

B: DISCHARGING THE CITY COUNCIL'S INTERNAL AUDIT FUNCTION

Introduction

1. This report concerns the decision of Leicester City Council to delegate its Internal Audit function to the County Council. Under Article 11.04 a delegation from another authority requires the approval of the County Council.

Background

2. Section 151 of the Local Government Act 1972, states that every local authority should '*make arrangements for the proper administration of their financial affairs, and shall secure that one of their officers (often referred to as the s151 Officer) has responsibility for the administration of those affairs*'. CIPFA defines that '*proper administration*' should include '*compliance with the statutory requirements for accounting and internal audit*'.
3. The Accounts and Audit Regulations 2015 (the Regulations), require that '*A relevant authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance*'.
4. In the light of reducing budgets for the Internal Audit team at the City Council and the inability to recruit to vacant positions, the City Council's Director of Finance is getting close to being unable to deliver an effective internal audit function through its internal teams
5. The two councils' Directors of Finance (s151 Officers) have been exploring the potential for combining their two internal audit functions into a single team employed and managed by one council, which would then deliver the service to both councils in a more sustainable, efficient and effective manner.

Constitutional and statutory requirements

6. The City Council's Constitution Article 12.04 'Delegation to and from other local authorities' states that '*The City Mayor may delegate executive functions to another local authority or the Executive of another local authority where the law permits*'.
7. On 12 January 2017, the City Mayor decided that with effect from 1 April 2017, or such other subsequent date as is agreed between the City Council and the County Council, to: -
 - a. Delegate the City Council's internal audit function to the County Council in accordance with the provisions of Section 9EA of the Local Government Act 1972, the Local Authorities (Arrangement for the Discharge of Functions) (England) Regulations 2012 and all other enabling powers. This would be for an initial period of three years;

- b. Approve the City Council entering into an Administrative Collaboration Agreement (the Agreement) with the County Council under S9EA of the Local Government Act 1972;
- c. Approve the transfer of City general internal audit staff to the County Council on the terms set out in the Agreement from the Commencement Date, and in accordance with the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE); and
- d. Note that the two council's Section 151 Officers (or their representatives) will oversee the implementation and ongoing monitoring of the Agreement.

Future working arrangements

- 8. The Director of Corporate Resources (through the Director of Finance) will oversee the implementation and ongoing monitoring of the arrangements from the County Council's perspective. The details of the delegation, including responsibilities, liabilities, roles and expectations will be secured through the Agreement which will record that the City Council retains all pre-existing pension and other employment liabilities up to the date of the transfer of staff.
- 9. The County Council's Head of Assurance Services will act in the capacity of Head of Internal Audit Service (HoIAS) for both councils.
- 10. Each council will retain its own internal audit charter, annual plan and annual report including the HoIAS opinion on the organisation's control environment. Oversight of the internal audit function will not change with the HoIAS reporting initially to the respective Directors of Finance and to the Corporate Governance Committee at the County Council, and the Audit and Risk Committee at the City Council.
- 11. Whilst there will need to be a period of stabilisation at the start of the arrangement, the intention is to build an integrated audit team where staff would be directed to undertake audits at both councils and other clients that the County Council team currently provides an internal audit service for.

Risks and Benefits

- 12. There are a number of examples of delegated internal audit functions between local authorities and so it has been possible to plan taking into account of others' experiences. Nevertheless, there are risks applicable to any change project, and this is in effect a merger of two functions which has its own risks.
- 13. Some examples of risks to the success of the project are: -
 - a. Head of Internal Audit Service capacity is over-stretched;
 - b. Staff resistance to change;
 - c. The change could (if managed badly) result in a fall in morale and the loss of staff and/or increased turnover;
 - d. Lead-in time adapting to different systems and working practices; or

- e. Either party chooses to terminate the delegation
14. Predicted benefits include: -
- f. Economies of scale from the employment of a single Head of Internal Audit Service across the two councils;
 - g. Optimising use of resources through a modern collaborative approach;
 - h. Efficient and effective use of audit managers and specialist auditors
 - i. Provision of a critical mass and improved business resilience e.g. enabling the risk of sickness and vacancies to be better managed;
 - j. Opportunities for staff to experience different audits and workplaces;
 - k. Synergy – auditing the same risks with the same auditor and capacity to share best practice across both councils. For example research and development work is undertaken once only and as a result can be done in more depth. Audit programmes and other audit resources will also only be developed once;
 - l. Benefits of adopting common day to day audit reporting and procedural approaches driven by a single Audit Management System;
 - m. Capacity to increase trading; and
 - n. Enabling succession planning, career opportunities and development for staff.
15. The risks and benefits will be actively managed by the Head of Assurance Services.

Resource Implications

16. As well as a £10,000 one off contribution to start-up costs, for an agreed level of service, the City Council has agreed to pay the County Council £280,000 for each of the initial three years of the Agreement. This would release savings to the City Council.
17. The County Council Internal Audit Service is required to make savings in its 2017-18 budget, and the City Council's payment would contribute to the costs of the Head of Internal Audit Service, which is currently fully met by the County Council.
18. A detailed schedule on financial arrangements will support the Agreement.

Decision of the Corporate Governance Committee

19. The Corporate Governance Committee at its meeting on 17th February supported the approach by the City Council to delegate its internal audit function and recommended that Cabinet and full County Council accept the delegation

Consideration by the Cabinet

20. The Cabinet at its meeting on 10th March supported the proposed delegation and recommended the Council to accept the delegation.

(Motion to be moved:-

That the County Council accepts the delegation of the internal audit function from Leicester City Council on the basis outlined in the report.)

17th February 2017

**A. M. Kershaw
Chairman**

Background Papers

Reports on the proposed delegation of the City Council's Internal Audit Function to the:-

- Corporate Governance Committee on 17th February 2017
- Cabinet on 10th March 2017.