



WALES AUDIT OFFICE  
SWYDDFA ARCHWILIO CYMRU

Archwilydd Cyffredinol Cymru  
Auditor General for Wales

# Invitation to Comment: Future Audit Arrangements for Community Councils in Wales 2020-21 Onwards

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Mae'r ddogfen hon hefyd ar gael yn Gymraeg. This document is also available in Welsh.

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# Section 1 – Introduction and overview

## 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.

## What this consultation covers

- 8 This consultation focuses on the audit of community councils in Wales. This includes community, town and city councils and joint committees of such bodies including joint burial boards and committees.
- 9 It sets out, in sections 2 and 3, my findings from a review of the current audit arrangements and proposals for a new audit regime to apply for the audit of the 2020-21 accounts and future years thereafter.

## Section 2 – Current arrangements and the need for change

**While the current audit arrangements are designed to be proportionate to the size of individual councils, they are not adequate to meet my needs as Auditor General as they do not address some significant audit risks**

**The current audit arrangements follow a limited assurance approach to reflect the complexity and risk of the sector**

- 10 The Audit Commission first introduced the limited assurance regime for 2001-02. I inherited this approach in 2005. The current revised arrangements were introduced in 2015-16. The audit regime is applied to all community councils in Wales.
- 11 The regime is designed specifically to minimise the audit requirement upon, and cost to, these small public bodies. There are two levels of audit applied dependent upon the size of the council as measured by its income and expenditure.
- 12 For councils where neither income nor expenditure exceeds £2.5 million, the audits are based on the submission by the body to the auditor of an annual return that is subject to a desk review. The annual return contains a simple form of accounting statements and an annual governance statement. The audit report provides a limited level of assurance to the body commensurate with the amount of work undertaken.
- 13 The audit approach includes three key elements:
  - a compliance test against the requirements of the annual return;
  - a high-level analytical review of the financial and other information provided to the auditor; and
  - a review of the two-part annual governance statement provided by the body, the supporting report from its internal auditor and any further documentation requested by the external auditor.
- 14 Auditors are required to be mindful of the size of the council when setting their expectations as to the quality and quantity of information to be provided for audit.
- 15 However, those bodies with annual income or expenditure over £2.5 million, prepare accounting statements that reflect their larger size and complexity. Auditors are required to carry out a programme of transaction-based testing as part of their audit approach to reflect the higher risk to public funds.
- 16 In addition, further audit work is required where:
  - auditors identify issues when undertaking their normal audit work;
  - matters are brought to the auditor's attention as a result of media coverage or correspondence received in relation to specific councils; or

- local electors ask questions or make objections to the accounts at audit.

Such additional work is focussed on addressing the specific issues identified.

- 17 The audit approach is designed to discharge my statutory responsibilities while providing a reasonable level of assurance to readers of the accounts. The extent of audit work undertaken is designed to be proportionate to the sums of public money managed by individual councils and the risk to the public purse.
- 18 To achieve this, the audit focuses on areas where councils have specific statutory responsibilities linked to financial management and governance. Councils receive a 'qualified' audit opinion when they do not meet those statutory responsibilities.
- 19 **Appendix 1** provides an overview of the current audit arrangements.

## Since 2011-12, I have identified significant and systemic failings in financial management and governance across the sector

- 20 In 2008, the Auditor General published a report, Good Governance – Good Practice, highlighting common governance failures that had been identified by auditors. A Good Practice Exchange guide was also issued to help councils address the most common shortcomings.
- 21 Following the 2011-12 audits, the Auditor General published the first of a series of annual reports on financial management and governance at community councils. The report highlighted systemic weaknesses across the sector and aimed to support improvement by highlighting these issues.
- 22 Further reports in the subsequent years highlighted similar findings; 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.
- 23 These reports are published on the Wales Audit Office website. Links to the reports can be found in **Appendix 2**.

## Community councils have not addressed these risks despite changes to the audit regime in 2015, and the identification of longstanding issues at individual councils has resulted in the publication of 18 public interest reports in 2018 and 2019

- 24 In response to significant issues identified in previous years, I enhanced the limited assurance audit regime for community councils in 2015.
- 25 The 2015 arrangements introduced a five-year programme of audit work that addressed the most significant failings identified by auditors between 2001 and 2014. Insofar as was possible, I also committed to informing councils in advance of the year of audit, of those areas of focus to enable them to review their extant arrangements and to introduce any improvements needed. The advance

notifications have been published in the annual financial management and governance reports.

- 26 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 2](#).
- 27 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
- 28 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 would have been needed for early identification of emerging problems.
- 29 The type of issues reported in these public interest reports are generally not identified by internal auditors. In several cases, reference is made in the reports to the poor standard of internal audit work.

#### Exhibit 1: question 1

##### Question 1

- Q1 I believe that the current community council audit arrangements can lead to identification too late of the type of audit issues highlighted in recent Wales Audit Office reports in the public interest. Do you agree?

## Section 3 – Proposals for a new system of audit

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

In developing my proposals for future audit arrangements consideration has been given to design principles specific for the sector and the principles of public audit

### Design principles

- 30 In proposing a new framework for community council audits in Wales, I have followed a set of design principles:
- Legality – any audit arrangements must ensure that both councils and the Auditor General are able to meet their respective statutory responsibilities annually
  - Proportionality – ensuring that the scope provides a proportionate approach for smaller bodies
  - Transparency – ensuring that the results of audit work are easily accessible to the public, helping local people to hold local public bodies to account for spending decisions
  - Manageable audit fees – ensuring that the cost of audit is manageable for all councils
  - Proper standards of auditing – ensuring that there is effective and transparent public audit, and conformity to the principles of public audit
- 31 These principles are not wholly independent of one another. For instance, there is a clear relationship between the quality and scope of the audit and the level of audit fees. I wish to find the right balance to ensure an effective, robust, quality audit for community councils, while keeping fees as low as possible. Legislation prohibits me from charging more than the cost of the audit.

### Public audit principles

- 32 I have also had regard to the principles of local public audit. These are:
- independence of public sector auditors from the organisations being audited. Auditors must be independent, to avoid improper influence and allow work to

be carried out objectively and without hindrance. Independence encompasses the financial relationship between auditor and audited bodies, discretion in the amount of work necessary, the ability to follow up the implementation of recommendations, and the ability to have access to information necessary for audit work.

- the wide scope of public audit – public audit involves more than an opinion on accounts. It also covers issues such as regularity, propriety and value for money. In this way, it helps to contribute to the corporate governance arrangements of public bodies.
- the ability of public auditors to make the results of their audits available to the public and other stakeholders. For this, there must be appropriate reporting arrangements, under which auditors report the results of their work both to the audited bodies and to the public.
- as public service delivery models change, public sector audit develops so it is relevant to the needs of those holding public bodies to account, the public and other stakeholders. Being responsive to changing environments and emerging risks and communicating in a timely and effective way show that audit continues to be a credible source of independent and objective insight and guidance to support beneficial change in the public sector.

#### Exhibit 2: questions 2 and 3

##### Questions 2 and 3

- Q2 Have I identified the correct design principles for the proposed community council audit arrangements?
- Q3 Do the proposed community council audit arrangements meet the design principles I have identified?

**The proposed audit regime incorporates a three-year audit programme including transaction-based audit procedures on a cyclical basis to reflect the risk to the public purse and enhance the assurance provided by the audit whilst managing overall cost**

- 33 The current limited assurance audit arrangement involves a desk-based review of a council's annual return and limited supporting documentation. As set out above, this is insufficient to identify significant issues on a timely basis.
- 34 The proposed new arrangements will involve an element of transaction-based audit testing. A transaction-based approach to the audit would involve auditors examining an individual council's accounts and tracing the accounts 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 provided at present.

- 35 I am currently testing this transaction-based approach at a number of councils including those where public interest reports have been published. This approach is leading to the identification of some significant failings by councils. Analysis of the issues identified in the recent public interest reports confirms that the issues reported have generally existed for a number of years.
- 36 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.
- 37 In order to ensure the arrangement, as a whole, is proportionate, for councils with income and expenditure less than £2.5 million, transaction-based audits will be interspersed with more limited audit procedures on a cyclical basis. A three-year cycle will allow for identification of issues within a relatively short timescale. Councils would also be aware that they would be subject to more detailed scrutiny on a regular basis.
- 38 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.
- 39 I propose that the future audit regime for these small bodies incorporates a three-year cycle of two limited procedure audits followed by a transaction-based audit. The introduction of the transaction-based audits will be staggered across the first three-years of the new arrangements.
- 40 A summary of the audit approach is provided in [Appendix 3](#).
- 41 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, eg 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

### Exhibit 3: questions 4, 5 and 6

#### Questions 4, 5 and 6

- Q4 Do you agree that the proposed community council audit arrangements should incorporate detailed testing of transactions?.
- Q5 Are there any alternative procedures that should be considered for inclusion in the proposed community council audit arrangements?
- Q6 Do you agree that the proposed community council audit arrangements should be a cyclical programme over a three-year period?

### In addition to reporting the outcomes of the annual audits to individual councils, additional assurance and analysis will be provided by the publication of national reports and good practice guidance

- 42 As set out in [Appendix 2](#), the Auditor General publishes an annual report summarising the outcome of all audit work undertaken across the sector. The reports also provide further analysis and commentary on the financial position of the sector and explain where there is scope to improve financial management and governance arrangements across the sector as a whole.
- 43 I propose to continue to publish these reports annually to highlight areas where councils can learn from the experiences of others.
- 44 The national study on internal audit arrangements in the sector was undertaken to address a key risk area identified during the course of my regular audit work. The review was undertaken as a national study as this was the most efficient means of identifying the key areas for development for the sector rather than undertaking a review at each council. I will continue to seek to identify areas where I can address issues through a national study in order to maximise the efficiency of the use of my resources and to manage the cost of audit to individual councils. Areas that may be considered for a national study include the sector's approach to the Well-being of Future Generations Act and the use made of a general power of competence once that is available.
- 45 In recent years, I have hosted Good Practice Exchange webinars on matters related to the sector. I will continue to support improvement within the sector by identifying areas where good practice can be shared across all councils.

#### Exhibit 4: questions 7 and 8

##### Questions 7 and 8

- Q7 Do you agree that the publication of annual reports and occasional national studies would be of benefit to the sector?
- Q8 Are there any specific areas of concern you consider it would be helpful for the Auditor General to undertake a national study on, or to provide a Good Practice Exchange event (such as a webinar)?

### The overall impact on audit fees is expected to be modest, although it is likely that fees will increase in the years in which transaction-based audits are carried out

- 46 Audit fees are charged to community and town councils in accordance with the Wales Audit Office Fee Scheme. This scheme is updated annually and approved by the Finance Committee of the National Assembly for Wales.
- 47 The Wales Audit Office does not generate profits on fees. Legislation requires that the fees I charge may not exceed the full cost of exercising the function to which the fee relates. My fee rates are set at a level to recover that full cost.
- 48 My proposals mean that for two years out of three, the audit work undertaken will be similar to the work undertaken under the current audit arrangements. Therefore, I expect that audit fees for these two years will be broadly comparable to the current audit fees charged to councils.
- 49 In the third year, the audit procedures will require more audit time and it is likely that this will mean an increased audit fee for one year in three. The impact of the proposals is currently being modelled but it is expected that there would be a modest increase to overall audit fees over the three-year cycle. Under the current legislation I would be unable to smooth the fees charged to individual councils over the three-year cycle.
- 50 In 2019, the Wales Audit Office decided that all audit work on community council audits would be carried out directly by staff of the Wales Audit Office. This arrangement will apply from the audit of the 2020-21 accounts onwards.
- 51 The Wales Audit Office is currently planning for the handover of audits from BDO and Grant Thornton and identification of key contacts for councils across Wales. We will notify councils of these key contacts in due course.
- 52 The necessary audit tools are also currently under development. The Wales Audit Office aims to develop tools that will make the audit process as efficient as possible in order to manage the impact on audit fees.
- 53 Councils can also play their part in managing fees by reviewing the standard of their documentation and record keeping – the better prepared the council is in relation to relevant documentation and record keeping, the smoother and cheaper the audit process will be.

- 54 The National Assembly is currently considering amendments to the Public Audit (Wales) Act that may impact on my fee setting arrangements. It is not, therefore, possible to propose an indicative range of audit fees at present. I will provide further information when the legislative position is clearer.

## Section 4 – Consultation questions and next steps

### I am running a six-week consultation with the sector (and the public) and welcome responses from all interested parties via an online survey

#### Timing and how to get involved

- 55 This consultation will run for six weeks from 6 February to 19 March 2020. Following this period, I will consider the responses I receive and will publish a summary of the responses and final details of the audit arrangements.

#### Who am I consulting?

- 56 Anyone is welcome to respond but I would particularly welcome comments from community councils and any other relevant bodies or individuals. This document is available on the Wales Audit Office website ([www.audit.wales](http://www.audit.wales)) and I will be drawing it to the attention of all community councils and their joint committees, sector representative bodies and the Welsh Government.
- 57 It is open to all to make representations on the proposed new system of community council audit and all submissions will be considered.

#### How to respond

- 58 To assist interested parties in responding to the consultation, I have set up an online survey. [The survey can be found here.](#)
- 59 If you are unable to access the survey or have not received an email invitation, please contact [CommunityCouncilConsultation@audit.wales](mailto:CommunityCouncilConsultation@audit.wales). We will assist you further in providing your response.
- 60 Please ensure that I receive your response by 19 March 2020.

#### Publication of responses – confidentiality and data protection

- 61 Information provided in response to this consultation, including personal information, may be published, or disclosed in accordance with the access to information regimes (these are primarily the Freedom of Information Act 2000, the General Data Protection Regulation (GDPR), Data Protection Act 2018 and the Environmental Information Regulations 2004).
- 62 If you want any information you provide to be treated as confidential you should be aware that under the Freedom of Information Act, there is a statutory Code of Practice with which public authorities must comply, and which deals, amongst other things, with obligations of confidence. In view of this, it would be helpful if you

could explain to us why you regard any information you have provided as confidential.

- 63 If I receive a request for disclosure of the information, I will take full account of your explanation, but I cannot give any assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on the Wales Audit Office.
- 64 The Wales Audit Office will process your personal data in accordance with the GDPR and the Data Protection Act 2018, and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

## I would like to hear your thoughts on eight questions about the audit arrangements

- 65 I would like to hear your views on the following questions. Further background information is included in the remainder of this Invitation to Comment.

### Exhibit 5: consultation questions

Consultation questions	
<b>Current arrangements and the need for change</b>	
Q1	I believe that the current community council audit arrangements can lead to identification too late of the type of audit issues highlighted in recent Wales Audit Office reports in the public interest. Do you agree?
<b>Proposals for a new system of audit</b>	
Q2	Have I identified the correct design principles for the proposed community council audit arrangements?
Q3	Do the proposed community council audit arrangements meet the design principles I have identified?
Q4	Do you agree that the proposed community council audit arrangements should incorporate detailed testing of transactions?
Q5	Are there any alternative procedures that should be considered for inclusion in the proposed community council audit arrangements?
Q6	Do you agree that the proposed community council audit arrangements should be a cyclical programme over a three-year period?
Q7	Do you agree that the publication of annual reports and occasional national studies would be of benefit to the sector?
Q8	Are there any specific areas of concern you consider it would be helpful for the Auditor General to undertake a national study on, or to provide a Good Practice Exchange event (such as a webinar)?

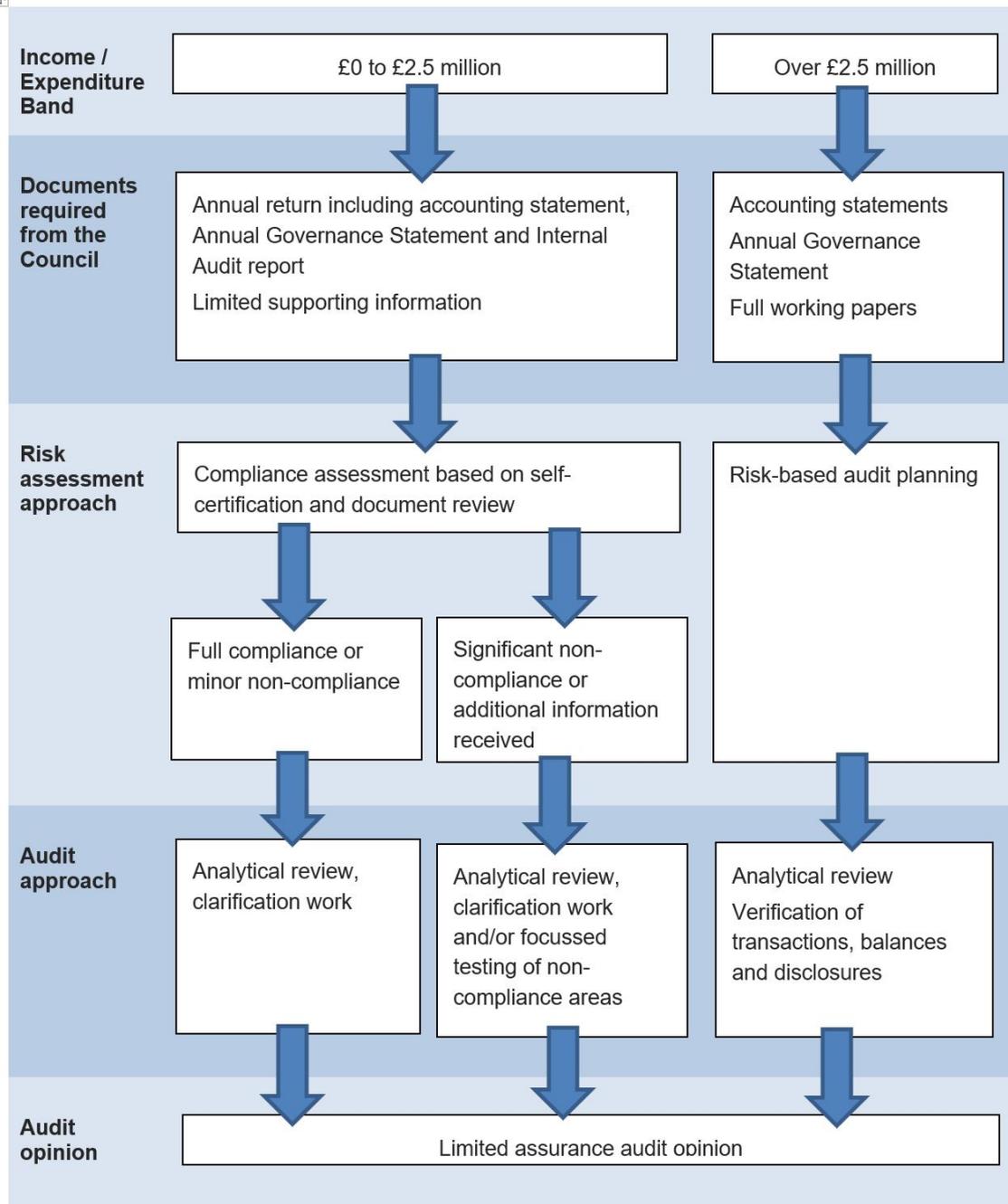
## After considering the consultation responses, I will publish the final arrangements and host a Good Practice Exchange webinar in July 2020 to explain those arrangements

- 66 I will consider all responses received during March 2020 and decide on the final audit arrangements in the early spring.
- 67 In addition to informing all councils of the final arrangements, I will host a Good Practice Exchange webinar in early July 2020.
- 68 At this webinar, I will explain the new arrangements and explain how councils can prepare for their introduction.
- 69 The webinar will commence at 7 pm and I invite interested parties to submit questions beforehand or during the webinar where they wish to receive more detailed explanation. Councils are invited to arrange a council meeting on 7 July so that members can collectively join the webinar.
- 70 Further details will be sent to councils nearer the date.
- 71 In March 2021, I plan to hold a further event to assist councils to make preparations for the first-time submission of their accounts for audit under the new arrangements.

# Appendix 1

## Current audit arrangements

Exhibit 6: current audit arrangements



# Appendix 2

## Reports issued by the Auditor General for Wales

Exhibit 7: Auditor General's annual reports

<b>Annual financial management and governance reports</b>
<a href="#">Financial Management and Governance – Town and Community Councils 2017-18</a>
<a href="#">Internal Audit Arrangements at Town and Community Councils in Wales</a>
<a href="#">Financial Management and Governance in Local Councils 2016-17</a>
<a href="#">Financial Management and Governance in Community Councils 2015-16</a>
<a href="#">Financial Management and Governance in Local Councils 2014-15</a>

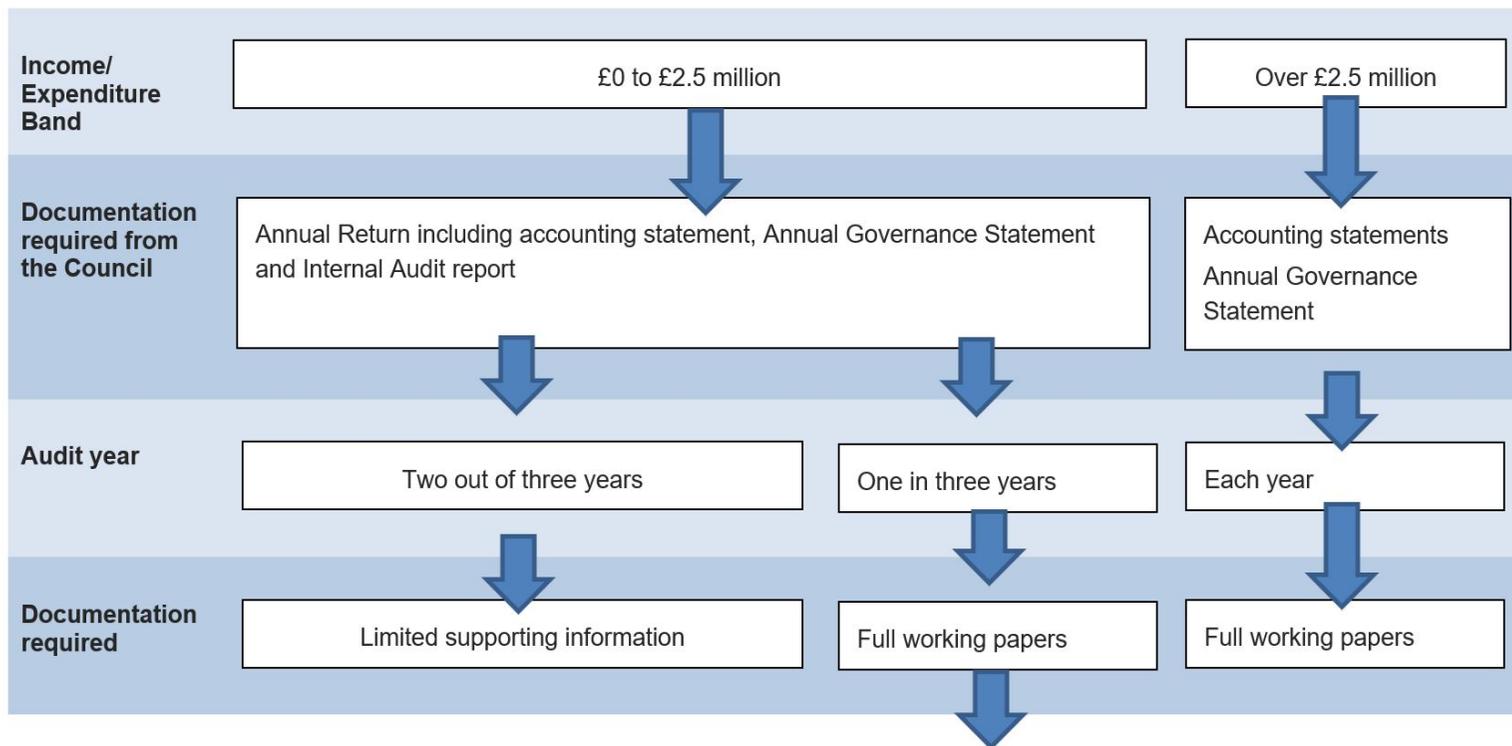
Exhibit 8: reports in the public interest

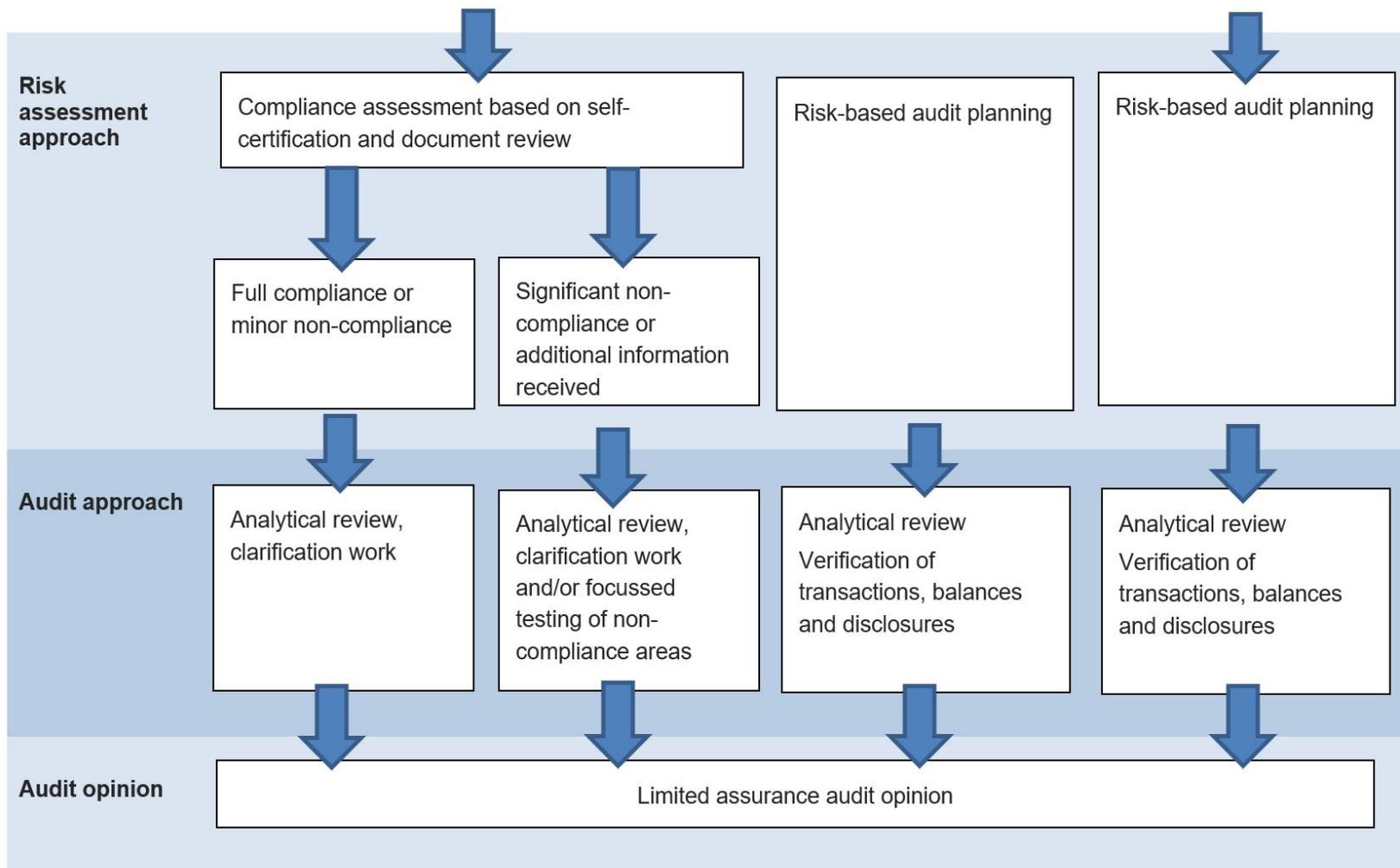
<b>Public interest reports issued in 2018</b>	<b>Public interest reports issued in 2019</b>
<a href="#">Whitford Community Council</a>	<a href="#">Bodorgan Community Council</a>
<a href="#">Cadfarch Community Council</a>	<a href="#">Buckley Town Council</a>
<a href="#">Tirymynach Community Council</a>	<a href="#">Connah's Quay Town Council</a>
<a href="#">Llanwnnen Community Council</a>	<a href="#">Cynwyd Community Council</a>
<a href="#">Penally Community Council</a>	<a href="#">Glynneath Town Council</a>
<a href="#">Glantymyn Community Council</a>	<a href="#">Llanfairpwll Community Council</a>
<a href="#">Llanbrynmair Community Council</a>	<a href="#">Llanfrothen Community Council</a>
	<a href="#">Llangristiolus and Cerrigceinwen Community Council</a>
	<a href="#">Maenclochog Community Council</a>
	<a href="#">Mumbles Community Council</a>
	<a href="#">Penmaenmawr Town Council</a>
	<a href="#">Rhosyr Community Council</a>

# Appendix 3

## Proposed audit arrangements from 2020-21 onwards

Exhibit 9: proposed audit arrangements





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