



THE 2003 GENERAL REPORT ON THE FINANCIAL AUDIT WORK OF THE AUDITOR GENERAL FOR WALES

Report by the National Audit Office Wales on behalf of the Auditor General for Wales

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Report by the Auditor General for Wales,
presented to the National Assembly for
Wales on 30 July 2003

This report has been prepared for presentation to the National Assembly for Wales under the Government of Wales Act 1998.

John Bourn
Auditor General for Wales

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30 July 2003

The Auditor General for Wales is totally independent of the National Assembly. He certifies the accounts of the Assembly and its associated sponsored public bodies; and he has statutory authority to report to the Assembly on the economy, efficiency and effectiveness with which the Assembly and its sponsored public bodies have used their resources in discharging their functions.

This report was prepared for the Auditor General for Wales by the National Audit Office Wales.

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FOREWORD BY THE AUDITOR GENERAL FOR WALES

I am delighted to present this General Report to the National Assembly for Wales.

My financial audit work at the National Assembly for Wales and its related public bodies enables me to provide independent assurance that the annual financial statements are properly prepared and that income and expenditure has been applied for the purposes intended by the relevant United Kingdom statutes.

This report summarises the results of financial audit work undertaken on my behalf by the National Audit Office Wales in respect of the 2001-02 accounts. It also provides an update to 31 March 2003 on other important areas such as my advice and assistance to the Welsh Assembly Government concerning its restructuring of the NHS in Wales, issues arising from the correspondence I have received from Assembly Members and the general public, and the audit of European-funded projects.

Overall, I consider that standards of financial management and probity remain high in Wales. However, in this report, I comment on the importance of sound and prudent financial management and set out several areas where improvements need to be made. For example, I have drawn attention to the decline during 2001-02 of the Welsh central government sector's performance in paying its suppliers promptly - a failing that can cause considerable cash-flow difficulties for small businesses. I have also commented upon the need to improve the procedures for the procurement of goods and services.

I also warmly welcome the recently announced potential changes to the public audit arrangements in Wales that would enable the Auditor General for Wales to head a single audit body for Wales. This is an exciting development for the public sector in Wales that would greatly enhance my ability to undertake examinations of a 'crosscutting' nature.

I aim to continue to provide an efficient and effective audit service to my client bodies and other stakeholders and to provide independent assurance and comfort to the National Assembly and people of Wales.

John Bourn

30 July 2003

PART 1 Introduction

1.1 This report to the National Assembly for Wales summarises the results of my examination and certification of the 2001-02 accounts, the last of which I certified in January 2003. The report also summarises the results of my other financial audit work through to 31 March 2003.

Coverage of this Report

1.2 In this annual report I:

- ▶ summarise the results, conclusions and reports from my audits in Wales for the 2001-02 year of account (Part 2);
- ▶ set out examples of the added value of my work to my clients and the key themes that arose from it (Part 3);
- ▶ describe the other services that I provide to my stakeholders, for example in responding to issues raised in correspondence from Assembly Members, MPs and the public (Part 4);
- ▶ set out the results of my continuing audit work on the European Structural Funds (Part 5);
- ▶ comment on instances of poor procurement practice in 2001-02 (Part 6); and
- ▶ provide a forward look at developments in accountancy and audit within the Welsh central government sector (Part 7).

1.3 This report does not deal with the value for money (VFM) audit work of the National Audit Office Wales, which supports the production of my published VFM reports. **Appendix A** lists the published VFM reports on which work was undertaken by the National Audit Office Wales during 2001-02; they are available on the internet at www.agw.gov.uk. These reports are considered separately by the Assembly's Audit Committee and records of these meetings are available on the Assembly's website at www.wales.gov.uk.

Auditor General for Wales

1.4 As Auditor General for Wales, I am required by statute to examine and certify the annual accounts of the National Assembly for Wales, its sponsored public bodies and certain other public bodies, and to report my audit opinions to the Assembly.

1.5 I conduct my financial audits in accordance with Auditing Standards issued by the Auditing Practices Board. In common with private sector practice, these auditing standards require me to:

- ▶ undertake procedures designed to obtain sufficient, reliable and appropriate audit evidence to determine with reasonable confidence whether the financial statements are free of material misstatement; and
- ▶ assess the overall presentation of the financial statements in order to ascertain whether they have been prepared in accordance with Accounting Standards and the relevant Accounts Directions.

1.6 An additional audit requirement, unique to public bodies, is that of **regularity**. This means that the income and expenditure of each audited body must be applied only to the purposes intended by Parliament and/or the National Assembly for Wales and must comply with all relevant governing authorities and statutes.

1.7 I therefore design my audit examinations to satisfy myself that, in all material respects, money provided to and by the National Assembly for Wales has been used only for the purposes intended. In carrying out this work, I also have regard for the **propriety** with which public funds have been handled and the manner in which public business has been conducted.

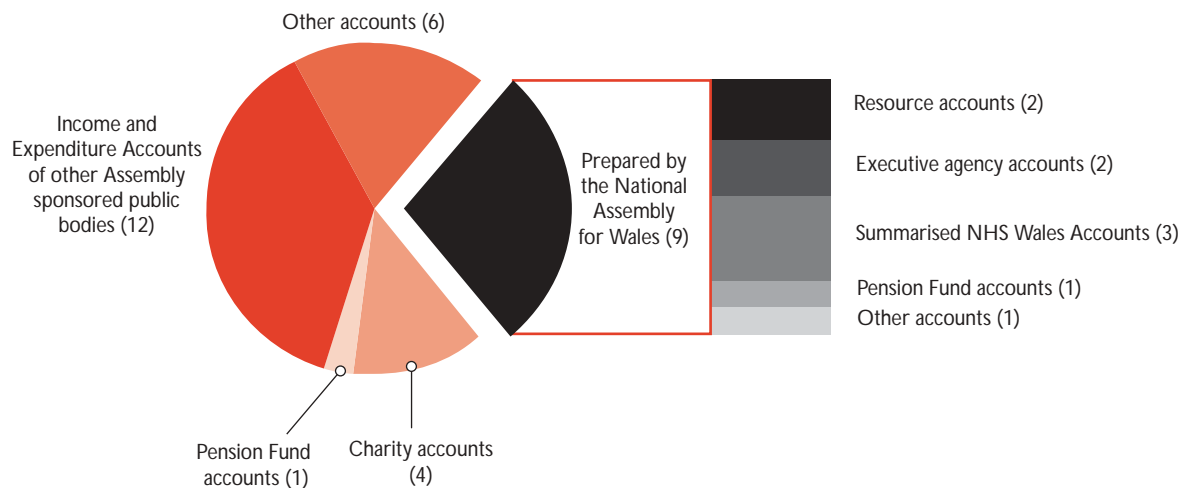
National Audit Office Wales

1.8 The National Audit Office Wales undertakes under my direction the detailed financial audit work necessary to support my duties and statutory responsibilities. For the 2001-02 year of account, they audited 32 accounts which reported the spending programmes financed by the Welsh block budget of some £8.9 billion.

1.9 The accounts were prepared by the Assembly and its sponsored public bodies in compliance with directions issued, as appropriate, by both the Assembly and Treasury. The various organisations differ greatly in nature, size and complexity and operate an array of financial procedures and accounting systems. **Figure 1 overleaf** illustrates the variety and numbers of accounts audited for 2001-02 (a full listing is set out in **Appendix B** to this Report).

Figure 1

Accounts audited by the Auditor General for Wales 2001-02



Source: National Audit Office Wales

Role of the Accounting Officer

1.10 Each body that I audit has a designated 'Accounting Officer' - usually the Permanent Secretary or Chief Executive. This role includes responsibility for financial management and control within the organisation as set out in the Statement of Accounting Officer's Responsibilities, which is published alongside each annual account.

1.11 These responsibilities include:

- ▶ the keeping of proper records and the preparation of financial statements which comply with statutory and other disclosure requirements;
- ▶ the propriety and regularity of the public finances for which he or she is responsible; and
- ▶ reviewing the effectiveness of the organisation's systems and controls.

1.12 The Accounting Officer is supported in executing these responsibilities by a body's Corporate Governance or Audit Committee and by the senior management team, together with advice from the internal auditors and the National Audit Office Wales.

1.13 Each Accounting Officer can be summoned by the Assembly's Audit Committee to give oral or written evidence on reports that I may produce on the accounts of the bodies for which they are responsible. The Committee, which is chaired by an Assembly Member belonging to an opposition party, considers this evidence and then produces its own reports containing recommendations to which the Welsh Assembly Government is required to respond within 30 working days.

1.14 Taken together, these audit and reporting arrangements provide a significant level of public accountability and assurance to the people of Wales that public money is being spent wisely and in accordance with the intentions of the Assembly. In the remaining parts of this report, I set out the key findings and results of my financial audit work in respect of the 2001-02 financial year.

Introduction

- 2.1 This part of the report summarises the results and conclusions from my financial audit work for the 2001-02 year of account. Specifically, it sets out:
- ▶ the results of my examinations on each of the accounts that I audited in 2001-02; and
 - ▶ summaries of the substantive reports that I issued on the accounts of the new National Council for Education and Training for Wales, the summarised account of the Welsh health authorities and on the financial health of NHS Wales.
- 2.2 In general, standards of financial control in client bodies throughout Wales remained good. During the course of its work, and as in previous years, the National Audit Office Wales was also able to make a wide range of recommendations to the Accounting Officers and senior management of client bodies for improvements to systems of control, compliance with the regulatory framework and accounting processes.

Reporting the results of audit examinations

- 2.3 I report the results of my financial audit work as follows:
- ▶ **Audit Certificates on the financial statements**, giving a clear expression of my audit opinion;
 - ▶ **Published reports on the account**, bringing to the Assembly's attention matters that have a direct or indirect effect on public expenditure. (I always report on an account when I qualify my audit opinion, and I may also report matters without qualifying my opinion if I believe them to be of significant interest to Assembly Members); and
 - ▶ **Unpublished reports to the audited client body's management**, drawing attention to areas where improvements to systems and procedures may be made and providing constructive recommendations and advice (addressed in Part 3 of this report).

Audit Certificates on the financial statements

- 2.4 I report my opinion as to whether the financial statements give a **true and fair view** and have been **properly prepared** in accordance with the relevant statute and Treasury directions made thereunder. In preparing accounts there is a need for judgement in determining accounting estimates and policies, and the uncertainties inherent in financial estimates. In assessing such judgements, the auditor considers the relative importance of each issue arising from the audit in the context of the whole account. A matter is regarded as material if its misstatement or omission would reasonably influence the users of the financial statements in drawing conclusions from the information contained within them.
- 2.5 I also report my opinion as to whether the transactions contained within the financial statements are regular; that is, that in all material respects they have been undertaken in accordance with primary and secondary legislation, other regulations issued by Ministers, and with Parliamentary and Treasury authority.

My audit opinions in 2001-02

- 2.6 As Auditor General for Wales, I gave an unqualified audit opinion on all but two of the 32 Welsh accounts that I certified in respect of the 2001-02 financial year. I qualified my opinion on the first accounts of the new National Council for Education and Training for Wales (the National Council) and also on the summarised account of the health authorities in Wales. My reports on these accounts explained the reasons for my qualified opinions, and summaries of these reports are set out below.

Reports on accounts

- 2.7 For the 2001-02 financial year, I made substantive published reports in respect of the following:
- ▶ the National Council;
 - ▶ the Summarised Account of the Health Authorities in Wales; and
 - ▶ Financial Health of the NHS in Wales.

National Council for Education and Training for Wales

- 2.8 The National Council was established on 10 October 2000, in accordance with Section 30 of the Learning and Skills Act 2000. On 1 April 2001 it acquired the functions of the former Further Education Funding Council for Wales and also assumed control of the four Welsh Training and Enterprise Councils (TECs) and the Council of Welsh TECs. The National Council's first set of published accounts covered the 17-month period from the date of its establishment to 31 March 2002.
- 2.9 I qualified my audit opinion on these accounts because of expenditure by the National Council totalling some £2.2 million, incurred in respect of 14 contracts, for which the requisite approval of the National Assembly for Wales was not obtained and which was therefore irregular. My report considered the circumstances in which this irregular expenditure had been incurred, and the corrective action subsequently taken by the National Council and the Assembly.
- 2.10 In my report on the accounts, I also noted a number of weaknesses that were apparent in the organisational structure of the National Council in its early months, and commented on the failure of the National Council to provide the National Audit Office with complete draft accounts for audit until shortly before the 31 August statutory deadline. I also expressed concerns about the use of confidentiality clauses in the negotiation of departure settlements agreed by the National Council with over 100 staff. This practice ran counter to recommendations made previously by the Audit Committee of the National Assembly for Wales that had been accepted by the Welsh Assembly Government.

Summarised Account of Health Authorities in Wales

- 2.11 In carrying out my audit of the summarised accounts of the health authorities and trusts in Wales I have regard to work undertaken by the auditors of those bodies, which are appointed by the Audit Commission (the "appointed auditors"). In 2001-02, for the second successive year, I qualified the regularity element of my audit opinion on the summarised account of the health authorities in Wales in respect of a potential shortfall in prescription income. This qualification mirrored the qualifications given by the appointed auditors to the 2001-02 accounts of four out of five health authorities in Wales.
- 2.12 In my report I also noted that the appointed auditors of the Dental Practices Board had qualified their regularity opinion on the Board's 2001-02 financial statements on the basis that they contained a material amount of inappropriate expenditure, including administrative error, misunderstanding of regulations, inappropriate or poor quality work and deliberate theft. For 2001-02, the Board had estimated that, for England and Wales combined, approximately £74.6 million could have been paid inappropriately, of which almost half was in respect of claims for exemption from patient charges.

Financial health of the NHS in Wales

- 2.13 My annual report for 2002 on the finances of NHS Wales was published on 22 May 2003. In that report, I commented on issues of financial performance in 2001-02 and also considered other key challenges impacting on delivery of service, including restructuring and progress in tackling fraud.

Financial performance of NHS Wales

- 2.14 There was a significant deterioration in the financial health of NHS Wales during 2001-02. The overall result for the year was a total net deficit of £16 million, compared to an overall surplus in 2000-01 of £23.7 million. The deficit for 2001-02 was net of £11.2 million strategic assistance funding received by the trusts in Wales from the National Assembly for Wales. Without this assistance the overall deficit for the year would have been £27.2 million

2.15 For the 2002-03 financial year, the unaudited out-turn figures for NHS Wales indicate a deficit of some £7.7 million. Factors contributing to this deficit, which excludes the agreed write off of £23.7 million of loans to Dyfed Powys Health Authority, included the increased premiums payable to the Welsh Risk Pool and increases in the cost of primary care drugs.

Challenges facing NHS Wales

2.16 The National Health Service Reform and Health Care Professions Act 2002 provided for the abolition of the five health authorities in Wales on 31 March 2003 and for the setting up of 22 Local Health Boards. On 1 April 2003, the Assembly also established Health Commission Wales (Specialist Services), an executive agency that will provide a strengthened function to commission tertiary care and other highly specialised acute services throughout Wales.

2.17 In my report I noted the risks associated with this significant restructuring and commented specifically on my review of the transitional and running cost budgets of the new NHS structures, which I had undertaken at the request of the Director of NHS Wales. I provide further information on this review at paragraph 4.8 of this report.

Progress in tackling NHS Fraud

2.18 During the last year, the Welsh Assembly Government has continued to work with the NHS Counter Fraud Service and the Audit Commission to establish an effective structure to counter fraud in Wales. In my report I noted the results of this work, in particular the conclusions of a measurement study undertaken by the NHS Counter Fraud Service which estimated the level of patient prescription fraud at £8 million for 2001-02, a reduction of £7 million annually from the £15 million estimated in my report 'Maximising Income from Prescription Charges', published in November 2000. I also noted the establishment of the Post Payment Verification Unit at Velindre NHS Trust to verify patient prescription payment exemption claims, and the recovery of £244,000 as a result of the work of the NHS Counter Fraud Service and Local Counter Fraud Specialists. By 31 May 2003, total recoveries had risen to £265,000.

Introduction

3.1 In this part of my report, I describe the various audit services provided to my clients arising from the annual financial audit work undertaken on my behalf by the National Audit Office Wales and highlight the key issues arising from this work on the 2001-02 accounts.

Reporting to client management

3.2 When performing an audit of a body's annual financial statements, the National Audit Office Wales assesses the adequacy of a body's accounting systems and records to the extent necessary to form an opinion on the accounts. In undertaking this work, the National Audit Office Wales is able to offer constructive **advice to management** where it identifies weaknesses in the design, operation or application of these systems, or potential improvements that could be made to the effectiveness or efficiency of the client's operations.

Management Letters

3.3 Advice provided during the course of an audit is often given orally. However, the more significant issues are raised formally at the end of the audit in the form of a **management letter** addressed to the client's senior management. Each of the observations raised by the National Audit Office Wales is agreed for factual accuracy by client management, who provide a formal substantive response to each point raised, together with a target date for implementation of each of the recommendations made. This enables me to monitor progress. The National Audit Office Wales recognises the need for controls to operate cost-effectively, and aims to produce practical recommendations that genuinely aid clients in their attempts to operate their businesses efficiently and effectively without creating unnecessary bureaucracy.

'Additional Assurance' reviews

3.4 In 2001-02, the National Audit Office Wales continued, at the request of the Assembly Accounting Officer, to undertake **'additional assurance' reviews** at Assembly Sponsored Public Bodies. The intention of these reviews is to provide both the audited body's management and Assembly officials with assurance over and above that obtained from the standard external audit of the

accounts themselves. In many cases, this work can also add value by recommending improvements to systems, controls and operating procedures.

3.5 Whilst the precise scope of each review is tailored to the individual circumstances of the audited body, there are certain core elements to each review. These include checks designed to identify whether:

- ▶ the systems of control had operated effectively;
- ▶ operations were in compliance with the client's Financial Memorandum and Management Statement;
- ▶ there were any occasions when members or staff had fallen short of the high standards of financial integrity expected of those responsible for the management of public funds; and
- ▶ there was any extravagant or wasteful expenditure in the period.

Findings

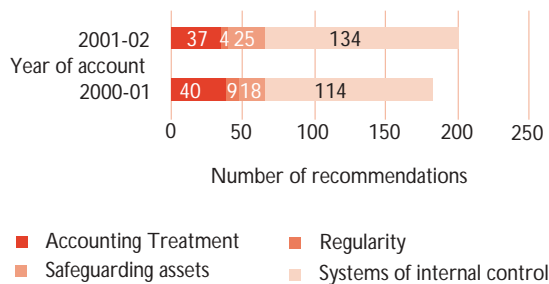
Recommendations made to client management

3.6 The overall results of my work in financial audit indicate that, in general, the standards of financial control in audited client bodies throughout Wales remained good during 2001-02. However, the National Audit Office Wales was able to make a number of recommendations, in both Management Letters and 'Additional Assurance' reports, for improvements to each body's control environment and accounting processes.

3.7 For 2001-02, the National Audit Office Wales made 200 recommendations - an increase of 10 per cent on the number of recommendations made in 2000-01. **Figure 2** provides an analysis, by category, of the recommendations made for 2000-01 and 2001-02. The analysis shows that the most significant change, in percentage terms, related to the 'Regularity of expenditure', an important area where I am pleased to note a decrease of some 50 per cent in the number of points identified. However, the summary also highlights increases of 39 per cent and 18 per cent in respect of recommendations on 'Safeguarding assets' and 'Systems of internal control' respectively.

Figure 2

Recommendations made to client management



NOTE

The number of recommendations for 2000-01 includes recommendations made in respect of one audited body that were not available at the time of my 2000-01 General Report.

Source: National Audit Office Wales analysis

3.8 In the following paragraphs, I report on a theme which emerged from the points raised in Management Letters and 'Additional Assurance' reviews for the 2001-02 financial year: **the monitoring and control of payroll expenditure.**

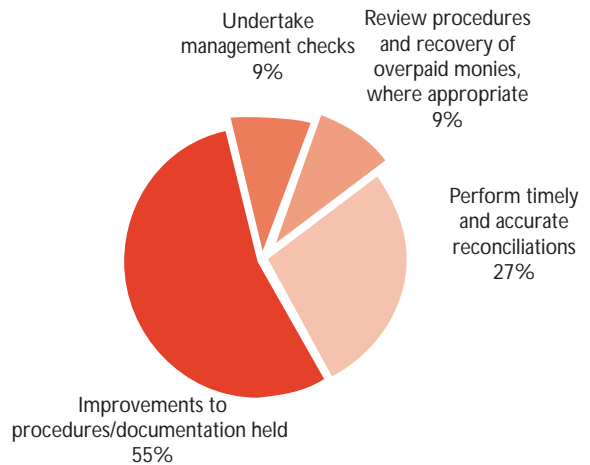
3.9 For the year ending 31 March 2002, staff costs expenditure by the National Assembly for Wales and its sponsored bodies amounted to some £170 million. I consider the audit of payroll costs to be particularly important, not only in terms of the amount expended but also due to the mandatory requirement to disclose sensitive information, such as employees' remuneration, accurately in the annual accounts.

3.10 Of the 200 recommendations referred to in paragraph 3.7, around 10 per cent related to staff costs expenditure. The recommendations made by the National Audit Office Wales covered, for example:

- ▶ the need to undertake adequate periodic reconciliations between payroll and personnel records;
- ▶ the need to recover overpayments to staff;
- ▶ the need to strengthen personnel procedures; and
- ▶ instances of poor documentation in support of disclosures in the financial statements.

Figure 3

Recommended improvements to existing controls over the personnel and payroll functions



Source: National Audit Office Wales analysis

Figure 3 provides an analysis, by category, of the recommendations made in respect of the monitoring and control of payroll expenditure.

Lack of action by management in respect of previous years' recommendations

3.11 In my last General Report I commented that, whilst many of the management letter points made by the National Audit Office Wales related to issues that had emerged for the first time during 2000-01, there had been instances where recommendations arising from the previous year's financial audit had not been actioned appropriately.

3.12 I am concerned to note from my 2001-02 audit work that there has been little improvement in this position. In the most serious instance, the National Audit Office Wales has reported to the management of one Assembly Sponsored Public Body its observation over a fundamental control weakness and recommendation for the fourth year in succession.

3.13 The Permanent Secretary of the National Assembly for Wales provided an assurance to the Assembly Audit Committee, at its hearing on 18 April 2002, that all future recommendations made by the National Audit Office Wales would be implemented by the agreed dates. The Audit Committee, in its

subsequent report on that hearing, commented that 'We consider that external audit reports to management are a vital and integral part of the audit process that must be given full respect and acted upon. It is clear that the Permanent Secretary takes his responsibilities seriously in this regard and we commend the procedures that he and the Finance Group have put in place for monitoring the implementation of the recommendations made by the National Audit Office.'

3.14 Given these comments and the assurances provided in 2002, I look to the Permanent Secretary to ensure that robust procedures are put in place to address all National Audit Office Wales recommendations in full and by the agreed dates. The actions taken in this regard by the Assembly and its sponsored bodies will be reviewed by the National Audit Office Wales as part of its 2002-03 financial audit examinations.

Corporate governance

3.15 In April 1999, the Turnbull Committee proposed that the scope of the existing statement of internal financial control be widened to encompass all systems of internal control. The Treasury adopted the Committee's recommendations and issued guidance to all central government bodies in 2000. This guidance explains that a sound system of internal control depends on a thorough and regular evaluation of the nature and extent of the risks to which an organisation is exposed. It also stresses that the purpose of internal control is to help manage and control risk, rather than eliminate it.

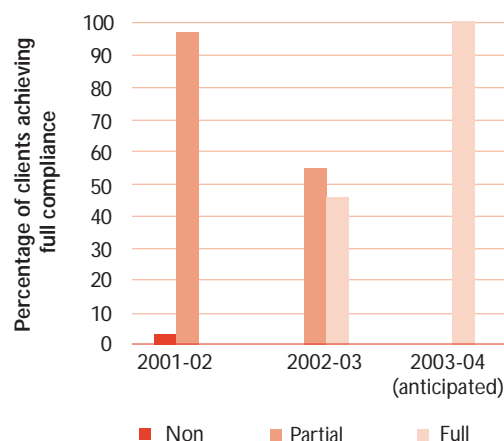
3.16 The Treasury strongly encouraged the preparation of a full statement of internal control for the 2001-02 year of account. If central government organisations were unable to achieve this goal, they were required to produce a statement within their 2001-02 accounts, setting out progress and providing an assurance that full compliance would be achieved by 2003-04 at the latest. For 2001-02, where bodies had introduced effective risk management procedures during the accounting year they disclosed the achievement of 'partial' compliance and the expectation of a natural progression to 'full' compliance from 2002-03

3.17 As part of its 2001-02 audits, the National Audit Office Wales has continued to work closely with the National Assembly and all other central government bodies in Wales in their development of sound corporate governance. This work has assisted the implementation of effective risk management procedures in line with the timetable set by Treasury. For example, National Audit Office Wales staff have participated in client risk management workshops and given presentations to audit committees on corporate governance issues and risk management techniques.

3.18 My review of the progress made by the National Assembly for Wales and its sponsored bodies found that many had achieved 'partial' compliance in 2001-02 with the expectation of full compliance from 2002-03. I am pleased to note that all clients currently expect to achieve full compliance in 2003-04, in line with the Treasury deadline. **Figure 4** provides a summary of results in 2001-02, as well as a summary of client expectations for the 2002-03 and 2003-04 financial years.

Figure 4

Actual and anticipated compliance against the HM Treasury timetable from 2001-02



NOTE

The above percentages exclude those bodies, such as those in respect of NHS restructuring, that were created in 2003-04.

Source: National Audit Office Wales analysis

3.19 Staff of the National Audit Office Wales will continue to work closely with the management of client bodies in helping them to develop their risk management policies and procedures.

3.22 Figure 5 shows that there has been a decrease in the number of clients that had made 95% of their payments within the stipulated 30 days. This formal target was achieved by only 41 per cent of clients in 2001-02, compared with 60 per cent in 2000-01.

Payment performance

3.20 The Late Payment of Commercial Debts (Interest) Act 1998, which came into force on 1 November 1998, requires that supplier invoices that are not in dispute are paid within 30 days of receipt of goods or services or valid invoice, whichever is the later. The Act reinforces the terms of the UK Government's Better Payment Practice Code, which built upon and replaced the former Confederation of British Industry's 'Prompt Payers Code'. The Act also makes provision for suppliers to claim statutory interest from the public sector if valid invoices are paid late.

3.23 I am concerned at the decline in these overall payment performance statistics, which reflect poorly on the Welsh central government sector and may impact adversely on the cash-flows of the businesses that hold supply contracts with these bodies. I look to the Welsh Assembly Government to ensure that effective payment and reporting procedures are in place, so that valid invoices are paid to creditors promptly and in accordance with the requirements of the 1998 Act and the Better Payment Practice Code. I shall continue to monitor the overall performances achieved in future financial years.

3.21 For a number of the client accounts that I audit, their regulatory framework requires disclosure within the Foreword to their annual accounts of the percentage of all payments that are made within the specified 30 day period. For 2001-02, some 75 per cent of the 32 accounts audited were required to disclose this information, which is summarised with prior year comparatives, at **Figure 5**.



Working with other auditors

Internal Audit

- 3.24 The internal audit function operates as a service to the management of each audited body by measuring and evaluating the effectiveness of its internal control systems. Internal audit therefore constitutes an important part of the systems of control within each organisation. To be most effective, internal auditors should be afforded appropriate independence from management, reporting directly to the Accounting Officer and the body's Audit or Corporate Governance Committee.
- 3.25 The National Audit Office Wales has, in carrying out its audits, considered the work of internal audit and sought wherever possible to take assurance from its work. This reliance, facilitated by regular liaison and collaboration, provides audit cost savings to my clients by reducing the overall audit burden.

Other auditors

- 3.26 I am required by Section 98(4) of the National Health Service (NHS) Act 1977 to examine, certify and report on the NHS summarised accounts. These accounts are prepared by the National Assembly for Wales from the underlying primary accounts submitted by the five health authorities, the Dental Practices Board and the 15 NHS trusts. The primary auditors of these accounts are appointed by the other spending watchdog in Wales, the Audit Commission. In order to fulfil my responsibilities under the Act, and consistent with the principles of Statement of Auditing Standard 510 (*The Relationship between Principal Auditors and Other Auditors*), my staff have reviewed the work of the primary auditors, scrutinised their reports and discussed their findings with them.
- 3.27 The Audit Commission is also responsible for appointing the primary auditors of local government expenditure in Wales. The appointed auditors examine the annual accounts of Welsh local authorities and report their findings to each authority's elected representatives. In addition to this core work the Audit Commission also examines, certifies and reports on the use by local authorities of other project-specific funding provided by the National Assembly.
- 3.28 The Audit Commission reports its findings on project-specific funding to the relevant division of the National Assembly, for example, by reporting its findings on local authority transport grants to the Highways and Transport Division. However, in 2002 officials of the National Assembly, National Audit Office Wales and Audit Commission undertook a review of the reporting mechanism in place. The review noted that the reporting arrangements in place were 'division-specific' and that as a result they did not provide an 'overview', by local authority, to the National Assembly.
- 3.29 To improve the reporting arrangements in place, the National Audit Office Wales liaised closely with the National Assembly and the Audit Commission to enhance the reporting of project-specific local government expenditure funded by the National Assembly. The revised format will be introduced from 2003 and will ensure that the Audit Commission provides the Assembly's Finance Group with an Annual Audit Report for each local authority. These annual reports will complement the existing arrangements and will summarise the results of all audit examinations and report on important thematic findings and recommendations.
- 3.30 I am encouraged by the potential benefits of this development and the anticipated improvements and I look forward to reviewing the outcome of these new arrangements as part of my 2002-03 audit examinations.

PART 4 Other advice and services provided

Introduction

4.1 In addition to my financial audit and value for money audit work, I have continued to carry out a range of other work during 2001-02.

This part of the report sets out:

- ▶ the work I have undertaken in response to correspondence and other enquiries;
- ▶ my role as a 'prescribed person' under the Public Interest Disclosure Act 1998; and
- ▶ the ways in which I have assisted my clients and other stakeholders.

Correspondence work handled in 2001-02

4.2 My work in respect of correspondence and other enquiries from members of the public, businesses, Assembly Members and officials continues to increase. This increase has been particularly evident in respect of correspondence received from the public, which I believe reflects a heightened awareness of my role as the independent watchdog of public expenditure in Wales.

4.3 During 2001-02, I received 54 letters from Assembly Members, Members of Parliament and the general public, of which 49 required a full examination by the National Audit Office Wales and a substantive response. This is an increase of 58 per cent on the number I received in the previous twelve months.

4.4 Issues raised with me during 2001-02 included concerns regarding:

- ▶ the regularity and propriety of expenditure by the Assembly or its sponsored public bodies;
- ▶ alleged failures to secure good value for money in the disposal of public assets;
- ▶ alleged non-compliance with European procurement rules; and
- ▶ instances of the poor management or application of public funds resulting in delays or deficiencies in the provision of public services.

4.5 I consider dealing with correspondence to be an important aspect of my work and it is important for the people of Wales to know that all concerns raised with me are taken seriously, investigated fully and objectively, and responded to promptly. Together with staff in the National Audit Office Wales, I shall continue to accord high priority to this work.

4.6 I am also a 'prescribed person' under the Public Interest Disclosure Act 1998. This Act provides protection for employees wishing to make disclosures regarding alleged malpractice in the workplace that threatens the public interest. Some of the correspondence addressed to me has been raised by individuals (whistleblowers) wishing to make disclosures under the Act.

Other advice to client management

4.7 During the 2001-02 financial year, a number of client organisations sought advice from myself or staff of the National Audit Office Wales on accounting, regulatory and control environment issues. The following paragraphs provide examples of the advice provided to client management and how I have responded positively to requests for assistance.

NHS restructuring

4.8 In May 2002, the Director of NHS Wales invited me to review the estimated running and transitional costs of the restructured NHS Wales. This request followed an announcement by the Minister for Health and Social Services that the ongoing running costs of the new structures would not exceed the existing running costs and that the transitional costs would lie in the region of £12.5 million to £15.5 million.

4.9 My review concentrated on examining the composition of the existing 'running costs envelope' within which the on-going running costs would have to be contained, together with the make up of the running cost and transitional cost estimates.

4.10 My findings were set out in a letter to the Director of NHS Wales dated 6 December 2002 and have since been made public. In summary these are:

- ▶ The existing running costs had been soundly calculated by the NHS Directorate;

- ▶ The savings needed in order for the restructure to be cost-neutral had been identified within the NHS Wales Department and Health Commission Wales (Specialist Services) budgets but not for the National Public Health Service (NPHS), Local Health Boards and Business Services Centre (BSC); and
- ▶ Transitional costs were, by their nature, prone to uncertainties and would need to be revisited as plans progressed.

4.11 My letter set out six recommendations:

- ▶ Operational planning work should be completed as soon as possible to ensure the projected savings can be achieved;
- ▶ A need for a more detailed review of how the BSC and NPHS will operate in practice;
- ▶ To revisit transitional staff costs as the main determinants of these costs become clearer;
- ▶ A need for tightly controlled contingency provision;
- ▶ Accommodation and IT costs should be reviewed as staff requirements become clearer; and
- ▶ Procedures to monitor running costs of the new structure should be developed.

4.12 The Director of NHS Wales has accepted all of these recommendations. I will be monitoring the actual spend on running and transitional costs as part of my future work on the finances of NHS Wales.

Welsh Risk Pool

4.13 During 2001-02, the Welsh Risk Pool reimbursed health authorities and NHS trusts for payments for clinical negligence and personal injury amounting to some £46.3 million in respect of 136 cases, a rise of £35.9 million from the £10.4 million paid out in 2000-01. This sharp rise in claims reimbursement payments was not fully anticipated by the Welsh Risk Pool when it set the premium levels payable by NHS bodies for that financial year. As a consequence, the Pool had to collect a further £20 million of premium contributions at a late stage in the year in order to fund the totality of its reimbursement payments.

4.14 Following the emergence of these largely unforeseen financial problems in November 2001, the Accounting Officer for NHS Wales commissioned an external review of the Welsh Risk Pool to identify what further measures should be taken to strengthen and ensure the cost-effectiveness of management arrangements for clinical negligence and other claims funded by the Pool.

4.15 The review was led by the Director of NHS Wales, who chaired a steering group which included representatives of the Audit Commission and the National Audit Office Wales, as well as senior NHS and Assembly officials. The team concluded its work in October 2002, and its final report and recommendations were submitted to Ministers for consideration. As Auditor General, I was pleased that the National Audit Office Wales was able to contribute specialist analytical skills to the financial aspects of this review, assisting in the diagnosis of problems and identification of solutions to assist NHS Wales in the future management of these important issues.

Advice to new clients

4.16 The National Council for Education and Training for Wales, the Care Council for Wales and the Children's Commissioner for Wales all produced their first sets of accounts for the 2001-02 financial year. The National Audit Office Wales assisted the management of these bodies by providing technical accounting and audit advice on a range of issues. Examples of this advice are given in **Figure 6**.

Secondments to audit clients

4.17 I have also arranged, where appropriate, for staff from the National Audit Office Wales to be seconded to client organisations. This has helped forge closer links between the National Audit Office Wales and the organisations concerned, and provides opportunities for each secondee to gain a greater understanding of the operating environment of each client. These secondments are funded fully by the client bodies concerned, and are therefore undertaken at no financial cost to me.

Figure 6

Examples of advice given to new clients in respect of the 2001-02 financial year

- ▶ The National Audit Office Wales provided advice regarding how one client's financial management system could be used to support more fully its financial statements, thereby streamlining the accounts production process.
- ▶ The National Audit Office Wales advised the National Council for Education and Training for Wales on its accounting treatment of the former Training and Enterprise Councils, including the transfer of their assets and liabilities.
- ▶ The National Audit Office Wales provided advice on the requirements of the Treasury-led corporate governance initiative and the benefits of effective risk management procedures.

4.18 The National Audit Office Wales currently has a member of staff seconded as Director of Support Services at the Sports Council for Wales. It also has two staff on secondment to the Assembly, within its Financial Accountability Division and NHS Directorate. These seconded officers are assisting on the Whole of Government Accounts project and the restructuring of the NHS in Wales respectively. In a reciprocal arrangement, a member of Assembly staff is currently working at the National Audit Office Wales as part of a programme to develop the Assembly's knowledge and understanding of external audit.

4.19 Arrangements are also in place for secondment exchanges with the Audit Commission. A member of staff from the National Audit Office Wales has been seconded to the Audit Commission's technical unit and, in return, members of staff from the Audit Commission are currently leading a number of audits at the National Audit Office Wales.

Introduction

5.1 In my last General Report I stated that, with the value and volume of European-funded projects expected to increase significantly over the next few years, the National Audit Office has an important role to play in ensuring that these projects are managed properly. In this part of my report I:

- ▶ provide an overview of the European Structural Funds in Wales;
- ▶ explain the reporting requirements associated with the closure of the 1994-1999 structural fund programmes; and
- ▶ summarise the findings of the National Audit Office Wales regarding its audits of individual European grant claims.

The European Structural Funds in Wales

5.2 There are four Structural Funds;

- ▶ the **European Regional Development Fund (ERDF)**, which aims to reduce regional inequalities;
- ▶ the **European Social Fund (ESF)**, which aims to improve employment prospects across the European Union;
- ▶ the **European Agricultural Guidance and Guarantee Fund (EAGGF)**, which part-finances national agricultural aid schemes (the Guarantee section) and assists the development and diversification of communities in rural areas (the Guidance section); and
- ▶ the **Financial Instrument for Fisheries Guidance (FIFG)**, which assists the restructuring of the fisheries sector.

5.3 The European Structural Funds provide grant aid for projects which have been approved under targeted programmes agreed between the European Commission and Member States. European Programmes aim to address Objectives determined at Commission level. In Wales, funding is currently available under three Objective programmes, and four, much smaller, Community initiatives. The three Objective programmes are:

- ▶ **Objective 1**, operating in West Wales and the Valleys, which aims to assist the development and structural adjustment of regions whose economic development is lagging behind;
- ▶ **Objective 2**, operating in parts of East Wales, which aims to support the economic and social conversion of areas hardest hit by urban and industrial decline, restructuring and the loss of traditional activities in rural areas; and
- ▶ **Objective 3**, operating in all areas outside the Objective 1 area, which aims to combat long term unemployment by tackling such issues as social exclusion and equal opportunities, and by promoting lifelong learning.

5.4 Organisations with projects that meet the criteria set out in the Programming documents agreed by the European Commission may apply for grant aid towards the total costs of their project. The level of grant awarded varies but is usually around 50% of the total estimated cost. The remainder, known as match funding, must be raised by the organisation managing the project.

5.5 The total level of European Funding available to Wales during the period 2000-2006 (excluding match funding) is around £1.4 billion. This represents a significant increase from the funding of £395 million provided to Wales during the previous Programme period, the six years between 1994 and 1999. Within Wales, the European Structural Funds are managed by the Welsh European Funding Office (WEFO), an executive agency of the Welsh Assembly Government, in partnership with a wide range of bodies from the public, private and voluntary sectors.

Closure of the 1994-99 European Programmes

5.6 During 2002-03, as well as managing the funds received under the current European Programmes, WEFO were also in the process of closing a number of the old (1994-1999) programmes. Programme closure required WEFO to make any outstanding payments of grant on projects approved under the old programmes, and to submit certain documentation to the Commission. This included a General Statement of Expenditure, and a request to the Commission to release the final balance of grant due on each Programme. The deadline for submission of this information to the Commission was 31 March 2003. After this deadline, any expenditure not claimed by WEFO would be "decommitted", and hence the Structural Funding withdrawn.

5.7 In addition to the information submitted by WEFO, the European Commission regulations required programme closure statements for each of the 1994-99 programmes. These statements, which the Commission regulations stated should be prepared by an independent audit body, were required to provide an overall conclusion on the accuracy of the financial data submitted to the Commission and to give an overall conclusion on the management of the programmes. The Commission agreed that, in Wales, programme closure statements should be prepared by the Head of Internal Audit of the National Assembly for Wales.

5.8 As part of his work on the closure statements the Head of Internal Audit would specifically examine the following areas of administration of the 1994-99 and 1997-99 European Programmes and Community Initiatives:

- ▶ The robustness of management and control systems including systems for the appraisal and approval of projects, and the payment of interim and final claims to project sponsors.
- ▶ The adequacy of control examinations undertaken by WEFO, in accordance with the Commission's requirements that Member States carry out inspection visits on a representative sample of projects, and that the total expenditure examined is at least 5% of the total Programme spend.

▶ The sufficiency of procedures for the investigation and resolution of irregularities, including follow up action in respect of errors identified by WEFO's own systems of control or by the external auditors of interim and final expenditure claims submitted by project sponsors.

5.9 The work on closing all the Programming and Initiatives was completed within the deadlines set by the Commission. At the time of writing, WEFO were awaiting the Commission's deliberations and ruling on the results of the closure of the 1994-1999 programmes. I will be examining the results of this work, which is still ongoing, as part of my audit of WEFO's 2002-03 accounts later this year.

Audit of European Grant Claims

5.10 In last years' report I noted that, in addition to auditing the accounts of the Welsh European Funding Office itself, staff of the National Audit Office Wales were providing audit certificates for an increasing number of grant claims by Assembly Sponsored Public Bodies. In this part of my report I comment on the volume and value of claims audited during 2001-02, and on the results of my audit examinations.

5.11 Under the current European Programmes, all projects in receipt of European funding, with the exception of ESF grant for less than £20,000, are required to submit audit certificates to the WEFO in support of their annual claims for grant. At the end of each project, a final audit certificate must also be submitted to WEFO before the last instalment of grant is paid over. Under the previous European programmes there was no requirement for external audit certification of projects funded by the European Social Fund. In auditing annual and final project claims for European grant, staff of the National Audit Office Wales have regard to audit instructions issued by WEFO, as well as to auditing standards issued by the Auditing Practices Board.

5.12 In the year to 31 March 2003, the National Audit Office Wales issued a total of 23 audit certificates. This represents an increase from the 15 certificates issued during the previous year due to the need for project sponsors to submit audited final claims to WEFO on the older European Programmes and Initiatives, to facilitate their closure by 31 March 2003.

5.13 Of the 23 audit certificates issued in the year to 31 March 2003, the National Audit Office Wales issued 20 final audit certificates on projects approved under the older European Programmes and Community Initiatives. All but two of these certificates were qualified, with an average of four separate audit observations made on each. **Figure 7** below provides an analysis of the reasons for audit qualification. It shows that over half of the observations made related to insufficient documentation being held in support of claims. For a quarter of these cases, the auditor observed that grant recipients did not have documentation in support of the time spent by staff on the project.

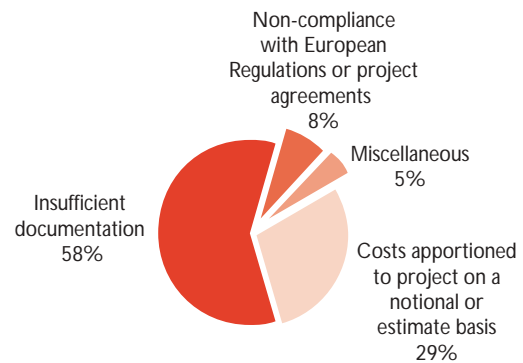
5.14 WEFO have told the National Audit Office Wales that, as a result of these audit qualifications, funding in excess of £0.75 million has been withheld, or is due to be clawed back, from grant recipients.

The new European Programmes

5.15 In last year's report, I noted that it was still a little early to draw any substantive conclusions from audit work on the 2000-06 European Programmes. A temporary embargo on the need for project sponsors to provide annual audit certificates in respect of European Social Fund projects during the period March 2002 to 1 January 2003 has meant that a large number of projects are only now being audited for the first time. At the time of writing, the NAO Wales is working on the audit of 28 claims received under the current European Programmes and is awaiting notification that a further 45 claims are ready for audit. The preliminary results of these ongoing audits indicate that there are still problems arising from a lack of awareness amongst many project sponsors as to the documentary requirements of European Funding.

Figure 7

Analysis of the reasons for qualification of audit certificates for European funded projects



Source: National Audit Office Wales analysis

5.16 With the volume and value of European Funding set to increase in Wales over the next few years, it is important that European projects are managed properly. The National Audit Office Wales has an important role to play in that respect, both as the auditors of the Welsh European Funding Office itself and as the external auditors of a number of European grant claims. To this end, during 2001-02, they have worked closely with project sponsors and the Welsh European Funding Office, to provide support and guidance to those Assembly sponsored bodies for which I am the appointed auditor. At the request of Assembly sponsored bodies, staff in the National Audit Office Wales have attended, and spoken, at conferences designed to increase an awareness of the documentary requirements of European funding. They have also provided ad hoc advice to other organisations such as Colleges of Higher and Further Education for which I am not the appointed auditor, but which act in partnership with the bodies I audit.

Introduction

- 6.1 In this chapter I comment on instances of poor procurement practice in 2001-02. These instances concerned: the procurement activities of the National Council for Education and Training in Wales, which was examined by the Assembly's Audit Committee in January 2003; and Assembly's procurement of suppliers in respect of its flagship 'Lifelong Learning Network' project.

Importance of effective procurement

- 6.2 As with any business, the Welsh central government public sector is dependent on the provision of goods and services to achieve its objectives and deliver its core services. The failure to procure these goods and services on a cost-effective and proper basis:

- ▶ places the achievement of key objectives and services at risk;
- ▶ prevents the achievement of sound value for money; and
- ▶ increases the likelihood of adverse publicity that affects the reputation of the Assembly and its sponsored bodies.

- 6.3 In the following paragraphs I report on examples where the National Audit Office Wales, in liaison with internal audit, have identified significant weaknesses in the procurement actions taken and their failure to comply fully with the regulations and procedures in place.

The National Council for Education and Training in Wales

- 6.4 In my Report on the opening accounts of the National Council for Education and Training for Wales (the National Council) I summarised the procurement failures which resulted in my qualification of those accounts. In the following paragraphs I have detailed those failures, describing the main weaknesses identified and corrective action subsequently taken.

- 6.5 The National Assembly issues to all its sponsored bodies a Management Statement and Financial Memorandum, which sets out the relationship between the two bodies. In particular, the Management Statement defines the framework

within which the sponsored body will operate, whereas the Financial Memorandum details the terms and conditions under which funding is given, requiring the adoption of particular standards of financial control. Areas addressed in the Financial Memorandum include procurement, requiring a body to adopt competitive tendering for all procurement, with specified limits of delegated authority covering areas such as single tender action (up to a value of £25,000 per procurement). Where an activity exceeds that delegated limit, as with any sponsored body, the National Council is required to approach the National Assembly for approval.

- 6.6 During the National Council's first 17-month period of account, a series of contracts were identified where the National Council had not complied with the various requirements of the Financial Memorandum, but had also failed to seek approval from the Assembly for that action. In total, 21 contracts were found where one or more failures of the Financial Memorandum had occurred. Expenditure incurred under these contracts totalled some £2.8 million.

- 6.7 The National Council applied to the Assembly for retrospective approval to diverge from the requirements of the Financial Memorandum for these 21 contracts. Approval was withheld in 14 cases and the resultant expenditure, totalling some £2.2 million, was therefore deemed irregular, resulting in the qualification of my audit opinion on the National Council's accounts.

- 6.8 I established a number of reasons behind these breaches. Firstly the National Council had been created from five main predecessor bodies, including the former Further Education Funding Council for Wales and the four TEC companies in Wales, previously operating as private companies. In its first year, the National Council adopted the inherited systems from those five predecessor bodies, and as a result the National Council operated five sets of procedures along with five accounting systems. The National Council also inherited the staff of the five predecessor bodies, with each body having different private and public sector operating cultures and backgrounds.

- 6.9 I found that there had been no effective review to ensure that each of these five systems complied with the stringent operational requirements of an Assembly sponsored body, nor did senior management implement adequate procedures to ensure all staff were familiar with the requirements

of the National Assembly. In particular, the TEC companies would not previously have operated within the public sector framework, and were not familiar with the concept of regularity. I also noted that specific guidance should have been issued on the requirement of European Commission's procurement regulations.

- 6.10 I identified two main areas of weakness in the National Council's procurement practices: non-compliance with procurement regulations, as required by the Financial Memorandum; and poor contract management. The weaknesses are summarised in **Figure 8**:



- 6.11 To help ensure that further instances of non-compliance do not arise, the National Council has since taken a range of measures to strengthen its procurement procedures and systems of control. A professional Procurement Manager was appointed in October 2001, with responsibility for the production of a unified set of procurement procedures. These were issued in January 2002 and were supplemented by the provision of detailed training to all staff.

- 6.12 As part of my 2002-03 examinations I shall review closely the National Council's progress and developments in this important area that is crucial to sound financial management, and I shall report to the National Assembly as appropriate.

The National Assembly's Lifelong Learning Network Review

- 6.13 The Welsh Assembly Government established its Lifelong Learning Network project in 2001 with the aim of providing a high-speed network link and Internet access to schools, libraries and other learning centres throughout Wales. The National Assembly for Wales approved the project at a total cost of some £9.5 million, with the majority of expenditure to be incurred from 2002-03.

- 6.14 In February 2002 I received correspondence from a member of the public concerning the management of the project, in particular the Assembly's appointment of its procurement agent. To address these concerns the National Audit Office Wales conducted a joint review with officials of the Assembly of the circumstances, including the management and administration of the project.

- 6.15 In respect of this project the joint review found that there had been:

- ▶ A lack of a coherent procurement strategy and general documentation to support the actions taken by the National Assembly;
- ▶ A failure to comply fully with European Union procurement regulations, in that the National Assembly for Wales did not place an invitation to tender in the Official Journal of the European Communities (OJEC) and did not comply with European Commission deadlines for responding to requests for information from prospective bidders;
- ▶ Failures to comply fully with the Assembly's internal procurement guidelines in respect of the avoidance of conflicts of interest, the approval of single tender appointments, the completion of financial vetting and the failure to use a 'sealed bid' process for the competitive tenders received;

- ▶ Inadequate contractual documentation, in that there was no formal contract in place between the National Assembly for Wales and the appointed procurement agent. This in turn compounded a general lack of clarity over the respective roles of the Assembly and the appointed procurement agent; and
- ▶ An inappropriate funding mechanism between the Assembly and one of its sponsored bodies, in that some £9 million was paid to the sponsor body in advance of need. The Assembly recovered this amount in full within days of the advance payment.

6.16 To address these shortcomings, the joint review recommended that:

- ▶ The Assembly should centralise responsibility for the procurement of certain services such as information technology;
- ▶ The Broadband Unit of the National Assembly for Wales should be staffed with an appropriate 'mix of skills' and that, where necessary, appropriate training be provided on project, procurement and contract management;
- ▶ The Welsh Assembly Government should introduce procedures to ensure that all projects are managed in accordance with accepted best practice, such as the principles of the PRINCE 2 methodology;
- ▶ The Broadband Unit should seek the advice and guidance of the Assembly's Compliance Officer and Procurement Unit prior to placing submissions before Assembly Ministers where an external supplier is to be used as a partner for delivering projects under the broadband agenda;
- ▶ The Procurement Unit should remind all Assembly staff of the internal regulations and guidance available on the National Assembly's Intranet;
- ▶ The Broadband Unit should reviews its records' management procedures to ensure that an adequate audit trail is maintained for all future projects and that key decisions and the reasoning behind them are recorded fully; and

- ▶ The existing project arrangements should be extended for a period of no more than six months pending a review of the Assembly's legal position, after which a re-tendering process should take place.

6.17 Following the completion of the joint review and in light of the recommendations made, the Assembly Accounting Officer has taken the following actions:

- ▶ Heads of Division are now regularly reminded of their responsibility to ensure that they have systems in place to secure compliance with the Assembly's procurement policy through their annual statements of internal control. The Permanent Secretary additionally issued a reminder to all Heads of Division and the Accounting Officers of Assembly Sponsored Public Bodies of the need to take their compliance responsibilities particularly seriously so that they could satisfy themselves that the roles and responsibilities of staff involved in procurement exercises are clear; that the staff involved have the necessary skills and understand clearly what is required of them; and that the relevant delegation limits are understood and being observed.
- ▶ The Assembly now has clear policies on procurement, which reflect best practice. The Assembly's Head of Procurement delivered a series of awareness-raising courses to all grade 7s and above to reinforce the messages contained within that guidance and to ensure that senior managers are clear about their roles.
- ▶ The Permanent Secretary sought independent assurance from his Internal Auditors on the standard of procurement compliance across the Welsh Assembly Government. A review of the framework and practices supporting procurement and contract management was undertaken and a report produced jointly by the Assembly's Procurement Unit and Internal Audit Services. From a subsequent review, Internal Audit was satisfied that overall controls in respect of procurement practices within the Assembly were now generally effective.

- ▶ To enable the Procurement Unit to monitor continuing compliance across the Welsh Assembly Government, a procurement database is being developed which will be used to capture all contracts information, match it with the details of officials letting contracts and identify what training they have had. Only officials who have undertaken formal training in Assembly procurement procedures will be authorised to let contracts and place purchase orders.
- ▶ The Assembly's Procurement Unit enhanced its suite of procurement training courses, made one of these courses mandatory and has enhanced the induction training programme to include additional guidance on procurement procedures for new entrants.
- ▶ In relation to the Wales On-Line / Cymru Ar-Lein division of the Welsh Assembly Government, responsibility for managing all procurement exercises has been transferred to the Procurement Unit and an additional procurement professional is being recruited to undertake this work. All new projects will be delivered following PRINCE2 methodology to ensure that projects are properly managed and controlled. A management steering group has been established to oversee the Broadband programme, to ensure that it achieves the Welsh Assembly Government's required outcomes, including those relating to procurement.

6.18 I welcome the various corrective actions taken by the Accounting Officer, and look to him to ensure that all officials responsible for the procurement of goods and services are made fully aware of the need to comply with both internal procurement regulations and guidance, and also the European Union's requirements. During my 2002-03 audit examinations of the National Assembly for Wales, I shall be undertaking a follow-up review of the actions taken in respect of the Lifelong Learning Network project and the Assembly's procurement practices.

6.19 During 2003 the National Audit Office Wales will also be undertaking, as part of its additional assurance reviews at each Assembly sponsored body, a review of the adequacy of the procurement procedures in place. This work should encourage the audit committees and senior officials of Assembly sponsored public bodies to focus on the quality of, and compliance with, procurement procedures.

PART 7 Looking Forward

Introduction

7.1 In this part of my report, I look beyond the 2001-02 financial year and consider potential changes to the scope of my work in 2002-03 and beyond.

Restructuring of NHS Wales

7.2 The National Health Service Reform and Health Care Professions Act 2002 gave legal effect to the Welsh Assembly Government's plans to restructure NHS Wales as set out in "Improving Health in Wales, A Plan for the NHS with its Partners" published by the Minister for Health and Social Services in February 2001. Under this plan, the five health authorities were abolished on 31 March 2003 and 22 Local Health Boards established with responsibility for deciding on local needs for family health, community health and hospital services. Under the new structure, local government, Local Health Boards and the voluntary sector will work together more closely to achieve better co-ordination of health and social services. The Audit Commission will appoint the auditors of the Boards and I will be responsible for auditing the summarised account to be prepared by the Assembly.

7.3 In addition, the Assembly has established an executive agency known as Health Commission Wales (Specialist Services) to provide a strengthened function to commission tertiary and other highly specialised acute services throughout Wales. Under the Government of Wales Act 1998, I will be the external auditor of that agency.

7.4 The Health (Wales) Bill, currently before Parliament, will, if enacted, create two Assembly sponsored public bodies, the Wales Centre for Health and Health Professions Wales. I will be the external auditor of both bodies. The Wales Centre for Health will be an independent training, advisory and research body that will bring together information and evidence and provide advice on which policy-makers can base decisions, co-ordinate professional surveillance of health trends and undertake risk assessments of threats to health and well-being. Health Professions Wales will undertake quality assurance of pre-registration nurse, midwife and health visitor training and quality assurance work. The Assembly will also be able to confer other functions on that body such as the maintenance of a register of students in training and the preparation of a code of conduct for healthcare workers.

7.5 These changes to the health and social care sector in Wales will, taken together, add a significant additional dimension to my audit remit.

Whole of Government of Wales Accounts

7.6 Under the Government Resources and Accounts Act 2000 the Treasury has introduced its 'Whole of Government Account' project, with the ultimate aim of producing a set of commercial style consolidated accounts for the whole of the public sector in the United Kingdom. The main objectives of this project are summarised in **Figure 9**. A key component of the project is the Assembly's preparation of a 'Whole of Government of Wales Account'. This account is to be completed on an incremental trial basis to coincide with the Treasury aim of first producing "Central Government Accounts" for the 2003-04 financial year and then a Whole of Government Account for 2005-06.

Figure 9

Objectives of Whole of Government Accounts

- ▶ To assist the setting and monitoring of fiscal policy, by providing improved information on financial performance and sustainable investment;
- ▶ To promote consistency in financial reporting across government and so assist decisions on funding;
- ▶ To help capital planning by providing comprehensive information on asset holdings across government;
- ▶ To provide an audited overall view of government performance and finances.

7.7 The first stage of the project requires the consolidation of the National Assembly for Wales, its executive agencies, all of its sponsored bodies, Estyn, the five health authorities and the Dental Practice Board. The Treasury has split this stage of the project into four milestones as detailed in **Figure 10**. The Assembly successfully achieved Milestones 1 and 2 by the respective Treasury deadlines of 31 October 2001 and 15 March 2002. The National Audit Office Wales reported no fundamental weaknesses to the Treasury over the achievement of the two milestone targets. These results compare favourably with the many Whitehall government departments that failed to meet the deadlines set.

Figure 10

Whole of Government Accounts Milestones

Treasury Milestone	Target Date	Assembly progress against the Milestones
Milestone 1 Agreement of balances as at 31 March 2001 within the Central Government Accounts boundary.	31 October 2001	Achieved. Of 17 government bodies producing sub-consolidations, the Assembly was one of only three bodies to meet this target.
Milestone 2 Achieving consistency of accounting policies, records of account and 2000-01 financial information.	15 March 2002	Achieved. The Assembly was one of only three bodies to meet this deadline.
Milestone 3 First 'trial run' of 2001-02 consolidated accounts of the Assembly and its sponsored bodies.	20 December 2002	Deadline missed with the draft account received on 18 March 2003.
Milestone 4 Second 'trial run' of 2002-03 consolidated accounts of the Assembly and its sponsored bodies.	19 December 2003	Treasury guidance issued on 10 March 2003. Assembly work ongoing.

7.8 However, the National Assembly for Wales delivered its pilot 2001-02 consolidated account on 18 March 2003, some three months after the Treasury's Milestone 3 deadline of 20 December 2002. The primary cause of this delay concerned the late receipt of underlying accounting information from many of the Assembly's sponsored bodies, and in particular the considerable delay in the production of the first set of accounts of the National Council for Education and Training in Wales. The Assembly also experienced technical difficulties arising from the introduction of the Treasury's computer software package. Despite these difficulties I am pleased to report that the National Audit Office Wales was able to complete its examinations of milestone 3 and provide a clear opinion on the 'pilot' accounts produced.

7.9 Welsh Assembly Government officials have continued their development work on the Treasury's Whole of Government Accounts computer software package that automates and streamlines the consolidation process. The Assembly is one of only ten government bodies to pilot the new system and I am pleased to note that officials have played a pivotal role in its design and testing prior to Treasury implementation across all government departments.

7.10 I shall continue to work closely with the National Assembly for Wales and its sponsored bodies in moving towards the production of a Whole of Government of Wales Account and I look to Assembly officials to continue in this pivotal role within the Treasury-led project.

Resource-based budgeting

7.11 Resource-based budgeting is designed to bring the reporting and budgeting process together on an accruals basis, enabling meaningful comparisons to be made between annual financial out-turn and accruals-based 'resource' estimates. The key change brought about by this new process is that activities are budgeted for when resources are 'consumed' and not when they are paid for.

7.12 The Welsh Assembly Government agreed to the introduction of resource based budgeting in principle from 2002-03, and the Assembly then converted its cash estimates for forward years to resource estimates. Following this endorsement, the Assembly's 2001 budget planning round, which set the budget of the Assembly and its sponsored bodies from 2002-03 to 2004-05, was also undertaken on a resource basis.

7.13 These developments represent a fundamental change in the financial management of the Welsh central government sector that has removed the longstanding principles of cash-based accounting. Given the significance of this change, it is important for senior management, and other officials affected, to take full account of the new resource-based budgeting principles and to introduce and implement effective resource-based budgeting procedures.

7.14 The introduction of resource-based budgeting will require careful monitoring. Overspending on Main Expenditure Groups could potentially be more difficult to control than under the previous cash-based system. As part of my 2002-03 audit work I shall review the progress made in the first full year of resource-based budgeting and report to the Assembly's Audit Committee as I deem necessary.

Care Standards Inspectorate

7.15 The Care Standards Inspectorate for Wales (CSIW) was established as part of the Welsh Assembly Government by virtue of the Care Standards Act 2000. It came into existence on 1 April 2002 and its financial transactions will form part of the Assembly's resource account from 2002-03 onwards. The CSIW is a new comprehensive social and health care regulator for all services relating to personal social services and support to children and young people, older people and their carers. Its remit includes deciding who can provide services in this sector and the inspection of such services to ensure that regulations and national minimum standards are met.

Changes to the public audit arrangements in Wales

7.16 The Secretary of State for Wales has produced a Bill for public consultation and pre-legislative scrutiny that would, if enacted, establish a single public audit body for Wales from April 2005. This body would be headed by the Auditor General for Wales and would incorporate the work currently undertaken in Wales by the Audit Commission and, on my behalf, by the National Audit Office Wales. The staffs of both bodies based in Wales would transfer to the new organisation.

7.17 I welcome this development. The new body would be able to work to common high standards, and would be able to follow public money throughout the public sector in Wales. It would also be able to undertake studies of a cross-cutting nature covering the joint provision of services by central and local government. In setting up the new body it would, of course be necessary to protect the constitutional position of local government who are accountable to their own electorates. It will also be necessary to provide a new mechanism for the provision of appropriate cross-border comparative information by working in collaboration with other audit and inspection bodies operating in the United Kingdom.

Adding value

7.18 The National Audit Office Wales continues to provide advice to client organisations, informally and formally, on a range of finance related matters. The National Audit Office Wales remains committed to ensuring that the Assembly and its sponsored bodies maintain a high level of regularity and propriety in their day to day activities and in serving the people of Wales.

7.19 As Auditor General for Wales, I intend to continue to provide an efficient, effective and economical service to the National Assembly for Wales on all aspects of my work, with the primary aim of helping taxpayers' money to be spent wisely.

APPENDIX A

Published value for money reports on which work was undertaken in 2001-02

Securing the future of Cardiff Bay (published June 2001)

Procurement in the further education sector (September 2001)

The National Assembly's new building project: update report (November 2001)

The Arts Council of Wales: Centre for Visual Arts (November 2001)

Managing the estate of the NHS in Wales (November 2001)

Themes in procurement (March 2002)

Continuing the regeneration of Cardiff Bay (May 2002)

European Union Structural Funds: maximising the benefits for Wales (June 2002)

The renewal and disposal of property held by the NHS in Wales (July 2002)

The disposal of the mid-Wales hospital (October 2002)

Osiris: the PFI contract for information technology in the National Assembly for Wales (October 2002)

Management of the further education estate in Wales (February 2003)

Management and delivery of hospital cleaning services in Wales (May 2003)

APPENDIX B

Accounts covered by this report

This Report covers all of the 2001-02 accounts prepared by the National Assembly for Wales and the other public bodies that I audit. A complete listing is given below:

Accounts prepared by the National Assembly for Wales

- ▶ Assembly Core Resource account
- ▶ Assembly Consolidated Resource account
- ▶ Cadw: Welsh Historic Monuments
- ▶ Welsh non-Domestic Rating
- ▶ Summarised Health Authorities' account
- ▶ Summarised NHS Trusts' account
- ▶ Summarised Funds Held on Trust account
- ▶ Welsh European Funding Office
- ▶ Assembly Members' Pension Fund Account

Accounts prepared by other bodies categorised by subject area

Agriculture and Rural Development

- ▶ Countryside Council for Wales
- ▶ Forestry Commission Wales
- ▶ Forest Enterprise Wales

Economic Development

- ▶ Wales Tourist Board
- ▶ Welsh Development Agency

Health and Social Services

- ▶ Welsh National Board for Nursing, Midwifery and Health Visiting
- ▶ Care Council for Wales

Local Government and Environment

- ▶ Local Government Boundary Commission for Wales

Education and Lifelong Learning, Sport, Culture and Heritage

- ▶ Arts Council of Wales
- ▶ National Council for Education and Training in Wales
- ▶ Higher Education Funding Council for Wales
- ▶ National Library of Wales
- ▶ National Library for Wales Pension Fund Account
- ▶ National Museum and Galleries of Wales
- ▶ Qualifications, Curriculum and Assessment Authority for Wales
- ▶ Sports Council for Wales
- ▶ Sports Council for Wales Trust Account
- ▶ Welsh Language Board
- ▶ Estyn
- ▶ General Teaching Council for Wales

Other

- ▶ Welsh Administration Ombudsman
- ▶ Health Service Commissioner for Wales
- ▶ Children's Commissioner for Wales

Welsh accounts audited by the Comptroller and Auditor General and laid before the National Assembly for Wales

The Comptroller and Auditor General was responsible for the audit of the following Welsh accounts for 2001-02:

The Secretary of State for Wales (Wales Office) resource account.

This account is prepared by the National Assembly for Wales on behalf of the Wales Office, but as this is a Whitehall department it is subject to audit by the Comptroller and Auditor General;

Sports Council and Arts Council Lottery Distribution Accounts.

The Sports Council for Wales and the Arts Council of Wales are Lottery distributors. Each prepares a separate annual statement of account for the discharge of their Lottery functions. These activities are not devolved responsibilities and are instead performed under delegated authority from the Department of Culture, Media and Sport;

The European Agriculture Guidance and Guarantee Fund.

This European fund pays subsidies to Welsh farmers, which are routed through the National Assembly for Wales and the Countryside Council for Wales. This is not a devolved function, and an annual account is prepared by each body in the form prescribed by the European Commission.