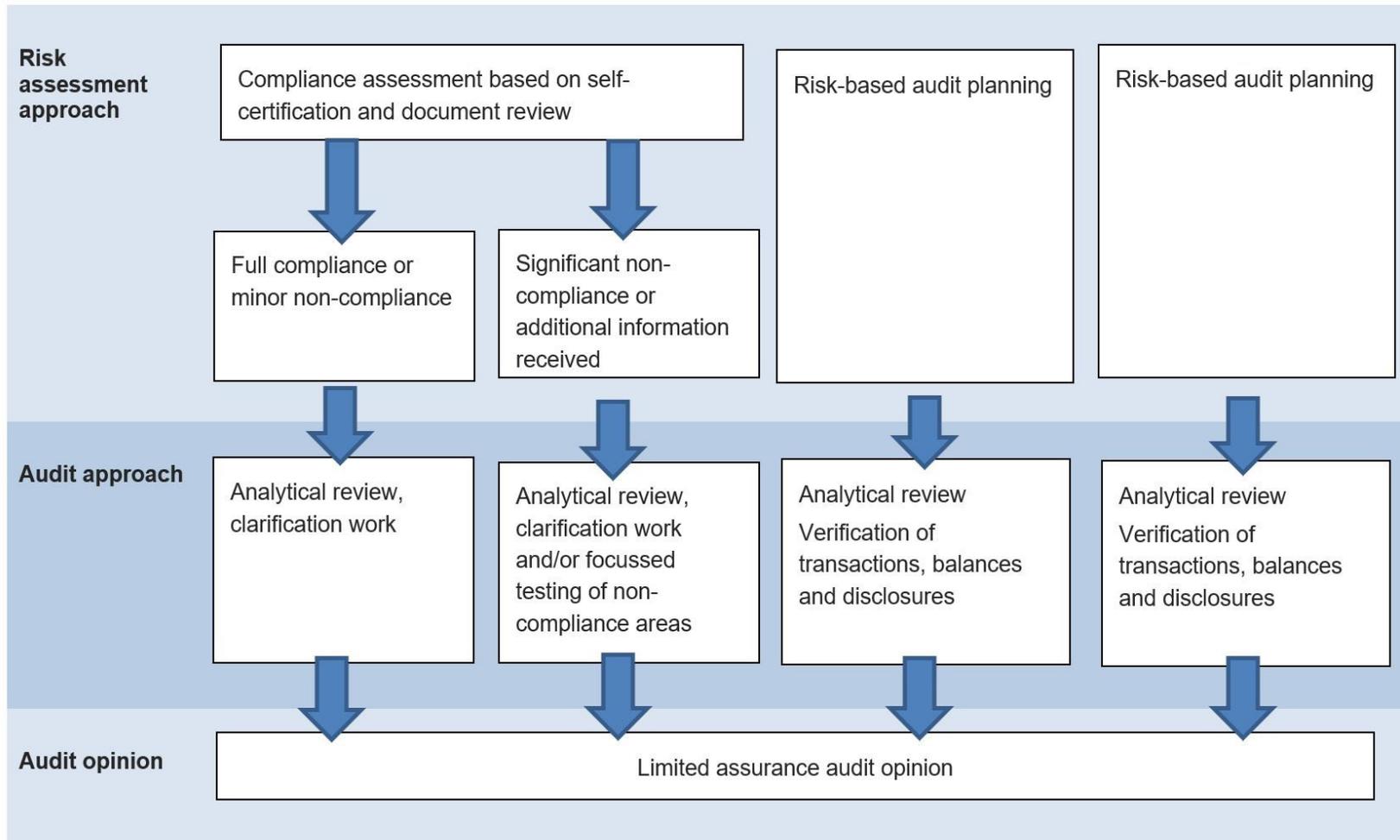
It is not likely to be possible for all transaction-based testing to be completed at council premises. A large number of councils do not in fact have premises and clerks work from home. Audit Wales is currently looking at different models for delivery of all audit work at community and town councils. Transaction-based audits will, however, be carried out at a local level and councils will not be required to send all of their documentation to a central Audit Wales office.

Appendix 4

Three-year cyclical audit arrangements from 2020-21 onwards

Exhibit 4: audit arrangements for community and town councils in Wales from 2020-21







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