



Cynulliad Cenedlaethol Cymru **The National Assembly for Wales**

Y Pwyllgor Cyfrifon Cyhoeddus **The Public Accounts Committee**

Dydd Mawrth, 11 Mehefin 2013
Tuesday, 11 June 2013

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Cofnodir y trafodion yn yr iaith y llefarwyd hwy ynndi yn y pwyllgor. Yn ogystal, cynhwysir trawsgrifiad o'r cyfieithu ar y pryd.

The proceedings are recorded in the language in which they were spoken in the committee. In addition, a transcription of the simultaneous interpretation is included.

Aelodau'r pwyllgor yn bresennol
Committee members in attendance

Mohammad Asghar	Ceidwadwyr Cymreig Welsh Conservatives
Jocelyn Davies	Plaid Cymru The Party of Wales
Mike Hedges	Llafur Labour
Sandy Mewies	Llafur Labour
Darren Millar	Ceidwadwyr Cymreig (Cadeirydd y Pwyllgor) Welsh Conservatives (Committee Chair)
Julie Morgan	Llafur Labour
Jenny Rathbone	Llafur Labour
Aled Roberts	Democratiaid Rhyddfrydol Cymru Welsh Liberal Democrats

Eraill yn bresennol
Others in attendance

David Aldous	Rheolwr Cyswllt—Cefnogaeth Dechnegol Archwilio, y Comisiwn Archwilio Associate Controller—Audit Technical Support, Audit Commission
Anthony Barrett	Archwilydd Cyffredinol Cynorthwyol Cymru, Swyddfa Archwilio Cymru Assistant Auditor General for Wales, Wales Audit Office
David Rees	Rheolwr Llywodraethu, Swyddfa Archwilio Cymru Governance Manager, Wales Audit Office
Mike Usher	Cyfarwyddwr Technegol ar gyfer Archwilio Ariannol, Swyddfa Archwilio Cymru Technical Director for Financial Audit, Wales Audit Office

Swyddogion Cynulliad Cenedlaethol Cymru yn bresennol
National Assembly for Wales officials in attendance

Dan Collier	Dirprwy Glerc Deputy Clerk
Tom Jackson	Clerc Clerk

Dechreuodd y cyfarfod am 9.01 a.m.
The meeting began at 9.01 a.m.

Cyflwyniadau, Ymddiheuriadau a Dirprwyon
Introductions, Apologies and Substitutions

[1] **Darren Millar:** Good morning, everybody, and welcome to today's meeting of the Public Accounts Committee. I remind everybody that the National Assembly for Wales is a bilingual institution, and people should feel free to contribute to today's meeting in Welsh or English, as they see fit. Headsets are available for translation and amplification of sound. I encourage Members to switch off their mobile phones, BlackBerrys and pagers as they can interfere with the broadcasting and other equipment. Finally, if there is an emergency, we should follow the instructions of the ushers. We have a full house today, so we will go

straight into item 2 on our agenda.

9.01 a.m.

**Materion sy'n Codi o Ganfyddiadau Adroddiad Swyddfa Archwilio Cymru
'Bwrdd Draenio Mewnol Cil-y-coed a Gwastadeddau Gwynllŵg'
Issues Arising from the Findings of the Wales Audit Office report 'Caldicot
and Wentlooge Levels Internal Drainage Board'**

[2] **Darren Millar:** We are starting this morning's meeting with a video link with the Audit Commission. This is the second meeting in which we have taken formal evidence on this particular issue. We will be hearing from the Wales Audit Office a little later on in the meeting. I welcome David Aldous, who is the associate controller of the audit technical services at the commission. Good morning to you, David.

[3] **Mr Aldous:** Good morning.

[4] **Darren Millar:** We are very grateful for your help with our inquiry this morning. If there are problems with the video link or the sound, please let us know and we will ensure that Members repeat their questions. We have obviously had a look at this report in some detail in our previous committee meeting and committee members have a lot of concerns about the failures in governance at this particular organisation, and indeed what may, or may not be, a failure by the auditors to pick up the problems at the drainage board sooner. The Wales Audit Office, to be fair, has acknowledged that there are legitimate questions regarding the effectiveness of previous audits. Your organisation was responsible for conducting audits at this organisation before 2006, I think—

[5] **Mr Aldous:** I think that 2005 was the last year.

[6] **Darren Millar:** Okay. Can you tell us whether you noticed any problems in any audits that were undertaken by the Audit Commission?

[7] **Mr Aldous:** First of all, I thank the committee, the committee clerks and the National Audit Office, whose office I am using today to facilitate the video link; it is extremely helpful and much appreciated. By way of introduction, it is probably worth providing a little bit of background to the role of the Audit Commission in relation to the audits of smaller bodies. The first point to make is that the Audit Commission does not itself carry out audits of local public bodies. The statutory responsibility of the commission is to appoint the auditors of local public bodies, and once appointed, those auditors have their own responsibilities in law and have statutory responsibilities that they must exercise independently and in their own right. So, there is that distinction between the commission and appointed auditors and the responsibilities of appointed auditors once appointed. That means that we do not, and cannot, direct auditors. Our role is to, for example, maintain and develop a code of audit practice that auditors have to follow and we provide guidance and technical support to auditors.

[8] It is part of my responsibility in the commission to provide technical support to the firms that we appoint to carry out audit work. That means that we specify the overall approach, and in relation to the audits of smaller bodies, the approach that we now have is one that is designed to provide limited assurance in relation to the annual returns and the information that is provided by smaller bodies, including the 127 internal drainage boards that we are now responsible for making audit appointments to. That approach is designed to give limited assurance, which is different in nature to an audit under international standards of auditing, which is designed to give reasonable and positive assurance. That may be one issue that you will want to talk about further in your discussion. We apply the limited assurance

approach to bodies that spend more than £6.5 million per annum. That is in line with the threshold above which companies are required to have a statutory audit under international standards of auditing. Therefore, it mirrors to some extent the fact that, in other sectors, there is recognition that having a full audit for smaller bodies may not be proportionate.

[9] Therefore, going back to your question about the Audit Commission, you are right to say that the commission had responsibilities in Wales before the Public Audit (Wales) Act 2004, which set up the Wales Audit Office. That included responsibilities in relation to this internal drainage board. We no longer have the audit files that relate to those audits, so I am not able to go back through the work that was carried out back then. Our policy is to hold on to files for six years and it is likely that the files would have transferred at the time to the Wales Audit Office. Therefore, I am afraid that I cannot go into any detail in terms of what auditors did at the time in relation to audits in 2004-05 and earlier audits. However, I am happy to talk through the current approach to internal drainage boards, which might contribute to your debate later this morning.

[10] **Darren Millar:** Thank you for those opening remarks about how the Audit Commission appoints auditors and does not undertake audits. However, you would be responsible, would you not, for the quality of the audits that are undertaken?

[11] **Mr Aldous:** We have a regulatory function—that is correct. That regulatory function flows from the fact that we appoint the auditors, and that, therefore, auditors are contracted to us. Therefore, part of it is contract management, ensuring that audits are delivered in a timely way. We also have a quality review programme to look at the results of audit work and to follow up on any issues that relate to the quality of work that has been undertaken. Therefore, yes, we have an overall regulatory role.

[12] **Darren Millar:** Given the findings of the Wales Audit Office in the report that is before the committee, are you satisfied that the quality of the audits that were undertaken on behalf of the Audit Commission, by the people who were appointed by your organisation, were of sufficiently high quality in the past?

[13] **Mr Aldous:** I have no evidence of any concerns that were raised in relation to 2004-05 or earlier.

[14] **Darren Millar:** So, no concerns were raised at that time as a result of any of those audits on the internal drainage board?

[15] **Mr Aldous:** No, not that I am aware of. As I say, it is going back some time, but I am not aware that any concerns were raised.

[16] **Darren Millar:** I have one final question, which is on the other drainage boards that are partly in Wales and partly in England, for which you still retain responsibility for the appointment of auditors. Have you changed the way or the methodology by which you appoint, or have you changed the guidance and technical support that you give to auditors, as a result of this piece of work by the Wales Audit Office?

[17] **Mr Aldous:** We liaised closely with the Wales Audit Office as soon as we were made aware by it that work was being undertaken, which led, eventually, to the public interest report. Even at that early stage, we encouraged the Wales Audit Office, and the relevant audit team, to liaise directly with the auditors of those internal drainage boards that are cross-border. Indeed, I believe that the Wales Audit Office not only liaised directly with those audit teams, but also with the auditor of the River Lugg IDB, which was receiving some services from Caldicot and Wentlooge IDB at the time.

[18] So, from an early stage we encouraged liaison; that is very much part of the way that we work together as public audit agencies. We have auditor groups that bring together audit representatives of our respective regimes. We also have other groups that bring key practitioners and stakeholders together. We liaise directly with each other in that way. We have a good and open relationship with the Wales Audit Office and information flow is good in that respect. That means that as soon as we are aware of something such as an emerging issue, we are able to consider whether we need to issue any new guidance to auditors. At the time that the Wales Audit Office started its work in relation to Caldicot and Wentlooge, we did not issue any new guidance. The right approach for us was to wait for the Wales Audit Office to conclude its investigations, which culminated in the public interest report that you are considering. As soon as that was published, we made that available to all auditors in our regime—not just auditors of internal drainage boards, but auditors of all small bodies, because it raised significant points around governance and the sort of things that can go wrong with governance. We have made that available to auditors.

[19] We do not think that we need to change the approach. I touched on the different approach that we have in any case; perhaps I will say a little bit more about that. We did not think that we needed to change the approach to limited assurance work, which is the approach that we have for internal drainage boards within our regime. Clearly, it is helpful for auditors to see the results of the work that was carried out at this particular IDB.

[20] **Darren Millar:** I have a number of Members who want to come in on this. We will hear from Aled first and then Jocelyn.

[21] **Aled Roberts:** I want to ask whether the limited assurance approach would have been the one adopted prior to 2005.

[22] **Mr Aldous:** No, it would not have been. The limited assurance approach came in for IDBs in 2009. We brought in a limited assurance approach for smaller bodies generally before then, from about 2000 or 2001. Internal drainage boards were brought more fully into the limited assurance regime in 2009, as I recall. At that time it would have been an audit, I believe, leading to reasonable assurance of the same sort of audit that the Wales Audit Office currently carries out at this IDB and other bodies.

[23] **Aled Roberts:** So, between 2005 and 2009, the Wales Audit Office would have carried out a reasonable assurance approach to audit, rather than the limited assurance approach that you referred to?

[24] **Mr Aldous:** That is my understanding. Clearly, the Wales Audit Office will be able to confirm that. What that means is that it is carrying out an audit that is designed to provide reasonable assurance, positive assurance if you like, that the financial statements are free of material misstatement. The difference between that and limited assurance is that limited assurance is based on an annual return, which the smaller bodies—IDBs in England—now prepare. This provides a summary financial statement. It also includes a governance statement with clear and explicit assertions around governance that is made by the board itself, in the case of IDBs, or the parish council or another smaller body in the case of other bodies. The auditor is required to review the annual return and supporting information and reach a report on whether there are any matters that come to the auditor's attention that would give cause for concern. An example of this would be that relevant legislation or regulatory requirements had not been met. The auditor is then able to give an opinion that the information in the annual return is in accordance with proper practices. That audit report is in the form of a limited assurance—a negative form of reporting—and allows for exception reporting. So, if the auditor is made aware of particular issues or has concerns based on the information that has been presented to the auditor, the auditor can and does qualify the audit report by listing exceptions that set out those areas for concern. That is quite an effective and proportionate

way of carrying out the basic responsibilities of auditors at smaller bodies, allowing for the possibility of reporting any concerns on an exceptions basis, if that is appropriate.

9.15 a.m.

[25] For example, in 2011-12, when there were 154 internal drainage boards reporting, there were six qualifications of the auditor's report, and all of the qualifications related to concerns that the auditor had identified in relation to assertions by the board in its governance statement. There was a lack of evidence relating to the preparation of accounting statements and the timeliness of those statements; a lack of evidence in relation to adequate internal control; and a lack of evidence in relation to internal audit—these kinds of things, which gives rise to exception reporting. That is quite a proportionate and, we still think, appropriate way of fulfilling the auditor's basic routine responsibilities year on year.

[26] Clearly, if something does come to the attention of the auditor that warrants further investigation, then auditors in England, as in Wales, continue to have their statutory responsibilities and powers and can investigate further. In the case of issues such as those identified at Caldicot and Wentlooge, they can do work leading to a public interest report. We have had examples in parishes with the limited assurance regime where there have been a number of public interest reports setting out concerns relating to governance issues. So, we think that it is still quite an appropriate way of responding, on an exceptions basis, if there are concerns that the auditor needs to investigate further.

[27] **Darren Millar:** Mr Aldous, may I remind you that we are very limited for time this morning and you are giving us quite lengthy answers at the moment. If you could be brief with your responses, I would appreciate that so that we can get through all the issues we want to touch on.

[28] **Mr Aldous:** Of course.

[29] **Jocelyn Davies:** You do not keep any records past six years, which is understandable, but your records do not allow you to know whether they were destroyed or passed on to the audit office. Is that correct?

[30] **Mr Aldous:** I would need to check that, to be honest. I would imagine that, as there was a direct transfer of functions from the Audit Commission in Wales to the Wales Audit Office, there would have been a transfer of records and information at that time, but I would need to check that for you.

[31] **Jenny Rathbone:** I am struggling to understand how the audits that took place between 2005-06 and 2009-10 were done under a reasonable assurance regime because, normally, boards or trustees would take due account of any concerns raised. When the concerns raised in the 2005-06 report were not implemented and nothing was done about them, how is it that the auditor in the subsequent years did not take further action and talk to the board to tell it that it had to do something?

[32] **Mr Aldous:** I cannot comment on that because that is something that Wales Audit Office will comment on.

[33] **Jenny Rathbone:** They are supposed to be operating reasonable assurance, which means that they must have a critical mind when they go in to do their audit.

[34] **Mr Aldous:** The Wales Audit Office will comment on that. In relation to the limited assurance regime, one of the assertions included in the governance statement that board members have to sign up to is that they have taken appropriate action in response to previous

internal and external audit recommendations. That is quite an important assertion and one that is included in the list of assertions in the governance statement that is part of the annual return that supports the limited assurance approach. Without prolonging this, as I realise you are up against it in terms of time, the governance statement is much more explicit and direct in many ways than the lengthier narrative governance statement that you see at larger bodies. That is deliberate, to ensure that board members, parish councillors and others see very clearly what it is they are signing up to in terms of the governance arrangements, including actions taken on previous audit recommendations.

[35] **Aled Roberts:** Whether it is limited assurance or a reasonable assurance model, what action would you take if you found that trustees or a board had not complied with previous recommendations within an audit?

[36] **Mr Aldous:** It is the appointed auditor, rather than the commission, who would need to make that judgment. There are a number of responses available to the auditor. I would expect the auditor to consider what is appropriate. So, if the previous recommendation related to a fundamental weakness and no action had been taken on that, I might expect the auditor to consider taking further action, for example by considering a public interest report to raise the issue in that way. There are other mechanisms available. It is possible for the auditor to make what is known as a statutory recommendation under the legislation, which requires the body to make a formal response to the auditor. So, there is a range of tools available to the auditor, and it will be the auditor's judgment as to what will be the most effective mechanism for getting some further action to address the concerns that were previously raised.

[37] Reading the papers for today, it sounds as though the history of governance issues, coupled with the whistleblowing concerns, were part of what prompted—quite rightly—the auditor in this case to look more deeply at the issues that the auditor felt needed to be examined more closely at Caldicot and Wentlooge.

[38] **Sandy Mewies:** Good morning. You have talked about the good co-operation between the Audit Commission and the Wales Audit Office in producing the report, but to what extent is the commission working with the audit office to consider how internal drainage boards can be audited effectively in the future? If you are doing that, what sort of discussions have you had about examples of good practice, and have you shared those with the Wales Audit Office?

[39] **Mr Aldous:** We do liaise on our respective audit projects in the sense that the Wales Audit Office is represented by having an observer on the joint practitioners' advisory group and attends meetings with our suppliers. We also have an observer under equivalent arrangements within the Wales Audit Office. However, we each have to work within the specific legislative frameworks that apply within England and Wales. There are now differences between those, for example in relation to the accounts and audit regulations. So, we in England have to work within the context of the accounts and audit regulations that apply in England, just as you have to comply with the equivalent accounts and audit regulations that apply in Wales. Those regulations determine whether a body is a smaller relevant body, or not. If a body is spending less than £6.5 million, it is a smaller relevant body under the regulations, and proper practices require it to prepare an annual return. It has an option of preparing full accounts. In fact, one IDB in England—the Lower Severn Internal Drainage Board—has elected to prepare full financial statements that are then subject to a reasonable assurance audit, but that is the only one.

[40] So, bodies are entitled to prepare an annual return, which can only really be subject to a limited assurance review. That is the nature of the audit work that it is appropriate to carry out in relation to an annual return. So, there are some constraints that apply and I can understand different public audit agencies wanting to take slightly different approaches to

how they might respond to particular risk profiles for the bodies that fall within their respective areas of responsibility. Having said that, recognising the different legislative frameworks, we do try to learn from each other, and I think that that is done more via ongoing dialogue and keeping each other abreast of what we are doing, rather than through formal sharing arrangements, if I may put it that way.

[41] **Sandy Mewies:** So, it is quite limited in that case. I would expect, if you have joint working groups and something came to light that was important, you would share it, but you do not share it with individual organisations.

[42] **Mr Aldous:** It depends. We also work with other stakeholders. You have seen references to the practitioners guide. There is an advisory group that is responsible for preparing that, which includes the Association of Drainage Authorities. You have had evidence from the ADA previously. The ADA, quite rightly, is doing a lot of work in this area to develop better documentation and better guidance for bodies in relation to their key governance documents. We very much support and welcome that, and we continue to liaise with all stakeholders to try to ensure that what we are applying is appropriate to the circumstances of these bodies.

[43] **Aled Roberts:** The Wales Audit Office report refers to the regulations and standing orders of the board dating back to 1943, despite DEFRA having issued model standing orders in 2005. In those boards that operate partly in Wales, did the Audit Commission provide any advice to the internal drainage boards with regard to updating their standing orders?

[44] **Mr Aldous:** It would not have been for the Audit Commission to provide advice. That is not a role that we have in relation to IDBs. The responsibilities of the auditors of those boards relate to the preparation of the annual return, and they would have reviewed the annual return and looked at the assertions made in the governance statement supporting the annual return. As to whether they requested as part of that, or commented on, governance documents at those particular boards, I would need to check with the auditors concerned. However, they would certainly be able to request supporting information in support of the annual return to provide evidence in support of the assertions that are being made by the board. I do not know whether they looked at those documents specifically; I would need to check with the auditors.

[45] **Aled Roberts:** So, you are not able to tell us if an assertion was made that standing orders complied with current practice, as far as DEFRA was concerned, and that there would be no checking of the documents to ensure that that was the case.

[46] **Mr Aldous:** The assertion is a more general one in the governance statement. There are probably a number of relevant assertions, one of which is that the board is signing up to say that it has an adequate internal control system, that it is assured that it is complying with relevant laws and regulations, that it has assessed risks and has appropriate risk management arrangements and an effective internal audit function. In support of the annual return, there is a report on internal audit and the work of internal audit. Internal audit reports may cover accounting records, financial regulations, compliance with standing orders, and compliance with that kind of thing. It is worth recording or noting that the external auditor of Powysland—one of the cross-border IDBs—did qualify its report on the 2010-11 annual report. That was because of weaknesses in internal audit. One of the aspects in this discussion that we need to have regard to is the extent to which bodies are taking responsibility themselves to ensure that they are complying with key regulations. Clearly, internal audit also has a role in this, and bodies have a statutory responsibility to maintain an appropriate internal audit function. As I say, the auditor had concerns about that at Powysland in 2010-11.

[47] **Jocelyn Davies:** You mentioned earlier the ability of auditors to go for the public interest report should a board ignore their qualifications. That is very expensive to undertake,

at £110,000. Who, in England, would you expect to pay for that?

9.30 a.m.

[48] **Mr Aldous:** You are absolutely right that it is expensive and, therefore, should not be entered into lightly. That is one of the reasons why we always emphasise to auditors that they should consider whether there are other routes and other ways of addressing the weaknesses that have been identified. The reason we are keen to emphasise that auditors have to weigh up very carefully the pros and cons of incurring the cost of carrying out a public interest report, against the public interest of preparing a report and reporting in the public interest, is because the cost is passed on directly to the audited body. That can be quite a significant cost for quite small bodies. We have exactly the same issue in relation to parishes in England, for example. Occasionally, auditors are left with little option but to issue a public interest report, but they have flexibility and discretion about how they go about preparing that public interest report. It is quite possible for a public interest report to be brief and in the form of a letter, for example. Sometimes, the facts mean that it has to be a more extensive public interest report. Recently, the auditor of a parish in England issued quite an extensive public interest report because of a range of governance concerns that needed to be addressed, and the auditor felt that the public interest report was really the only route for doing so. However, it is very important that auditors weigh up very carefully the costs and benefits of going down that particular route.

[49] **Mike Hedges:** We are looking at a relatively small organisation. You talk about an internal audit, but my understanding from talking to this organisation is that it does not actually employ its own auditors. Newport City Council came and effectively did its internal audit for it. Is it not a problem with very small organisations like this one? Would that problem not be solved by making it a part of something like Natural Resources Wales, which is an organisation that is big enough to have its own auditors and is of a scale and size to be able to deal with these matters? You were talking about £110,000 for the action that you mentioned earlier, but that is over 10% of its annual income. That would have a huge effect. Is it not a problem of size, and would it not be better dealt with by making it part of a larger organisation?

[50] **Mr Aldous:** The only thing that I would say in response to that is that you are right that it is not necessary to employ an internal auditor. There are various ways in which smaller bodies can have an internal audit function. That is why I used the phrase earlier of ‘internal audit function’. In England, for example—and I can comment more on England—there are various ways in which small bodies secure an internal audit function. Some of them use the internal audit of the relevant districts, similar to the example that you gave, and others use appropriately experienced individuals who are willing to carry out internal audit work at a number of bodies. The practitioners’ guide that is available to support smaller bodies talks about the ways in which bodies can secure internal audit. It is important that bodies take responsibility for their own governance and, as part of that, secure the assurance that they need internally to enable them to make the assertions that, as board members, they are making. So, it is an important function, but there are many ways in which it can be carried out.

[51] **Mohammad Asghar:** Good morning, David. My question is related to the membership of and appointment to the internal drainage board. The Wales Audit Office report stated that many of the members appointed to the drainage board did not attend the meetings. Have regular Audit Commission audits discovered whether this issue is unique to the Caldicot and Wentlooge drainage board or whether it is commonplace across similar drainage boards in England and those operating partly in Wales?

[52] **Mr Aldous:** I was struck by that, too, when I read the public interest report, especially given the responsibilities that the board members have, collectively and

individually. We have not done any research to find out how extensive a problem that might be in smaller bodies. That would be quite an extensive piece of research to carry out. One question that I have asked is in relation to amalgamations that are taking place in England, and whether that means we are getting some very large boards as IDBs start to merge. As I understand it, the opportunity is taken, when an amalgamation takes place, to create a new board and to review what the membership requirements would be for that new board. I also saw in the evidence that the ADA gave to you that it is encouraging boards to review their membership, look at the size of boards, and so on. I did have some concerns, when I read the report, about the size of this particular board, in that this was maybe a factor in relation to individual board members taking the responsibility that they clearly have.

[53] **Mohammad Asghar:** Thank you, David. Would you let us know whether potential members should be expected to meet specific requirements ahead of their appointment to the boards? Also, do you believe that a lack of representation by local authority or its committees contributed to the problems at the Caldicot and Wentlooge Levels Internal Drainage Board? If so, what could be done to prevent such a situation occurring in future?

[54] **Mr Aldous:** I cannot really comment on what is the appropriate constituency from which to draw the members of the board. That is not really a matter on which I can comment. My perspective on this is around individual board members, in that, just as when individuals in a local authority context, say, become directors of a controlled company, if they become trustees of a charity that is linked to the local authority, or, in this case, if they are nominated to participate as members of a board, it is very important that those individuals understand the responsibilities that they are taking on as trustees or as members of a board. So, I think there is something about the way in which the members of boards are prepared for this role, how they are briefed and inducted, and how they understand the corporate and individual responsibilities they are taking on, just as they might if they were taking on a responsibility in relation to a charity.

[55] **Mohammad Asghar:** Finally, do you think that an appointed member is the most appropriate mechanism for informing the local authority about board decisions?

[56] **Mr Aldous:** Again, I cannot really comment on that; that really is something that is beyond my remit in terms of what the appropriate constituencies for representation on an IDB would be. That is something that, locally and nationally, politicians and others would need to determine as appropriate. It is not really something that I can comment on. As I say, my main concern is around skills, experience and expertise, and ensuring that board members understand their responsibilities, wherever they come from.

[57] One thing that did strike me in the report was that I did not see an explicit reference to the responsibility of the board for accountability for and the stewardship of resources. You could argue that it ran throughout the report, but I did not see an explicit reference to that. A previous witness in your discussions picked up on the point about the accountability of boards, and I just wonder whether there is something there as well, around ensuring that boards understand that they have a responsibility to ensure that, collectively, they are accountable for and show stewardship of the resources they are managing. That is not just a representative role; there is something around understanding their broader accountability.

[58] **Jenny Rathbone:** In the case of Wentlooge and Caldicot, we had the former clerk writing his own redundancy plan, his own re-engagement plan and a restructuring that safeguarded the position of his wife, but made unsafe the position of two members of staff with whom he was in dispute. In the IDBs operating in England and partly in Wales, what sort of arrangements do you have for ensuring detailed and robust monitoring of pay rises that get around the possibly over-cosy relationship that appears to have existed in this case?

[59] **Mr Aldous:** We do not. It is not the role of the commission to monitor that kind of thing. The boards themselves have a responsibility to ensure that they comply with relevant laws and regulations, and that includes any requirements relating to the exercise of discretions around appropriate remuneration packages and so on. So, the decision making is within the board. Clearly, if a matter comes to the attention of an auditor, perhaps in response to somebody inspecting the accounts, a whistleblower, or information that the auditor gathers as part of an audit that gives rise to some concerns about the reasonableness of a decision that the board has made, that is something that the auditor may wish to consider as part of their responsibilities. However, the primary responsibility for complying with the law, regulations and exercising reasonable discretion where appropriate lies with the board itself.

[60] **Jenny Rathbone:** Do you think that auditors now have a heightened awareness of the need to ensure that pay rises are subject to the independent scrutiny of non-executives, given the case of Wentlooge and Caldicot?

[61] **Mr Aldous:** It is not unusual for auditors to be asked to consider whether a body has acted reasonably in relation to a decision around a remuneration or severance package. This happens in other sectors as well. There have been examples where the auditor has raised concerns in other parts of the public sector around the reasonableness or otherwise of the decisions that have been taken by a public body in relation to remuneration. So, it is something that auditors clearly have on their radar, but it has to be something they respond to if they become aware of concerns. It is not their responsibility to approve pay awards or remuneration packages; clearly, that is the responsibility of the relevant public body. However, if there are concerns about the process or the reasonableness of the decision, that is something that the auditor may wish to consider and it is something that happens from time to time in other parts of the public sector, too.

[62] **Jenny Rathbone:** Okay; thank you.

[63] **Darren Millar:** Please be brief, Aled, if you want to come in on that point.

[64] **Aled Roberts:** In this case, the Wales Audit Office report states that Welsh Government officials were made aware of specific concerns regarding governance in February 2011. The Wales Audit Office started an investigation and yet the issues to which Jenny Rathbone has just alluded all occurred between April and June 2011. So, in relation to all of these issues, both the Welsh Government and the Wales Audit Office were aware that questions were being asked and yet these packages regarding redundancy payments et cetera were still approved after all of these issues were raised. Do you not think that that is rather strange, given the comments that you just made with regard to the public sector needing to show that it has control over these issues?

[65] **Mr Aldous:** There are various things that affect the reasonableness of decisions. I am not familiar enough with the facts and the chronology relating to the particular example that you have given to comment on that. What I am saying is that there are examples where auditors have raised concerns about the process or the reasonableness of decisions. However, that is the focus: it is on whether the body itself has acted appropriately. I cannot really comment on the facts of the case that you have just summarised, because I was not involved in carrying out the detailed work. However, that may be something that you want to ask the auditor about.

[66] **Aled Roberts:** I am sure that we will.

[67] **Julie Morgan:** I want to ask you about the role of the civil servants and Welsh Ministers. Who do you hold responsible for the lack of an appropriate decision-making process?

[68] **Mr Aldous:** I cannot really form a view on what actions Welsh Government officials or Welsh Government Ministers may or may not have taken; that is clearly outside my remit. I keep coming back to—and I will keep coming back to it—the point that the primary responsibility for ensuring that a public body complies with the requirements that are placed upon it lies with the board or its equivalent, or the council, or those charged with governance for that public body. That is the primary responsibility. Clearly, there are accountability relationships and reporting arrangements, and scrutiny and oversight arrangements that may apply to different public bodies in different sectors, but the primary responsibility has to be with those charged with governance.

[69] **Julie Morgan:** So, you do not see any responsibility for the Government in Wales.

[70] **Mr Aldous:** I did not say that.

[71] **Julie Morgan:** You said that you could not take a view; is that right?

9.45 a.m.

[72] **Mr Aldous:** I cannot take a view on the actions taken or otherwise by the Welsh Assembly Government officials. That is clearly outside my remit. The prime responsibility is the board's, but, clearly, you would expect any public body to operate within an accountability framework.

[73] **Julie Morgan:** Thank you.

[74] **Darren Millar:** Okay. On that note, David, that brings our evidence session with you to an end. I thank you for joining us via video link. It all seemed to work swimmingly well, which is unusual for Assembly video links. We are very grateful for the help that you have given us with our inquiry today. You will be sent a copy of the transcript, so that you can amend anything that is factually incorrect. Thank you.

[75] **Mr Aldous:** Thank you very much.

[76] **Darren Millar:** Okay. We will move on to the next part of this item, which is to take evidence from the Wales Audit Office in respect of the Caldicot and Wentlooge Levels Internal Drainage Board. I am pleased to be able to welcome to the table Anthony Barrett, assistant auditor general for Wales, Mike Usher, technical director for financial audit in the Wales Audit Office, and David Rees, governance manager of the Wales Audit Office. Welcome to the table. We appreciate your attendance today and the paper that you have prepared and sent to us in advance. I do not know whether you want to make any opening remarks before we go into questions, Anthony.

[77] **Mr Barrett:** I would be grateful if I could do so very briefly, Chair. I was going to explain who is sat here next to me, but you have already done that, which is very helpful. I was also going to draw the committee's attention to the briefing note I have provided, and you have done that for me as well. I would again draw the committee's attention to the distinction between the office of the auditor general and the office of the appointed auditor. I am here in my capacity as the appointed auditor responsible for the report, but also as the assistant auditor general, responsible for our financial audit work. I would like to say, by way of an opening statement, that we have taken on board the learning points from this experience, and I am sure that you will want to explore that with me as we go through. We are now much more robust in our dealings with small and unique bodies. I took the decision to issue the report in the public interest, despite the strong representations that I received at the time from the drainage board that such a public report was not required. I could have just reported directly

to the drainage board, as we have done previously on certain matters. In this case, my view was that to issue a report in the public interest was the right thing to do, while acknowledging possible deficiencies in previous audit work. We undertake our audit work and report without fear or favour. We will continue to do this, even where such action is subject to challenge from various parties, or when this could expose previous audit work to scrutiny and challenge. That is all that I want to say. I am happy to take any questions.

[78] **Darren Millar:** Thank you, Anthony. You referred there to possible deficiencies in previous audit work. Can you tell us why it took a number of years before a public interest report was produced and what were the deficiencies that you have identified in the previous audit work undertaken?

[79] **Mr Barrett:** The deficiencies over a number of years that we identified related to things that the committee will already be aware of, such as standing orders and standing financial instructions being out of date or being updated but not being formally approved, the lack of a corporate strategy and business plan, policies and procedures for budgetary control, human resources and information technology not being in place, a lack of internal audit arrangements going back a few years ago, and the lack of a medium-term financial strategy. Those were the areas that fell within the scope of the audit in terms of reporting on those issues. What we failed to do is to follow those issues up sufficiently robustly, largely because it is a small body, and, if you are going to add more time to the audit, it is going to cost even more. That is no excuse, but that is some of the background. Also, we did not bring everything together holistically, to ask, over a number of years, what this said about the drainage board. That only became an issue for us once we had some of the allegations under the whistleblowing. We looked at those and saw that there was a pattern emerging.

[80] **Darren Millar:** We have just heard from the Audit Commission, which says that, in all likelihood, it would have passed its files to you when responsibilities passed from the Audit Commission to the newly established Wales Audit Office in 2005 for the audit work in respect of this particular drainage board. In the files that were passed to the Wales Audit Office, were any problems identified that made you think, ‘This is, potentially, something that we need to look at rather carefully’?

[81] **Mr Barrett:** The files that are available to us now are from after that date, because we only retain files for six years. However, looking at some of the previous audit files, issues were flagged and reported throughout the process. They were reported by the auditor as part of the normal process in terms of standing orders and standing financial instructions. So, there were some issues highlighted and reported to the drainage board going back to 2005-06.

[82] **Darren Millar:** When you identify an issue that you then raise with the board, expecting it to take action and address that issue, how do you escalate the matter if the board does not address the issue that has been identified?

[83] **Mr Barrett:** There are a couple of different ways of escalating it, depending on the impact that it has on the audit. If it is something that would be directly related to the audit of the financial statements—for example, weaknesses in budgetary control—that would, invariably, result in us having to do more testing, which is what happened in this case, because we could not rely on the budgetary control system. As a result, the fee for the drainage board increased. That is one way in which it is escalated.

[84] The other way in which an issue is escalated is to report again, which we have done on occasion, that an organisation still has not introduced revised standing orders or approved the standing orders. The nuclear option, for want of a better term, is very much the public interest report that you have before you.

[85] **Jocelyn Davies:** Has there been more or less escalation? There are no records prior to 2005-06, although we can assume—I suppose that it is up to us—that things were flagged up before then, unless something happened in 2005-06 that started all of this off. So, what action did the appointed auditors take to escalate things since 2005?

[86] **Mr Barrett:** They would have done two things; one would have been to continue to report to the board that it was not doing the things that it had been recommended that it should do.

[87] **Jocelyn Davies:** However, if you prod somebody and they do not do anything, and you prod them again and they do not do anything, and so you prod them again, what happens then?

[88] **Mr Barrett:** There comes a point at which you say, ‘This is not good enough’, and then you need to do some form of public reporting, which is very much what happened in this case.

[89] **Jocelyn Davies:** However, you were asked to do this public reporting by the Welsh Government, were you not?

[90] **Mr Barrett:** No, that is not correct.

[91] **Jocelyn Davies:** Why is the Welsh Government paying for it, then?

[92] **Mr Barrett:** That is a question that you will have to ask the Welsh Government. It is interesting that, prior to the Welsh Government giving its evidence, I was not aware that that was the case, because we would charge the drainage board for the work, as we are required to do. I have issued a number of public interest reports on small bodies over the years—community councils, for example—and they have paid their own fees. We have agreed to let them spread that payment over a couple of years to help them to manage their finances.

[93] **Jocelyn Davies:** Of course. So, will you be billing the drainage board for this?

[94] **Mr Barrett:** We have billed the drainage board for that work.

[95] **Aled Roberts:** You referred to the nuclear option, and the representative from the Audit Commission also referred to the use of statutory notifications. Were any statutory notifications issued against the drainage board prior to the public interest report?

[96] **Mr Barrett:** No, they were not. Another option is to make statutory recommendations, which, again, have to be dealt with in public. They do not go into the level of detail of a public interest report; they simply say, ‘This recommendation is made under section 25 of the Act, and therefore you have to take it to a public meeting and decide what you are going to do’. However, no statutory recommendations were made prior to this.

[97] **Aled Roberts:** With the benefit of hindsight, might it have been better for statutory notifications to have been issued prior to the report?

[98] **Mr Barrett:** I think that, with the benefit of hindsight, there would probably have been an opportunity to have said, ‘You have not done some of these things that we have been asking you to do—we will now make a statutory recommendation to you’.

[99] **Jocelyn Davies:** So, with regard to the undertaking of the public interest report, even though you were not asked to do this by the Welsh Government, there was involvement by the Welsh Government via the whistleblower, and it seems to me that that was the trigger for

undertaking a public interest report. When you reported back to the interim manager and to the board with your interim report, was there any suggestion at all that this might not necessarily go to a full public interest report at that time, September 2011, or were you clear, at that time, with the board or interim manager, that there would definitely be a public interest report?

[100] **Mr Barrett:** The nature of public interest reports is such that a decision cannot be made on issuing a public interest report until all of the work has been completed, and until what we call a 'consideration document' has been passed for factual accuracy. So, back in September 2011 when we relayed some of the early findings, it would have been clear—it should have been clear—to the drainage board that all options were still open in terms of reporting this.

[101] **Jocelyn Davies:** So, at that point, there may have not been a public interest report. You would not have been in a position—

[102] **Mr Barrett:** I would not have made a decision at that point, no.

[103] **Jocelyn Davies:** Thank you.

[104] **Jenny Rathbone:** The board had ignored the recommendations of the auditors in successive years. Why did none of the auditors that came along subsequently ask to see the chair of the board to find out why they were ignoring the concerns of the predecessor auditors? Was that never done?

[105] **Mr Barrett:** I do not believe that that was ever done as an option, no.

[106] **Jenny Rathbone:** That would not have been a £110,000 conversation. Why was that never done? It seems to be an obvious thing to do, if a dialogue of the deaf is going on, to simply call in the chair of the board and say, 'Look, we've made these recommendations and you haven't done anything about them—why not?'

[107] **Mr Barrett:** In terms of the actual audit work itself, that progresses. In terms of the board dealing with those particular issues, the chair is in attendance at the board meetings where these items are discussed where the auditor reports that things are not being done. So, I am not sure that speaking directly to the chair would have had any more of an impact than talking to the board as a whole. Having said that, as has already been said, there were opportunities for us to have made statutory recommendations at an earlier stage, and that would have involved specific dialogue with the board.

[108] **Jenny Rathbone:** So, the auditor was going to the board meeting presenting their reports, and clearly receiving the response, 'Thank you very much, see you next year'.

[109] **Mr Rees:** If I could come in on the recommendations, while a number of recommendations were made, it is probably not correct to say that the board took no action in relation to a number of those recommendations. For example, the auditor recommended that the board put in place standing orders. In 2008, the board implemented standing orders, albeit they were not approved by the Minister. The auditor recommended that the board improved its budgetary processes, and, to be fair, some improvements were made to budgetary processes. So, there was some action on the part of the board, although it was probably not sufficient.

[110] **Jenny Rathbone:** So, some action was taken but no-one ever said, 'Well, this won't do—a root-and-branch restructure has to take place'.

[111] **Mr Rees:** We would have reported in subsequent years that some improvement had been made, but that there was still more to do.

[112] **Mike Hedges:** What I do not understand—I am sure that you can put me right—is that, if you take school inspections as an example, the first bit of the report will say, ‘We made these recommendations last time—these have not been carried out’ and ‘These have been carried out but not to the required standard’, and I have also seen audit reports in other bodies that say, ‘Last year’s audit said X, this has been done but more work needs to be done’, and I have seen internal audit reports that have said things along similar lines, so why did that not occur?

[113] **Mr Barrett:** It would have been very helpful to have presented it like that, to make it clear. Where issues impacted upon the auditor’s opinion on the financial statements, those issues would have been followed up as part of that financial audit. It is where the issues fell outside of that area that things were not followed up as robustly as I think they should have been.

[114] **Mr Rees:** Just to add to that, one of the difficulties in relation to this audit is the fact that Wales Audit Office auditors audited only one drainage board, and we probably did not appreciate the complexities associated with that type of audit. There are peculiarities, if you like, in terms of the way that drainage boards are set up, the way that they set their rates, the membership of the board and in relation to needing ministerial approval for standing orders. Therefore, when we made certain recommendations, such as the need to implement standing orders, it is probably the case that we did not appreciate at the time that those standing orders required ministerial approval.

[115] One of the things that we have learned from this exercise is the need, when you have unique audited bodies, to get a better understanding of the nature of that organisation. That is the only way, ultimately, that you can improve the standard of the audit.

10.00 a.m.

[116] **Sandy Mewies:** On that point, it seems a bit surprising to me that you would audit a new body—something completely new to you—without examining what needed to be looked at. We are now in a position where you see the deficiencies. I have read about the things that you are going to do—this sort of links into the issue that Jocelyn has been trying to tease out—and records were handed over to the Wales Audit Office by the Audit Commission. We have had two responses saying ‘Well, we don’t keep them longer than six years’—that is fine; I understand that perfectly—but there does not seem to be any evidence at all that they were even examined. I would have thought that, if you examined them and saw these issues coming up, it might have given you an idea of the methodology that you would follow when you did your first work. Is that flawed? Is that correct?

[117] **Mr Barrett:** With any audit, one aspect is to look at the previous year’s audit to see what issues arose from it. That would have happened, even with the handover. We would look at the previous year, to see what recommendations and issues were in there, as would have happened in previous years, and considered the extent to which they impacted upon the audit work that we had to do around providing an opinion on the financial statements. Some would have done and some would not have done. Those that did impact would have formed part of the audit work. On those that did not impact upon the audit of financial statements, I accept that they should still have been followed up more robustly. They were followed up, but they should have been followed up more robustly.

[118] **Jocelyn Davies:** You have seen the evidence of Mr Jackson-Johns, because you have referred to it in the briefing paper that you supplied to us. He thought that he had a clean bill

of health. You say, in paragraph 14, that nearly every year since 2005 you raised the same things with the board. You sit there and say ‘What does this say about the board?’ Well, I say, ‘What does this say about the appointed auditors?’ These people were given the impression that, because you were raising it every year but not escalating it, it did not seem to matter—this list of things that you raised every year. What was the fee every year for you to tell them the same thing? Why did it require a whistleblower before this was properly addressed? The board was under the impression that everything was tickety-boo, even though you say, in paragraph 15, that you raised these significant governance weaknesses in writing with the members of the board. What was their response to that?

[119] **Mr Barrett:** They were not always the same issues every year. Sometimes they were, in terms of standing orders, but sometimes they were new issues.

[120] **Jocelyn Davies:** It was all in the mix.

[121] **Mr Barrett:** Yes, it was all there. I have heard the phrase ‘a clean bill of health from the auditors’; in fact, I saw it used in the press only this week. While that may be what the media says, or what a member of the public who reads the report says, that is not what we provide. We provide an opinion or a report on those things that we are required to report on. So, in the case of the drainage board, we were required to provide an opinion on its financial statements; that is what we did. There would be some ancillary issues that came to our attention that we reported to the board. With hindsight, we should have escalated some of those issues earlier and taken a more holistic approach—which is what we do, I have to say, with every other body that we audit, largely because it incorporates elements from other parts of our business in terms of performance audit. In that way we get a much more holistic view of the organisation. That is what we should have done. That is what we do with other bodies and that is what we will do in future with this body.

[122] **Jocelyn Davies:** You can see from the response of Mr Jackson-Johns that he was under the impression that, because of the way things were going every single year, within the culture of this organisation, these weaknesses were acceptable. He thought that if it was minuted, it was okay.

[123] **Mr Barrett:** If that is the approach that Mr Jackson-Johns wanted to take or chose to take, that is up to him. That would not be my view of it. My view is that the auditor was identifying deficiencies, making recommendations and expecting them to be dealt with.

[124] **Jocelyn Davies:** What about the fee?

[125] **Mr Barrett:** I believe that the fee changed over the last four or five years, from about £2,500 to £9,500. That £9,500 represents about 20 days of audit work. If you compare that with the cost for a unitary authority, such as Cardiff Council, it is £320,000 or £340,000 a year.

[126] **Mike Hedges:** You talk about Cardiff, but that is substantially bigger. Is that the audit fee, or is that also the value-for-money fee, which is in there, and which it picks up? Also—I cannot find it in my papers now—from my understanding, the drainage board is substantially funded by local authorities. In fact, if it was a company, it would probably be considered a controlled company by local authorities, in terms of their sheer payment rates. Why did you not, at any stage, talk to any of the local authorities, or the local authority monitoring officers, about this? This is an organisation that had its annual meeting, and had all these things, but did not have any legal representation there, and did not have a senior accountant there. Surely, talking to the major funding bodies would have sorted this out several years ago.

[127] **Mr Barrett:** On your first point, the fee that I mentioned in relation to Cardiff Council of £324,000 is just the financial audit fee—it does not include the value-for-money work that performance audit colleagues do as well. In terms of its statutory arrangements, its accountability and its governance, the drainage board is a separate legal entity. As the appointed auditor to that drainage board, I am required to report to the drainage board. I am not saying that there are not circumstances under which I might take soundings from other people, but I have to be careful because I am also bound by a duty of confidentiality to the drainage board not to disclose information to other parties. That applies to any of the audit bodies. So, I am very much focused on reporting to those who are charged with governance, and those managing the drainage board, namely the board of the drainage board.

[128] **Darren Millar:** Aled Roberts has the next questions, followed by Jenny Rathbone. I will then bring you in, Oscar.

[129] **Aled Roberts:** Is that not an inherent weakness in the system? If you have a rotten apple, and you only report to the apple, you are wholly reliant on whistleblowers to take it somewhere else. I also wish to ask whether you are reviewing your file destruction procedures. I understand what you say regarding normal six-year destruction policies, but I find it somewhat unbelievable that, in a situation where a body is raising issues year after year—and those issues are still live, or pertinent—you would take the decision to destroy records with regard to previous audits.

[130] **Mr Barrett:** The retention period is very much a financial audit industry standard across the public and private sectors. Any audit that is closed is closed, and therefore there is limited scope to re-perform any of that work as an auditor. That is not to say that we would not look at it—I am just explaining why it is as it is. It is certainly something that I would be happy for us to take a look at, and revise the policy if it was necessary.

[131] **Aled Roberts:** It just seems rather strange. In legal practices, for example, there is a common policy, but where it is known that issues might arise, or that there are ongoing investigations, files would not be destroyed.

[132] **Mr Barrett:** As part of our normal audit work—notwithstanding the deficiencies that I have accepted—those recommendations are just part of our normal audit work and would form part of the audit file, and would be subject to that retention. Interestingly, things like statutory recommendations, or, indeed, public interest reports, by their nature are perhaps of more public interest, and we would normally retain those for a longer period, but we would not do so with the normal audit files.

[133] **Aled Roberts:** I would like to ask for some further clarification. A distinction is made by the Audit Commission regarding limited assurance reports, and reasonable assurance reports. What is the current basis of the preparation of audits as far as you are concerned for these drainage boards in Wales?

[134] **Mr Barrett:** The threshold for a reasonable assurance audit is anything over £1 million. So, this drainage board was subject to a reasonable assurance audit in terms of its financial audit, not a limited assurance.

[135] **Jenny Rathbone:** I am still troubled that, under those circumstances, when the auditor presents a report to the board with clear lines of action required, it would become obvious from the discussion or non-discussion at the board whether there were champions for change. Under this reasonable assurance, what action are auditors now obliged to take, where they have reason to believe that no action is going to be taken as a result of their concerns? That is extremely unusual.

[136] **Mr Barrett:** The reasonable assurance relates to our audit of the financial statements not to some of the other issues. In relation to our audit of financial statements, that will continue in line with the auditing standards et cetera to provide reasonable assurance that they are free from material misstatement whether due to error or fraud. In relation to the other issues, what will now happen, and not just in relation to the drainage board but some of the other small bodies that we might be dealing with, is that specific time will be set aside to ensure that those issues are properly followed up by the auditor. We will look to escalate—for want of a better word—if that is not happening. To be honest, we would not jump on them straight away, but we would say, ‘You were supposed to do this, you have not done it. You have got this next year to do it. If you do not, there are other options available to us as the auditor.’ I have to say that that is what we do with other bodies. It is just the small size and uniqueness of this—which is no excuse—that led to our not doing it with this body.

[137] **Jenny Rathbone:** Will that happen in future?

[138] **Mr Barrett:** It is already happening on this body. It will see an increase in its normal audit fee, which it will not be happy about, but that is not the issue. The issue is that we will make time in there to follow it up.

[139] **Darren Millar:** Julie, you wanted to come in here.

[140] **Julie Morgan:** Just to clarify, you were saying that, if present practice had been applied, these issues would not have arisen.

[141] **Mr Barrett:** No, I am not saying that the issues would not have arisen. In relation to the issues that we identified as part of our audit, we would have taken more prompt action. I have to say that some of the issues that are identified are not ones that we would normally be expected to pick up even as part of a reasonable assurance audit. If it was a limited assurance audit—

[142] **Julie Morgan:** What are those issues?

[143] **Mr Barrett:** They are things like, for example, the salary of the clerk and chief engineer. As part of our normal audit work, that salary figure appears in the accounts. In the correspondence that I have seen, Mr Jackson-Johns said that we required his salary to be put in the accounts. That is incorrect. That is a requirement of account and audit regulations and proper practice around accounts. We would have made sure that it was in there, which is a requirement, and then we would have seen that there had been a 5% increase. We would have looked to see that it was supported by some documentation. In this case, there were letters from the chairman confirming that the board had agreed his salary increase. That would have been sufficient evidence to satisfy us that the figure in the accounts was true and fair. The process by which that had been gone through would not have formed part of our normal audit of the financial statements. That is where someone who is at a board meeting, in attendance or close to it, such as a board member or a member of staff, says to us ‘You need to know that there is something going on here that we are not happy with’. I am happy to say publicly that whistleblowers are to be commended in bringing issues forward. I am not sure about this case, but I have seen private sector cases where people lose their jobs as a result of it. I would want to reassure the committee and whistleblowers that, if they come to us, we will look at those issues. We may not take them forward any further—it depends on the evidence that we find et cetera—but where we do find evidence, as in this case, we will pursue those issues.

[144] **Darren Millar:** Jenny, I think that you wanted to follow up on the salary issue.

[145] **Jenny Rathbone:** I want to follow up on the issue of remuneration, because having been made aware of the problems with this IDB in February 2011, how was it possible that

the former clerk was able to write his own redundancy and re-engagement terms and create a restructuring that safeguarded the position of his wife but not two other employees with whom he was in dispute? Whose responsibility was it to ensure that the inappropriate and cosy relationship that was going on in this board was stopped at the point the Government was made aware?

10.15 a.m.

[146] **Mr Barrett:** I will answer first, but Dave might want to come in on the specifics. As part of our additional work, we became aware of the possible redundancy of the chief executive and his re-employment as a consultant by the board to cover the period before which they could get someone else in. In the end, we did not need to do this, but I considered issuing an advisory notice, which is another very serious thing that auditors can do, which I have not yet done in my career, which prohibits an authority from undertaking something that the auditor considers to be unlawful prior to it taking place until such time as the board has demonstrated why it is lawful and why it can continue to do that. We considered doing that. It was deemed not necessary because the various terms and conditions et cetera that were being proposed were not seen through. I would say that they were not seen through because we raised concerns and made it quite clear that we would take action. That is something that has to happen very quickly. It has to happen before the event. Looking back, we were, at that time, on the ball on that issue and would have taken action if it had been deemed necessary.

[147] **Mohammad Asghar:** Mr Barrett, I clearly heard you say that this is a separate legal entity. Does that mean that it is a limited company? If that is the case, it should have its own articles and memorandum to run its own business within its own organisation and externally, dealing with others. Am I right? In that case, when you went to audit and you followed the rules, did you not tick the boxes as to whether the company was dealing within its own legal limitations? Why was it not tracked down in the earlier stages, rather than letting it go too far? Was there an incompetent audit?

[148] **Mr Barrett:** No. Looking back at when audit first started at the drainage board, in the mists of time, I do not know what took place. We did not have a sufficient understanding, because of its unique nature, and because it was small we deemed it to be low risk. Not particularly as a result of this, we have looked at our approach to small audits and have recognised that they are not low risk. I mentioned previously that I have issued public interest reports on a number of community councils in north Wales and the Swansea area over the last few years. They are very small bodies but they are high risk, because of their size, the lack of a separation of duties and, in some cases, the weakness of the board or the council and the strength of the chief executive or the clerk. What we did not have was a sufficient understanding of the legislative background of this organisation and the complexity of it. In some respects, it is more complex than a very large unitary authority.

[149] **Mohammad Asghar:** I personally think that it is not rocket science, as an auditor, to find out if somebody is going beyond their limitations of power. It can be traced down pretty quickly by auditors. That is the job of a competent auditor.

[150] **Mr Barrett:** No. In relation to an audit of financial statements, the job of the auditor is to ensure that those statements present a true and fair view and are free from material misstatement and error; it is not to see whether the organisation has done everything that it is supposed to do. That is, if you like, part of the expectation gap. I fully understand the expectation gap that exists. We are looking, as an organisation, at broadening our focus in terms of governance, because I think that governance is the key area for us to be looking at. We are developing some work—it is set out in our strategy—to look at governance, because good governance is a precursor to good, high-performing organisations.

[151] **Jocelyn Davies:** Yes. I would agree entirely with that. You are not responsible for the decisions of the board, we should not try to hold you responsible for the decisions of the board, but I am glad that you admit that you did not have a sufficient understanding and that the audit failed to bring about necessary improvements.

[152] **Mr Barrett:** It did, yes.

[153] **Jocelyn Davies:** Anyway, looking to the future, there is a proposal about the abolition of the Audit Commission in the Local Audit and Accountability Bill. If the Audit Commission is abolished, what action do you believe would be necessary to ensure that the arrangements for auditing and governing the internal drainage boards with cross-border responsibilities are robust and effective?

[154] **Mr Barrett:** For me, this goes to the heart of what I see as some of the problems with the changes in England. I do not agree, for example, that allowing a public body to appoint its own auditors is a good thing; it is contrary to the principles of public audit as set out by the public audit forum. My concern would be that, in appointing their own auditors, there is a risk that those auditors are unduly influenced because they need to be reappointed. I am not questioning the professionalism of those auditors, but in this case, both throughout the audit and, indeed, as a part of the public interest report, I and my officers came under significant pressure as to why we should not report in the public interest. However, because I do not require, in effect, the agreement of the drainage board to my appointment on a regular basis, it makes no difference to me and I will just do what is the right thing to do. I would be concerned that that is one of the risks in England.

[155] Also, the drainage boards that are cross-border are smaller than Caldicot and Wentlooge and they will fall within the limited assurance regime. My view is that the limited assurance regime would not pick up the sorts of issues that we have picked up. It remains to be seen how the issues that have subsequently been reported in a public interest report would be picked up through a limited assurance regime.

[156] **Jocelyn Davies:** You could always rely on whistleblowers, I suppose. [*Laughter.*]

[157] **Mr Barrett:** That also raises the question about who the whistleblower goes to—

[158] **Jocelyn Davies:** The Welsh Government, I suppose. In its consultation, the Welsh Government stated that it is keen to ensure that all internal drainage boards that operate wholly or mainly in Wales are audited on the same basis under the same rules as other Welsh public bodies—you will have seen that, I am sure—and it is considering that. Do you believe that that should happen—that we use the same rules for drainage boards as we use for other public bodies?

[159] **Mr Barrett:** I think so. I see merit in that. If you look at the two drainage boards that are wholly or partly in Wales, on a geographical basis, they are mostly in Wales.

[160] **Jocelyn Davies:** Yes.

[161] **Mr Barrett:** I think that Powysland Internal Drainage Board is 90% in Wales and the Lower Wye Internal Drainage Board is about 60% in Wales, but it includes Monmouth, which is the only town within the IDB area. I am not sure of the relative proportion of income that comes from Welsh authorities in support of those, but one might imagine that it is a similar percentage. Dave has already mentioned that we only audit the one, but there are benefits to us in auditing more than one—although that is not necessarily a reason for doing it. We have gained a very good understanding of drainage boards—probably far exceeding what we should have had in the beginning, anyway—over the last couple of years. So, I am

not making a plea that we should audit them, but if we were to do so, we are well placed to audit those.

[162] **Jocelyn Davies:** We have a better understanding of drainage boards, as well, I think. *[Laughter.]*

[163] **Mr Barrett:** What is interesting is that everyone now knows that there are drainage boards and knows that they are complicated and—

[164] **Jocelyn Davies:** In fairness, the people who were on the board were probably only on one board. They were in the same position as you, probably. They did not have experience of good governance elsewhere, given that they were just on the one board. I will leave it there, Chair.

[165] **Darren Millar:** Sandy, did you want to ask a question?

[166] **Sandy Mewies:** No. I accept that the questions were covered, but I was going to come back on a point that was made.

[167] **Darren Millar:** Please do.

[168] **Sandy Mewies:** It is a point of clarification. There are three local authorities that financially support this particular drainage board and you talked about the confidentiality of the audit process and reports to board. I know that there were elected members on the board too, but surely the people who part fund the board will have had access to those audit reports. I am just not clear about this; you might have talked about it in a meeting before I joined—

[169] **Darren Millar:** It is a fair point, is it not?

[170] **Mr Barrett:** Yes. We would not have provided those reports to them, because our reports are to the drainage board.

[171] **Sandy Mewies:** Would it not have been a duty of the board? I find it staggering that a local authority would finance, in any way, any organisation without seeing audit reports from that organisation, because of internal value-for-money regimes. I was just trying to tease out from you—I do not know whether other Members know this; I do not know whether it came out in a previous meeting—whether those previous and, obviously, very important audit reports were seen by the funders.

[172] **Mr Barrett:** I do not know whether they were. It is a very interesting point in terms of the relationship and of funding and information coming back.

[173] **Sandy Mewies:** Surely it is important for the future.

[174] **Mr Barrett:** In some respects, the past is the past. We need to look to the future, and Welsh Government needs to look at the arrangements that it wants for this particular body, but also for the broader issues that it raises in terms of representation, if that is the right word.

[175] **Darren Millar:** It is a fair point. Aled has a follow-up question. I will come to you in a second, David.

[176] **Aled Roberts:** I thought that I had read in some previous papers that Newport City Council internal audit had also had some dealings with the drainage board. Did you ever have any discussions with the Newport internal audit?

[177] **Mr Barrett:** Yes, as part of our audits we would have had a look at what internal audit was doing, to see whether we could place reliance on any of that. We had previously reported that the drainage board, going back a number of years, did not have internal audit in place, hence the reason it had a contract with Newport.

[178] **Aled Roberts:** If you are not able to give us the information today, could you provide us with a note on when you understand Newport internal audit became involved?

[179] **Mr Barrett:** Yes.

[180] **Aled Roberts:** Also, are you aware of whether section 151 monitoring officers from any of the three local authorities were involved? I recall, again from records of a previous meeting, that it was apparent that those section 151 officers started to attend meetings once the whistleblowing got out of control. I am not clear as to whether any of them were members of the drainage board de facto, as officers, but just did not attend.

[181] **Mr Barrett:** We can check that. I do not think that any of them were members.

[182] **Mr Rees:** No; I do not think that any of the section 151 officers were members of the drainage board.

[183] **Darren Millar:** Did you want to add anything?

[184] **Mr Rees:** I will just come back on the question of audit reports going through to local authorities. I do not believe that it was done formally. Obviously, all audit reports that went to the board of Caldicot and Wentlooge would have gone to all members of the board, which included, of course, the local authority representatives. As the report sets out clearly, there were problems in terms of the way that that representation took place. However, they did have access to the reports through that route.

[185] **Darren Millar:** It is a fair point. If there is criticism of the governance arrangements in an audit report, one or more of the individuals responsible for the governance arrangements that are poor are extremely unlikely to draw the attention of the constituent body that appointed them to that board to the problems. That has certainly given us some food for thought.

[186] **Mike Hedges:** I wish to carry on with that point for a second, and then move on to another question. I find it very difficult to understand this. No organisation that I have ever served on has not had a legal representative at all meetings. I cannot imagine how an organisation dealing with over £1 million a year could have meetings where there was no legal representative, but no-one seems to have brought that out.

[187] The other question is: is there really a future for small organisations like this? Would it not be better off subsumed into a larger organisation, such as Natural Resources Wales, which would have its own accountants and legal people so that it could be ensured that things were done as they should be done within the public sector?

[188] **Mr Barrett:** I will take the last point first. There are some small organisations that probably operate very effectively, despite the challenges that being a small organisation can bring. It is clearly a matter for Welsh Government, rather than the auditors, as to what future arrangements it wishes to have for drainage boards and drainage authorities.

[189] The first point that you made has now escaped my mind.

[190] **Mike Hedges:** It was about having a legal representative in meetings making

decisions.

[191] **Mr Barrett:** Again, it is very much up to the board or the organisation to decide what it needs. Smaller organisations, such as a drainage board or community council, rely ostensibly on one individual sometimes—a clerk or whatever—to provide them with everything. The better performing organisations will recognise when they need to bring in advice on particular issues.

10.30 a.m.

[192] **Mohammad Asghar:** Mr Barrett, my question will be on membership. In your report, you mentioned that appointed members to the drainage board did not attend the meetings, so that also probably was a lack of efficiency on their part. Have regular Wales Audit Office reports discovered whether this issue was unique to the Caldicot and Wentlooge drainage board or whether it is common practice across similar public bodies in Wales?

[193] **Mr Barrett:** The easy answer to that is ‘I do not know’. We would not routinely look at attendance at all meetings, but I know from my own experience that the only vaguely comparable bodies in terms of being small bodies are community councils and, sometimes, they struggle with attendance at meetings. However, they have a different model; it is not the same sort of model of appointment and election, and some community councils use a lot of co-opted members rather than elected members. So, being a small body and, in the case of the drainage board, requiring a large number of members and, at the time, having particular quorum rules that made things quite difficult, was not particularly conducive to the delivery of good business.

[194] **Mohammad Asghar:** Do you think that these members should have some sort of qualification or standard when they are appointed to these jobs?

[195] **Mr Barrett:** It is useful for any member, whether they be appointed from a local authority or elected directly, to have some training provided to them. I would expect appointed members from local authorities to have had access to general training through their local authority, but other members may not, and we see this as well on community councils. It is useful to have some training to realise that, as a group of people, they are collectively responsible for the governance and management of that board. Sometimes even that level of knowledge can be missing, so, when things go wrong, they say ‘Oh, well it wasn’t our fault’, but they are the ones who are responsible for that. I am not sure about the qualifications issue; I do not have a view on that. However, training, which does not have to be onerous, about what the basic responsibilities are and how they can best be discharged, would be effective.

[196] **Mohammad Asghar:** Finally, local authorities provide the main financing for these drainage boards. Their representatives should provide more informative linkages between boards and the local authorities, rather than not attending or going and doing nothing.

[197] **Mr Barrett:** If a local authority appoints a member to the board, there is an expectation from that authority that the member will attend meetings. I appreciate that it can be difficult to attend all the meetings that they are required to. The interesting point, which I think has already been alluded to, is the relationship that exists between that appointed member from the local authority, the drainage board and the local authority. That is an interesting triangle of accountabilities and responsibilities, which may not be entirely clear.

[198] **Darren Millar:** Jenny, you wanted to come in, before I bring Julie in.

[199] **Jenny Rathbone:** Community councils have been raised several times in our discussions. What evidence is there that Newport and Cardiff county councils, having failed

to follow the money with Wentlooge and Caldicot, are now waking up to the need to be aware of how money is being used in community councils?

[200] **Mr Barrett:** 'I do not know' is the easy answer to that question. From an audit perspective, the money that, for example, Newport council gives to the drainage board would not be material in terms of our audit of Newport's accounts. It is a relatively small amount of money and probably would not even figure as part of our audit.

[201] **Julie Morgan:** Who do you think should be held responsible for this IDB not following the right decision-making process?

[202] **Mr Barrett:** Ultimately, responsibility rests with the board, namely the collection of members who form the board. They are responsible for the governance and management of that drainage board.

[203] **Julie Morgan:** So, you do not accept any responsibility.

[204] **Mr Barrett:** I am not responsible for the governance and the management of the drainage board. I am responsible for the financial audit work that was delivered and the quality of that work. I accept that we could and should have done things better in terms of our understanding of the body and the follow-up of some of those issues. I take absolute responsibility for the quality of our audit work, but I am not responsible for the decisions that the drainage board makes.

[205] **Julie Morgan:** What about civil servants and the Welsh Government? Do they hold any responsibility?

[206] **Mr Barrett:** I do not have a view on that in terms of how the accountabilities are arranged, and, indeed, what the accountabilities might be going forward.

[207] **Julie Morgan:** Given that they did know, for quite a long period of time, do you think that they should have intervened in some way?

[208] **Mr Barrett:** Dave might correct me on this, but we kept Welsh Government up to date with the things that were going on, and I have to say that we formed the view that Welsh Government was doing things to support the drainage board in terms of making some of the improvements that were needed.

[209] **Mr Rees:** As soon as the whistleblowers made their disclosure to the Welsh Government, the Welsh Government, from that point on, worked very closely both with us and the drainage board, and actually supported it in terms of trying to sort out a number of the governance issues that were identified.

[210] **Julie Morgan:** So you feel the Welsh Government's actions were appropriate.

[211] **Mr Rees:** I cannot comment on matters previous to the whistleblowing as I am not sure about that, but, after the whistleblowing disclosures, the Welsh Government did act appropriately.

[212] **Julie Morgan:** So, all the responsibility, you think, is with the board.

[213] **Mr Barrett:** Legally and statutorily, I believe that that is the case.

[214] **Darren Millar:** Given that these boards are responsible to Welsh Ministers, would you not have expected Welsh Ministers, having seen audit reports that referred to weaknesses

in governance and internal audit and a number of other things over the years, to have given more guidance, perhaps, to the organisation in respect of addressing some of those issues and shortcomings?

[215] **Mr Barrett:** I do not know whether Welsh Ministers per se would have seen the audit reports. I do not even know the extent to which Welsh Government officials would have seen the audit reports. We made the reports to the drainage board.

[216] **Darren Millar:** If an organisation is accountable to Welsh Ministers, that is, to the Welsh Government, they ought to take an interest, should they not, in what is said in the financial audit statements?

[217] **Mr Barrett:** It very much depends on the specific detail of the accountability arrangements that exist. An organisation like the drainage board will have different accountabilities in terms of whether it is managerial accountability, operational accountability or governance accountability. I am not sure that it is clear what those different accountabilities are and who people are accountable to. However, if there are clear lines of accountability and audit reports are being made available, I would expect—and I do not know whether it did or did not—Welsh Government to take an interest in those audit reports.

[218] **Aled Roberts:** What is your understanding of when this whistleblower first approached the Welsh Government? I am not sure that he would share your view that it acted with due speed.

[219] **Mr Rees:** What was raised in terms of the whistleblowing disclosures, and perhaps this has not come out to date, was that there was a tremendous amount of material that was passed to the Welsh Government and subsequently passed on to us. That material identified some of the issues in the public interest report, but, in the course of our audit, we identified a number of other issues that were not in the original whistleblowing disclosures. There is always an issue with whistleblowers in relation to their expectations. Sometimes issues are raised within a whistleblowing disclosure that cannot be dealt with by, for example, the Welsh Government, or by the auditor. In those disclosures, there were a lot of issues in terms of their personnel issues within the board, which were not matters for the auditor and could not really be dealt with by the Welsh Government. It may be that there was an expectation gap there. As far as the Welsh Government is concerned, where it worked with the board was to try to put in place much more effective internal governance within the board, which was not necessarily dealing with some of the issues the whistleblowers were interested in.

[220] **Darren Millar:** We have one further evidence session on this particular issue, and we will be hearing from a whistleblower at that future meeting.

[221] Thank you for the evidence that you have provided today. It would be helpful for Members if you could provide a note on the escalation available to auditors when a problem has been identified. We heard reference today to statutory recommendations, advisory notices, public interest reports and a note in the audit statement. So, to have a list of the things that are available to auditors would be very useful. Other than that, you will be sent a copy of the transcript of the proceedings—you know the drill: anything that needs amending in there, you let us know. Of course, you can liaise with the clerks about that. Thank you very much indeed.

[222] **Mr Barrett:** Thank you, and thank you for your time.

10.40 a.m.

**Cynnig o dan Reol Sefydlog Rhif 17.42 i Benderfynu Gwahardd y Cyhoedd o
Weddill y Cyfarfod**
**Motion under Standing Order No. 17.42 to Resolve to Exclude the Public
from the Remainder of the Meeting**

[223] **Darren Millar:** I move that

the committee resolves to exclude the public from the remainder of the meeting in accordance with Standing Order No. 17.42.

[224] Does any Member object? There are not any objections, so, we will note the papers that accompany the agenda and go into private session. Thank you.

*Derbyniwyd y cynnig.
Motion agreed.*

*Daeth rhan gyhoeddus y cyfarfod i ben am 10.41 a.m.
The public part of the meeting ended at 10.41 a.m.*