

Review of The Exchequer and Audit
Department acts and role of the
Comptroller and Auditor General

GOVERNMENT

MACHINERY

PART I

May 1979

Referred to	Date	Referred to	Date	Referred to	Date	Referred to	Date
5.6.79		18.3.81					
8.6.79		31.3.81					
5.11.79		10.4.81					
12.11.79		7.5.81					
27.2.80		11.5.81					
28.2.80		1.6.81					
3.3.80		3.6.81					
10.3.80		15.6.81					
11.3.80		29.6.81					
17.5.80		12.8.81					
25.11.80							
29.2.81							
6.3.81							
12.3.81							
23.3.81							

PREM 19/480

Material used by
official Historian
DO NOT DESTROY

- ends -

PART 1 ends:-

12 August 1987

PART 2 begins:-

11 Nov 1987

Published Papers

The following published paper(s) enclosed on this file have been removed and destroyed. Copies may be found elsewhere in The National Archives.

1. Cmd. 7845: The Role of the
Comptroller and Auditor General
Published by HMSO, March 1980

2. House of Commons: First Special
Report from the Committee of Public
Accounts, Session 1980-81; Role of
the Comptroller and Auditor General
Published by HMSO, 14 February 1981

Signed Wayland Date 19 April 2011

PREM Records Team



*NBPM. A review in autumn
1982 will give us plenty of time to sort this out.
JWJ
Gao.*

MR WHITMORE

THE LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

The Chancellor saw Ian Bancroft's further minute of 4 August before he went on holiday. He asked me to record that while he does not dissent from the view that it would be prudent to review the detailed arrangements for the transfer of the post in the autumn of 1982, he feels that should the conclusion be reached that it would not be right to down grade the post to Under-Secretary, the corollary should be that it should remain in the Department of Industry, and not be transferred to the Treasury, for the reasons set out in his minute to the Prime Minister of 28 July.

2. I am sending copies of this minute to recipients of your minute of 26 July.

PJ
P S JENKINS
12 August 1981



NSPM yet.

The Chancellor

will be replying.

AKL

MR C A WHITMORE

THE LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

Perhaps I could comment briefly on one point in the minute that the Chancellor of the Exchequer sent the Prime Minister on 28 July.

There is undoubtedly a strong case for the post to be graded at Under Secretary level when it is transferred to the Treasury in October 1983 on the expiry of the contract of the present Head of the Government Accountancy Service. But a lot can happen in the next two years, particularly in view of the intense Parliamentary interest now being taken in all aspects of Government accountancy. It is for this reason only - and not because of any doubts about the Treasury being the correct eventual location of the post - that I still believe that it would be prudent to review the detailed arrangements in the autumn of 1982.

I am sending copies of this minute to the recipients of your minute of 26 July.

IB

IAN BANCROFT
4 August 1981

Southern



DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB
TELEPHONE DIRECT LINE 01-2123301
SWITCHBOARD 01-212 7676

Secretary of State for Industry

28 July 1981

Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1

Committee's response
WN
3/7

Ken Gifford

WHITE PAPER ON THE ROLE OF THE C & AG

Thank you for sending me a copy of your minute of 21 July to the Prime Minister covering the text of a White Paper setting out the Government's response to the PAC's proposals on the Role of the C & AG. I recognise that this has been a difficult drafting exercise and that it is necessary to appear conciliatory while rejecting almost everything of real significance asked for by the Committee. I agree to the publication of this text on Tuesday.

2 It may be as well to set out briefly the line which I think that the Government should pursue in the debate which you foresee for the Autumn.

3 On the NEB (paras 14 and 15) I should wish no change in the audit arrangements which at present exclude the C & AG from both audit and more general scrutiny. I shall also oppose C & AG access to any new body arising from the amalgamation of the NEB and the NRDC.

4 Paragraphs 22 and 23 deal summarily with the radical notion that the C & AG should be able to pursue Government grants or loans wherever they go in the private sector. I welcome the statement that the Government "do not agree with the PAC's proposal". I should make it clear that I regard this as also rejecting any idea of C & AG access to the books of British Leyland and Rolls Royce which are not specifically mentioned in this context.

5 I am copying this letter to recipients of your minute.

Emma

Ken

CONFIDENTIAL



DEPARTMENT OF THE ENVIRONMENT

2 MARSHAM STREET

LONDON SW1P 3EB

01-212 3434

MINISTER FOR LOCAL GOVERNMENT
AND ENVIRONMENTAL SERVICES

28 July 1981

Dear Nick,

AUDIT COMMISSION: STATEMENT

Further to my letter of 22 July, I now attach the final version of the statement which Mr King will make this afternoon and which Lord Bellwin will repeat in the House of Lords.

Copies go to Mike Pattison at No 10, Murdo Maclean and Michael Pownall.

Yours,

PJC

MAF

P J CASH
Private Secretary

Nick Huxtable Esq

LOCAL GOVERNMENT AUDIT IN ENGLAND AND WALES

1. With permission, Mr Speaker, I wish to make a statement on local government audit in England and Wales. In their Report on the Role of the Comptroller and Auditor General the Public Accounts Committee made recommendations on this subject among others. The Government's response to the Committee's Report as a whole is being published today in a White Paper. Since early legislation on local government audit is proposed it was thought right to make a separate statement to the House on this.

2. The Government entirely endorse the PAC's conclusion that the present arrangements for local authority audit need to be improved and that greater attention needs to be given to value for money work. In addition, we do not believe it is right in principle that a local authority should appoint its own auditors. We also wish to see the experience of private sector accountants used in substantially greater measure in local government audit.

3. The PAC concluded that the C & AG should assume responsibility for the District Audit Service. The Government have considered this very carefully, but have decided that such an arrangement would be fundamentally inconsistent with the constitutional position of local authorities. Parliament's proper interest in monies voted as Exchequer grants to local authorities is best pursued through the accountability to Parliament of the Ministers responsible for the payment of those grants.

4. The Government accordingly propose to introduce early legislation to establish a new Audit Commission which would be responsible for the audit of local authorities in England and Wales. Its members would be appointed by my rt. hon. Friends the Secretaries of State for the Environment and for Wales, partly from local government and partly from people with relevant expertise in industry, commerce and the professions, with an independent chairman.

5. The Commission would appoint auditors to the local authorities, either from District Audit or from the private sector. It would take over from my Department responsibility for the District Audit Service. Discussions with the staff about possible transfer arrangements will start now.
6. The Commission would also subsume the functions of the Advisory Committee on Local Government Audit.
7. The Commission would not be responsible for the audit of water authorities, whose auditors would in future be appointed by the relevant Secretary of State.
8. The Commission would have powers to promote or undertake work on value for money and efficiency. It would thus cover some of the area of work of the Local Authorities Management Services and Computer Committee, and I intend to discuss this with the local authority Associations.
9. The Commission would be self-financing, primarily from audit fees, as the audit service is now. Some increase in the present scale of fees would be required to accommodate the increased audit effort.
10. A consultation paper setting out the details of this proposal is being issued today.
11. My rt. hon. Friend also intends to use his powers under the Local Government Act 1972 to appoint as additional district auditors members of private accountancy firms. We believe that their diverse experience will be helpful to local authorities facing the challenges of a period of declining resources. They will undertake the audit of the accounts for 1981-82 of a small number of authorities in England, working under the general supervision of the Chief Inspector of Audit. The authorities will be selected to give a variety of types of authority, geographical locations, and expenditure patterns. Their names will be announced in due course.

12. Mr Speaker / local government expenditure in England and Wales will be about £22,000 million this year. The need to secure value for money for such a scale of public expenditure is crucial. The Government wish to establish an audit system for the future which is well equipped to meet this need. We believe that the measures I have announced are the right way to achieve that system.



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

*NBSM per.
S. J. Bancroft min. in
response
KJ
30/7/83*

LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

I have seen a copy of Derek Rayner's minute of 16 July and like you I agree with the proposals in paragraph 25 of his minute concerning the location of the post of Head of the Government Accountancy Service. It seems to me right to take the opportunity when Mr. Sharp's contract expires to seek to unify the post with that of the Under Secretary post now in the Treasury in charge of Management, Accountancy and Purchasing Policy. No doubt if we appoint an outsider we shall need to recognise that he will expect a salary considerably in excess of that of Under Secretary, but that should not present an insuperable difficulty.

2. I note that in his minute of 17 July to Clive Whitmore Ian Bancroft suggests that it is not necessary to commit ourselves now to the precise arrangements to be introduced in 1983. I must say I have misgivings about this. If the post is to be located in the Treasury, it should be, as Derek says, to do the job he has identified and this is unquestionably an Under Secretary job. It would be quite wrong in my view to contemplate the Treasury having a post at a higher level and being unable to give the incumbent the line responsibilities he needs to make the contribution we would be expecting from him. Although the accountancy contribution to financial management is important, I am convinced it must be fitted within the overall responsibilities of the Second Permanent Secretary handling public expenditure, and should therefore be subordinate

/to him.

PERSONAL & CONFIDENTIAL



to him. If it were thought desirable to leave open the grading issue - which I recognise raises political difficulties - I think we should also leave open the final decision on whether the post should be transferred from the Department of Industry to the Treasury.

3. I am sending copies of this minute to the recipients of Clive Whitmore's minute of 26 July.

(G.H.)

28 July 1981



From the Secretary of State

Govt Mach.

Wm
27/7

CONFIDENTIAL

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer
HM Treasury
Treasury Chambers
Parliament Street
London, SW1P 3AG

27 July 1981

Dear Geoffrey,

WHITE PAPER ON THE ROLE OF THE C AND AG

Thank you for giving me an opportunity to comment upon the draft White Paper enclosed with your minute of 21 July to the Prime Minister.

The Paper's somewhat oblique approach to certain sensitive matters no doubt reflects the need, to which you refer, to seem conciliatory at the same time as rejecting much of what the PAC has asked for. I am content that it should be published on the 28th as it stands. However, I should make it clear that the NDPBs for which I am responsible cannot be broken down into neat categories and that I shall rely heavily upon the reference to ministerial review in paragraph 21 should I wish at any time to vary (in either direction) audit arrangements which are largely a matter of historical accident or practical convenience.

I am copying this letter to the recipients of yours.

Yours
John Biffen

CONFIDENTIAL

JOHN BIFFEN



FILE

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10 DOWNING STREET

From the Principal Private Secretary

SIR DEREK RAYNER

Location of the Head of the Government Accountancy Service

The Prime Minister has seen your minute of 16 July 1981 about the location of the Head of the Government Accountancy Service. She has also seen Sir Ian Bancroft's minute of 17 July.

The Prime Minister agrees with your recommendation that we should leave matters as they are until October 1983 when Mr. Sharp, the present Head of the Government Accountancy Service, comes to the end of his contract and that we should then proceed as you propose in paragraph 25 of your minute. She takes, however, the point made by Sir Ian Bancroft in his minute of 17 July and she would therefore like to review her decision in the autumn of 1982.

I am sending copies of this minute to Mr. Wiggins, Sir Ian Bancroft, Sir Douglas Wass and Sir Peter Carey.

G. A. WHITMORE

26 July 1981

PERSONAL AND CONFIDENTIAL

CONFIDENTIAL

ms

PRIME MINISTER

HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

Earlier this year you raised with Sir Derek Rayner the question of where the head of the Government Accountancy Service should be placed in the machinery of government, and the attached folder contains his response to that remit (FLAG A). His recommendation is that we should leave things as they are until October 1983 when Mr Sharp, the present Head of the Government Accountancy Service, comes to the end of his contract and that then the post should be downgraded from its present level of Second Permanent Secretary to Under Secretary and transferred from the Department of Industry to the Treasury where, with the title of Director of the Government Accountancy Service, it would head the Accounts and Purchasing Group. At the same time the Department of Industry Under Secretary who heads up the Secretary of State's accountants would be given the duty of being his accountancy adviser.

dated
17/7.

— Sir Ian Bancroft, whose views are at FLAG B, goes along with Sir Derek Rayner's solution, but he suggests that because there is a good deal going on already to improve financial management in Government and to raise the status and contribution of accountants in Whitehall, it would be wise not to decide now on the precise arrangements to take effect when Mr Sharp goes in 1983 but rather to leave over settling the details until the autumn of 1982. I think that this is sensible advice and I suggest therefore that your decision might take the form of agreeing with Sir Derek Rayner's recommendation but subject to its being reviewed in the autumn of next year. Agree ?

JW

Yes
ms

24 July 1981

CONFIDENTIAL

From: THE PRIVATE SECRETARY

WR
2/7
Gust Mack



HOME OFFICE
QUEEN ANNE'S GATE
LONDON SW1H 9AT

24 July 1981

Dear Sir

WHITE PAPER ON THE ROLE OF THE C & AG

This is just to let you know that the Home Secretary has seen a copy of the Chancellor's minute of 21 July and is content with his proposal to publish the White Paper as revised on 28 July.

I am copying this letter to the Private Secretaries to all members of the Cabinet and to David Wright (Cabinet Office).

Yours sincerely
C. J. Walters

(C J WALTERS)

P S Jenkins Esq

CONFIDENTIAL

DS



10 DOWNING STREET

From the Private Secretary

23 July 1981

Dear Peter

WHITE PAPER ON THE ROLE OF THE C & AG

The Prime Minister was grateful for the Chancellor's minute of 21 July. She is content for this White Paper to be published on 28 July, and has no comments on the Chancellor's draft.

I am sending copies of this letter to the Private Secretaries to members of the Cabinet, to Anthony Mayer (Department of Transport) and to David Wright (Cabinet Office).

yours
Willie Rickett

Peter Jenkins, Esq.,
H.M. Treasury.

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DEPARTMENT OF THE ENVIRONMENT
2 MARSHAM STREET
LONDON SW1P 3EB
01-212 3434

MINISTER FOR LOCAL GOVERNMENT AND ENVIRONMENTAL SERVICES

My Ref: H/PSO/16343/81

22 July 1981

Dear Geoffrey

WV 23/7

WHITE PAPER ON THE ROLE OF THE C & A G

Thank you for sending Michael Heseltine a copy of your letter of 15 July to Francis Pym. Subject to incorporating a reference which my officials have given to yours about our proposals for the future audit of the water authorities, I confirm that the draft deals satisfactorily with our particular interests, notably the proposed Audit Commission.

Like you I realise that the draft White Paper will not be well received by some quarters in Parliament. But I see no alternative to the main line of argument so far as nationalised industries and local authorities are concerned.

I am copying this letter to the Prime Minister, Christopher Soames, Francis Pym and Sir Robert Armstrong.

2
→
lan

TOM KING

The Rt Hon Sir Geoffrey Howe QC MP

1 Mr Pattison

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2 Prime Minister

1

Mr Heseltine will make his statement on the Audit Commission the same day.



You have already seen the Chancellor's identical letter to Mr Pym seeking his approval for this White Paper.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

Content for it to be published on Tuesday 28 July?

PRIME MINISTER

WHITE PAPER ON THE ROLE OF THE C & AG

Yes Mr WFR 21/7

.....
The purpose of this minute is to invite your agreement, and that of other Cabinet colleagues, to the publication on 28 July of the attached draft White Paper on the Role of the Comptroller and Auditor General (C & AG). The draft has been the subject of extensive consultation between Departments.

2. The White Paper replies to the PAC's Report (First Special Report, Session 1980-81) published in March on the Role of the C & AG. The PAC's central recommendation was that the C & AG should be able to pursue public funds wherever they go. This would affect, inter alia, the nationalised industries, local authorities and numerous other public and private sector bodies in receipt of Government grants and loans. They further propose that he should become an Officer of the House and subject to the direction of the PAC. His staff in the Exchequer and Audit Department (E & AD) would be expanded and turned into a new National Audit Office. This would be controlled by a Public Accounts Commission consisting of members of the House of Commons.

3. These are radical proposals. They are essentially the same as recommendations in the last Parliament by the Expenditure and Procedure Committees. Michael English and John Garrett have long advocated these changes.

4. While I find it difficult to disagree with the PAC's diagnosis of a need for improvement in our system of public aid and accountability, I find it equally difficult to agree with their remedy. On the important question of local authority audit, we have already accepted Michael Heseltine's recommendation for the



establishment of an Audit Commission for local authorities in England and Wales. As to arrangements for the efficiency audit of nationalised industries, I believe that the right course is to build on the useful work already done by the MMC. The further statement on this promised by the White Paper will be based in part on the outcome of the current CPRS review of the nationalised industries.

5. The draft White Paper therefore rejects the PAC's main proposals for expanding the C & AG's responsibilities. In it, three basic principles in support of this position are set out: audit arrangements should reflect the degree of Ministerial responsibility; private sector auditors have a valuable contribution to make to the work of many public sector bodies; and the first priority is given to ensuring that the C & AG can carry out as effectively as possible his present substantial responsibilities.

6. On the status of the C & AG, the White Paper sides with the previous PAC (under Edward Du Cann) in favour of leaving the C & AG completely independent. On control of the E & AD, the White Paper though rejecting the PAC proposal, takes a somewhat more open line.

7. On the question of more general legislation, the Green Paper acknowledged the case for a more up to date prescription of the C & AG's functions. But it noted that the need was not pressing since the E & AD Acts posed no insuperable barriers to the development of the C & AG's work. The White Paper specifically leaves open the possibility of legislation during this Parliament, but restates the view expressed in the Green Paper that there should be a consensus about its content.



8. Though the White Paper has been drafted in as conciliatory way as possible, emphasising all areas of possible agreement between the Committee and the Government, the PAC will not welcome this reply to a report which occupied a great deal of time and effort on their part. We are likely to be pressed to offer a debate in Government time in the autumn. We shall not be without counter-arguments, and we can point to positive alternative policies for the local authorities and nationalised industries.

9. We have said that we hope to publish the reply to the PAC before the recess, and I see some advantage in getting it out as soon as we can. I should be glad to know if you would be content for the White Paper to be published on 28 July.

10. As you know, I think there would be advantage on all sides in synchronising publication of this White Paper with Michael Heseltine's announcement of the Audit Commission. If that were to take place in isolation and ahead of our response to the PAC report, it could provoke an even less enthusiastic reaction from the PAC than they are likely to give to the course which I propose. My Private Secretary has written separately about this, and I understand Michael Heseltine has now agreed to postpone his announcement to make this possible.

11. In order to meet this timetable, I should be grateful if colleagues could let me have any comments by close of play on Friday, 24 July.

12. I am copying this to all members of the Cabinet, to Norman Fowler and to Sir Robert Armstrong.

Robert Jenkins

for (G.H.)

21 July 1981

(Approved by the Chancellor of the Exchequer and signed in his absence).

DRAFT

WHITE PAPER ON THE ROLE OF THE C & AG

1. In their First Special Report⁽¹⁾ for the 1980-81 Session, the Committee of Public Accounts (PAC) make a number of recommendations for extending the scope of the work of the Comptroller and Auditor General (C & AG) and his staff in the Exchequer & Audit Department (E & AD), and for changing their status. The PAC took as their starting point the Government Green Paper (Cmnd 7845) published a year earlier, and recommendations on the same subject by the Expenditure, Procedure, and Public Accounts Committees of the last Parliament.⁽²⁾

2. This White Paper sets out the conclusions which the Government have reached after careful consideration of the Committee's Report and the substantial body of evidence submitted to the PAC in connection with their enquiry.

I THE GENERAL ISSUES

3. The Government's general approach to the Committee's Report is based on three guiding principles which the Government believe must be taken into account in determining the role of the C & AG. The first is the principle of Ministerial responsibility to Parliament, set out in the Green Paper. This constitutional convention does not fit all cases neatly but remains the only effective means by which Parliament can hold to account those to whom money is voted.

4. The second principle is the need for high standards of financial stewardship and prudence in handling public money. The Government agree with the many comments on the Green Paper in this sense, and recognise the contribution which can be made to this by audit in all its forms. But the Government do not share the Committee's implicit view that, apart from internal audit, this contribution should be made for the whole of the public sector predominantly by the C & AG. It is beyond question that the private sector accountancy profession has the competence to do such work, bringing to it a wide variety of commercial and industrial experience, and this is of great value to the audit of many public sector bodies.

(1) 'The Role of the Comptroller and Auditor General' (HC 115)

(2) Eleventh Report from the Expenditure Committee, Session 1976-77, (HC 535)
First Report from the Select Committee on Procedure, Session 1977-78, (HC 588)
Second Special Report from the Committee of Public Accounts, Session 1978-79,
(HC 330)

5. The third principle derives from the evidence that standards of audit, both external and internal, of Government Departments require improvement. The Government wish to work with the PAC and the C & AG to achieve this. The scope for achieving this improvement will be reduced if the C & AG's work is extended into large new areas of administration with which his Department is at present unfamiliar. The first priority, in the Government's view, is to ensure that the C & AG is able to carry out his present substantial responsibilities as effectively as possible.

New Legislation

6. It remains the Government's view that it would be useful to introduce legislation to provide an up to date prescription of the C & AG's functions. But this is not a pressing need. Experience of the past two years suggests that the existing legislation need not in fact inhibit further desirable changes in the work of the C & AG and the PAC.

7. The Government will keep under review the possibility of legislation within the lifetime of this Parliament.

II THE NATURE OF THE C & AG's AUDIT

8. The Government agree with most of the Committee's comments and conclusions in Chapter 2 of the Report about the nature of the C & AG's audit. They welcome the Committee's endorsement of the systems-based approach for audit reporting in the field of value for money (VFM) examination. The Government think the Committee are right to say that VFM investigations by the C & AG should be audit-based. The Committee's discussion of effectiveness audit shows that there is agreement on the important point that the C & AG should refrain from raising the merits of policy objectives.

III THE RANGE OF THE C & AG's AUDIT

9. The recommendation that "new legislation should establish the principle that the C & AG should either audit, or have access to, the books of all bodies in receipt of money voted by Parliament"⁽³⁾ is applied by the PAC to nationalised industries, other public corporations, local authorities, non-departmental public bodies, and many commercial bodies

(3) HC 115, para. 8.8

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in the private sector. The Government agree that an essential part of the role of the C & AG is to ensure accountability to Parliament for public money, but as mentioned above they wish to see more, not less, involvement of the private sector in the audit of public spending, and to avoid over-loading the C & AG. They believe that in defining the range of activities of the C & AG account should be taken of the principle and extent of Ministerial responsibility to Parliament. Audit arrangements should reflect the constitutional relationships between central government and the various bodies in receipt of public funds. Accountability to Parliament cannot be created simply by changing the auditing arrangements.

(a) The Nationalised Industries and Other Public Corporations

10. The Government fully share the PAC's concern about the need to promote the efficiency of the nationalised sector. Not only do the nationalised industries represent a significant proportion of the economy, but to a considerable extent they are insulated from competitive pressures. For this reason Parliament recently legislated (in the Competition Act 1980) to allow the Monopolies & Mergers Commission (MMC) to undertake efficiency investigations into the nationalised industries. The MMC has made a good start. Their investigations, of which 4 have been completed in the last 12 months, have identified a number of areas of weakness in the industries' operations.

11. The Government are not convinced that it would be fruitful to replace this framework so soon after its inception. The better course in their view is more vigorous use of the instruments that already exist. With this in view the Government are considering how the role of the MMC in the field of efficiency audit can be strengthened and supplemented. A further statement will be made in the near future.

12. As the auditor of the accounts of the sponsor departments, the C & AG has access to reports submitted by the MMC, and by the industries' auditors to the responsible Ministers. He can report on any inadequacies in the monitoring and control arrangements, and in the scope or validity of the information available to those Departments. The Government would welcome PAC examination, on the basis of C & AG reports, of departments' exercise of their responsibilities in this area. But they do not think the case has been made out for the further step, at this stage of development of arrangements for efficiency audit of the industries, of involving the C & AG directly in the industries' affairs. They note that to extend his role in the way envisaged by the PAC would result in a substantial increase in the work of the C & AG and his Department in a novel area.

13. Similarly, the Government do not favour systematic extension of the C & AG's role to the water authorities or to other public corporations. As regards the Water Authorities in

England and Wales, the Government propose that they should in future be audited by private sector auditors appointed by the Secretaries of State and not, as at present, by District or approved auditors. But they agree with the PAC that the fact that a body's activity is in whole or part commercial in character is not in itself an obstacle to giving the C & AG any form of audit responsibility for the body's accounts.

(b) The National Enterprise Board (NEB)

14. Under its present guidelines, the NEB is required to work in partnership with private sector capital wherever possible. Its operations depend for their effectiveness on co-operation and free exchange of commercially sensitive information with private sector companies and investors. The prospects for such co-operation would be impaired if the C & AG were to be given access to the books and records of the NEB.

15. The Government have announced recently their intention of bringing the NEB and the National Research Development Corporation closer together. If this leads to their eventual amalgamation, the question of accountability of any new body to Parliament will be considered when legislation is prepared.

(c) Local Authorities

16. The Government agree with the Committee that some reform is needed of the arrangements for local authority audit, but do not believe that the right solution is to put the District Audit Service under the control of the C & AG. For those functions relating to local authority activities for which Parliament has given them responsibility, Ministers are already fully accountable to Parliament. The Government do not consider that the C & AG needs for that purpose access to more information than is available to the Departments under audit.

17. The Government attach particular importance to the value for money content of local authority audit, and agree with the PAC about the desirability of further developing co-operation on technical matters between the District Audit Service and E & AD. The Government see an important role in local authority audit for auditors with private sector experience. They believe that the interests of all parties concerned, including local electorates, will best be served by the establishment of an Audit Commission for local authorities in England and Wales, ^{as} has been announced separately [today] by the Secretary of State for the Environment. The C & AG can be associated with the work of the Audit Commission as he is now with that of the Advisory Committee on Local Government Audit. The Government propose that present arrangements for the Commission for Local Authority Accounts in Scotland should continue but will wish to consider in due course whether experience of the new arrangements in England and Wales suggests that the arrangements in Scotland should be reviewed.

(d) Non-departmental Public Bodies (NDPBs)

18. Most NDPBs are advisory or judicial and do not spend money on their own account; in almost all cases their expenses are borne on the Votes of their sponsoring Departments and are therefore audited by the C & AG. It is only a minority of bodies which spend money on their own account; they generally exercise executive functions and are listed as "executive bodies" in 'Non-Departmental Public Bodies: Facts and Figures 1980' (HMSO, 1981). Paragraphs 19 to 21 below apply only to these bodies, apart from the water authorities and the NEB which are considered separately in paragraphs 13-15.

19. Irrespective of their functions, size and the degree of Ministerial control over these bodies, the Government are determined that all of them should achieve high standards of effectiveness, efficiency and economy. They recognise and welcome the contribution which the C & AG can make to achieving these standards and to proper accountability to Parliament.

20. The Government agree generally with the approach suggested by the PAC concerning NDPBs,⁽⁴⁾ but doubt the need to give the C & AG formal audit responsibility for all bodies mainly or wholly financed by Government. In many cases the requirements of accountability to Parliament are adequately met by existing arrangements under which the C & AG has access to the books of the bodies concerned without requiring him to undertake full certification audit. These arrangements have permitted the establishment of useful links between the bodies and their private sector auditors.

21. Most NDPBs are already subject to C & AG audit or access. In some cases, Parliament has specifically prescribed commercial audit by legislation. Ministers will, however, be conducting periodic reviews of the bodies they sponsor and will consider in the course of these reviews whether audit arrangements are satisfactory.

(e) Private Sector Recipients of Government Grants and Loans

22. The Government do not agree with the PAC's proposal that the C & AG should have access, "where he considers it necessary",⁽⁵⁾ to the books and records of private sector companies in receipt of Government grants or loans. Should the C & AG and his staff become involved in this way, such companies would be understandably concerned about disclosure of details of their commercial affairs.

(4) HC 115, Ch.3 and paras. 8.10(a) and (b)

(5) HC 115, para. 8.10(d)

23. The C & AG has access to departmental files in the course of his audit and can consider papers relating to companies receiving public funds. He is therefore already able to examine reports made by private sector accountants whom Departments may employ in assessing requests for support from private sector companies. Since Departments monitor the use companies make of loans and grants, he can also report on this aspect of Departments' activities.

(f) National Health Service

24. As the PAC recognised, the "statutory auditors" of the NHS are an integral part of the oversight of the NHS by the Accounting Officers of the Health Departments. If the "statutory audit" were transferred to the C & AG as the PAC recommend, the Health Departments would have to make other arrangements to enable this oversight to be exercised, thus in large measure duplicating the C & AG's work. The C & AG already has access to NHS papers at all locations enabling him to pursue his enquiries where he wishes. The Government agree that there should be the fullest co-operation between the staffs of the E & AD and the "statutory audit", but are not persuaded of the case for more fundamental changes.

IV THE STATUS OF THE C & AG AND OF HIS STAFF

25. The PAC proposed that the C & AG should become an Officer of the House appointed by the Queen by letters patent on the recommendation of the House of Commons; that the PAC should be able to give the C & AG directions to investigate particular programmes or projects; that the existing staff of E & AD and the District Audit Service should become servants of the House and transformed into a new National Audit Office; and that a Public Accounts Commission of the House should be established with responsibility for, among other things, determining the number of staff in the National Audit Office and their pay and conditions of service.

26. The Government are not convinced by the PAC's proposals as to the status of the C & AG or as to the question of powers to give him directions. There are as good reasons in the public sector as in the private sector for regarding independence as one of the essential attributes of an auditor. The Government believe that within the framework of specific legislative provision the C & AG should continue to be totally independent of any form of external influence or direction in the performance of his duties. The C & AG himself expressed this view in evidence to the Committee. The same view was taken by the PAC of the last Parliament.⁽⁶⁾ The PAC already have a working relationship with the C & AG which

(6) Second Special Report from the Committee of Public Accounts, Session 1978-79, (HC 330), para. 15.

CONFIDENTIAL

has proved effective over many years and to which both the Government and the Committee attach considerable importance.

27. The established method of appointment of the C & AG is by letters patent by the Queen on the advice of the Prime Minister. The Government are not persuaded of the case for changing it, but reiterate their view that when a new appointment is in contemplation, it will be appropriate for the Government to consult the Chairman of the PAC. This was done in regard to the new appointment recently announced.

28. In the Green Paper, the Government said that they would be ready to consider some form of control by the House of Commons Commission as an alternative to the oversight of the C & AG's budget and the staffing costs of E & AD currently exercised by the Civil Service Department (CSD). That remains their position, but the Government consider that the balance of advantage lies in retaining the present arrangements. As the Committee acknowledge, the E & AD have been exempted from the recent cuts in Civil Service numbers; indeed, the C & AG has reached agreement with the CSD on a substantial programme to increase staff numbers over the next five years to enable the Department adequately to fulfil its existing responsibilities. The Committee acknowledges that the present administrative arrangements work.

CONFIDENTIAL



PRIVY COUNCIL OFFICE
WHITEHALL, LONDON SW1A 2AT

Chancellor of the Duchy of Lancaster
and
Paymaster General

21 July 1981

Dear Geoffrey,

WM
2/7

WHITE PAPER ON THE ROLE OF THE C & A G

You wrote to me on 15 July enclosing a draft of a White Paper in response to the First Special Report (Session 1980-81) of the Committee of Public Accounts.

I am in general agreement with the line taken in the draft White Paper.

I have only two comments:-

- (i) In paragraph 7, whilst I agree there may well in due course need to be a debate on these proposals, I would not have thought it necessary at this stage to go beyond a general undertaking to keep under review the possibility of legislation. This might perhaps be incorporated at the end of para 6. The remainder of paragraph 7 might, I suggest, be omitted.
- (ii) In the last sentence of the second paragraph on page 3 of your letter you appear to suggest that we might at a later stage consider a concession to bring the staff in E & A D formally under Parliament. I do not believe this would be welcome to the House of Commons Commission, for whom it would be a major extension of their staffing responsibilities. Nor do I see another House Commission coping with the job. It might also prove contentious with the staff concerned. I would hope, therefore, that our position would remain as stated at paragraph 28 of the draft White Paper.

I am copying this to the recipients of your letter.

Francis Pym
Francis Pym

FRANCIS PYM

The Rt Hon Sir Geoffrey Howe QC MP
Chancellor of the Exchequer



Mr Lamberton

Wm 20/7

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

17 July 1981

in this office
→

D.A. Edmonds, Esq.,
Private Secretary
Department of the Environment

R 20/7

Dear David

MAD 20/7

AUDIT COMMISSION : DRAFT STATEMENT

- with request if required

You copied to me your letter of 16 July to Nick Huxtable.

As you know, the Chancellor of the Exchequer is currently seeking the agreement of the Chancellor of the Duchy and the Prime Minister to putting to Cabinet a draft White Paper on the Role of the C & AG, with a view to publication before the Recess. The date we provisionally have in mind is 28 July.

The Chancellor recognises that, other things being equal, your Secretary of State would prefer a longer gap between announcement of the Audit Commission and the Recess. But he thinks it would make a bad impression on the House if the announcement of the Audit Commission and publication of the White Paper cannot be synchronised. If the Audit Commission is announced in isolation, the PAC will be doubly annoyed: by rejection of one of their main recommendations (which was the subject of protracted and difficult debate within the Committee), and by the apparent discourtesy of announcing the Government's conclusion before we are ready to present that conclusion in the context of a considered response to the PAC's Report as a whole.

An incidental advantage of synchronising the two events is that it would then be possible to shorten your Secretary of State's draft announcement a bit, e.g. most of paragraphs 5 and 10 duplicate the draft White Paper.

I understand the House is unlikely to rise before 31 July. The Chancellor of the Exchequer would be grateful in these circumstances if your Secretary of State could reconsider his proposal to announce the Audit Commission on 21 July.

W

/I am



I am copying this letter to Tim Lankester at No.10,
to Nick Huxtable in the Chancellor of the Duchy's Office,
to the Private Secretaries to the Secretary of State for
Wales, the Chief Whip and Sir Robert Armstrong.

Yours ever,
Peter

P.S. JENKINS

Mr RICKETT

LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE
(HOTGAS)

1. Sir Derek Rayner would not regard the attached minute as having a strong claim to very early attention by the Prime Minister. It results from Mr Pattison's minute to Mr Colman of 30 January (on the CSD/Treasury merger). It follows a brief word Sir DR recently had with the Chancellor and consultation with Sir Ian Bancroft, Sir Douglas Wass and Sir Peter Carey, who is the official boss of HOTGAS, Mr Kenneth Sharp.

2. You will see that the issues are both personal and intellectual. The key points are these:

(1) The development of financial management in Government, which has generally been slow, is gathering momentum. The Treasury is the obvious lead Department. A good HOTGAS would help - and would help better if he were located in the Treasury.

(2) In fact, however, we have double faulted:

a. The emphasis placed on accountancy over the last ten years has to a degree been right, but it has blurred the primacy that should have attached to financial management, of which accountancy is only one part.

b. Although the post of HOTGAS was created in 1973 at Second Secretary level, it took two years for an acceptable candidate (Mr Sharp) to come forward. The post was not then and probably would not now be attractive to accountants of good success in the private sector. Mr Sharp himself,

although likeable and well-being^{meaning}, is not very good. He has neither the professional background nor the intellectual capacity to make a substantial contribution to the development of financial management. Although the Service has almost certainly not helped him as much as it should, there is little prospect that Mr Sharp will become more effective.

- (3) The substantive question of the function and location of the HOTGAS post is therefore tied up with the personal question of Mr Sharp himself. His contract was renewed last autumn and runs through to October 1983. Experience suggests that his post is over-graded by at least one grade. It should almost certainly be in the Treasury rather than in the Department of Industry as now. But the option of ending Mr Sharp's contract and putting his post, much down-graded, into the Treasury would both seem and be unfair to him as well as causing trouble for the Government outside.
- (4) There are two other options:
- a. To leave things alone until October 1983, but to take Mr Sharp more firmly under the Treasury's wing; or
 - b. To decide not to renew his contract in 1983 (when he will be nearly 57) and plan to move the post, if still needed but almost certainly re-graded, into the Treasury.
- (5) The minute asks the Prime Minister to authorise Sir Douglas Wass to implement option (b) above.



3. If the Prime Minister agrees, you might like to reply somewhat as in the attached draft.

SP

: C PRIESTLEY
17 July 1981

Encs: Minute to the Prime Minister from Sir Derek Rayner
Draft minute from you to Sir Derek Rayner

CONQUEROR

DRAFT OF 16 JULY 1981



PERSONAL AND CONFIDENTIAL

Sir Derek Rayner

LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

1. The Prime Minister was grateful for your minute of 16 July.
2. The Prime Minister believes that the fairest course would be to retain Mr Sharp's services until the end of his contract in October 1983 and to consider in the interim what arrangements should be made thereafter. She would be grateful if Sir Douglas Wass would undertake this as you suggested.
3. The Prime Minister is in general agreement with the course suggested in para. 25 of your minute, namely that the post of Head of the Government Accountancy Service should be transferred to the Treasury and be down-graded, but she would like the matter to be referred to her again before decisions are taken so that she can see how the change fits in with the broader strategy for developing financial management.
4. I am copying this to Mr Wiggins in the Chancellor's office and to Sir Ian Bancroft, Sir Douglas Wass and Sir Peter Carey.

W F S RICKETT



MR C A WHITMORE

LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

I have seen Sir Derek Rayner's minute of 16 July.

I am grateful to Sir Derek for reflecting my views in his minute, especially on the difficulties that would be caused by an immediate downgrading of Mr Sharp's post from Second Permanent Secretary to Under Secretary. I share his preference for the third option - a change in 1983, when the post would be relocated in the Treasury. I also agree that we should need to think carefully about the grading of the post and whether it should be filled by an outsider.

I have one additional comment. I doubt whether it is necessary to commit ourselves now to the precise arrangements to be introduced in 1983. As you know, a good deal of action is taking place to improve financial management in Government and to raise the status and impact of accountants. Developments over the next year may influence the shape of the 1983 solution. I therefore suggest that a final, precise decision on this point should be left open until the autumn of 1982.

I am copying this minute to the Chancellor of the Exchequer, Sir Derek Rayner, Sir Douglas Wass and Sir Peter Carey.

MB

IAN BANCROFT
17 July 1981

PERSONAL AND CONFIDENTIAL

PRIME MINISTER

LOCATION OF THE HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

At the end of January you raised the question of the siting of the Head of the Government Accountancy Service in the machinery of government. In order to offer advice, I have had to take into account work in hand, and its progress, including the transfer of Accountancy, Finance and Audit Division (AFA) from CSD to the Treasury.

2. This minute is therefore submitted to you in the context of continuing work to improve the quality of financial management in Government. I have consulted Sir Ian Bancroft, Sir Douglas Wass and Sir Peter Carey during its preparation and I have also had a personal word with the Chancellor of the Exchequer.

BACKGROUND

3. The HOTGAS post was created in 1973 at Second Permanent Secretary level but it took two years to fill it (see below). It is primarily non-executive. It has two main functions, to provide a "head of profession" for the Government Accountancy Service (on similar lines to the Government Economic and Statistical Services) and an Accountancy Adviser to the Department of Industry, where it is located. More details are given in the Annex, should you need them.

4. When the post was created, two years of advertising failed to produce a suitable candidate. Sir Ian Bancroft recalls the relief felt when the present incumbent, Mr Kenneth Sharp, came forward in 1975 "with glowing references from his professional peers". Mr Sharp had been a partner with a firm of accountants (Messrs. Armstrong, Watson and Co of Carlisle) for 20 years and was president of the council of the Institute of Chartered Accountants in 1974-75.

5. Sir Ian Bancroft tells me that the memory of the original difficulties in filling the post was still strong when the question came up whether Mr Sharp's contract, initially for 5 years, should be renewed. The offer of appointment made to Mr Sharp in 1975 had held out the expectation that the appointment could be extended, while making no commitment. Sir Ian Bancroft and Sir Peter Carey say that the problems of attracting a good outside applicant at Civil Service pay rates, coupled with Mr Sharp's own desire to see his organisational changes through, pointed towards the renewal of his contract for another three years. This was done last October.

"FINANCIAL MANAGEMENT" IN THE CIVIL SERVICE

6. Sir Douglas Wass and I are at the moment addressing some fundamental questions in this area, namely, "What is financial management in Government? Who are the financial managers in departments? What skills do they need? How are these best provided through training and experience?"

7. Put in the simplest terms "financial management" in Government consists of:

- (1) the common rules and procedures of public expenditure control and Parliamentary accounting which apply to all departments alike; and
- (2) the many different businesses which take place in departments. For example, the social security side of DHSS, the procurement side of MOD and the industrial sponsorship side of DOI or DEN are as different from each other as are insurance, manufacturing and retail in the private sector.

8. The staff of the central finance branches in spending departments are not and cannot be the only "financial managers". A Minister in charge of a department has to look to the staff of his policy and operational branches to take the main responsibility in such matters as:

- assessing the likely cost and "value added" of new policy proposals
- assessing the "value added" by existing policies
- saving Ministers from getting taken for a ride by private or public sector organisations seeking funds for investment or survival
- getting and responding to their own running costs
- monitoring and controlling the outflow of cash
- securing the timely delivery to Government of the goods and services it is procuring.

9. The professional accountant has an important part to play in devising and in running a good system of financial management, especially with regard to the supply of management information. But accountancy and the accountant do not have all the answers. In a private company, the Chief Accountant will be auxiliary to the finance director. Although in Britain the finance director will usually have trained as an accountant, his function now clearly extends to contributing to profits and the creation of wealth, rather than being limited to historical accounting. No responsible board could now accept that their collective financial duties could be serviced only by a technician.

WHAT IS HOTGAS'S PART IN FINANCIAL MANAGEMENT?

10. The Treasury is leading for you on your policy of better financial management, one key aspect of which is training. I myself would now look for a strong development of financial management as a specialism within the civil service.

11. The emphasis placed on accountancy over recent years is valuable. But it has blurred the primary importance of analysing the skills needed for financial management in the special circumstances of government and of providing a strong corps of financial managers.

12. I have commissioned a statement of training policy and a plan, consisting of particular objectives for giving it effect. Although the Treasury is the leading department, I envisaged that HOTGAS should have a part to play because:

- (1) Accountancy is an important part of financial management for which the Treasury has the overall responsibility.
- (2) As indicated in the Annex, HOTGAS's remit includes advising departments on financial management and control.
- (3) His position as "head of profession" should give him such a wide overview of financial management in practice - its strengths, weaknesses and the skills needed for success - that the Treasury could only benefit from his help and could not afford not to put its weight behind him.

13. I therefore invited HOTGAS to draft the statement and plan, which he gladly and enthusiastically agreed to do. I saw this somewhat unorthodox approach as one which had the

merits of leaving the Treasury in charge but also of tapping HOTGAS's particular knowledge and experience, which I believed should be in the Treasury in any case.

14. Unhappily, HOTGAS's approach to the policy statement and plan, although prompt, does not suggest that he finds it easy to look beyond the role of the accountant or to describe in practical terms the skills required for good financial management which can be taught or otherwise acquired.

15. The stage now reached is that the Treasury will instead draft the statement of policy, beginning with an analysis of "financial management" and "financial managers" and that HOTGAS will draft on training objectives.

16. This experience has left Sir Douglas Wass and me with these thoughts:

- (1) The policy lead on financial management is correctly placed in the Treasury
- (2) Within the Treasury, the responsibility is correctly placed on the Public Services Sector, now headed by Sir Anthony Rawlinson, since it has both the practical job of exercising control over public expenditure and the important complementary job of promoting developments in the field of financial management.
- (3) Within the Public Services Sector, the responsibility is correctly delegated to Mr J G Littler, Deputy Secretary; his charge includes the Treasury's accountants in the Accounts and Purchasing Group, and more recently those in the Accountancy, Finance and Audit Division (AFA) transferred from CSD.

- (4) The Treasury has a need for a strong input from professional accountants, not only in the field of overseeing and advising on the financial systems maintained by Departments, but also of approving public sector projects, vetting the disbursement of public funds on commercial activities etc. In recent years it has been stepping up this input. But the level at which it is best made is broadly Assistant Secretary or Principal.
- (5) The head of the GAS should be in charge of developing the profession, as now, and of a group of accountants, so that he has management responsibilities and his feet stay on the ground.
- (6) Because accountancy is one part of financial management, a case can be made for putting the head of profession in the Treasury, where he should help the Specific and General Expenditure divisions in their work; take responsibility for the Accounts and Purchasing Group and AFA; take the lead in developing internal audit; and contribute to the general improvement of financial management.
- (7) The function summarised in (6) is not that of a Second Secretary in the Treasury. It is nearer that of an Under Secretary. This makes the appropriate job comparison with private sector practice (see para. 9 above); the "head of accountancy" must, in our view, look to the Second Secretary Public Services for policy direction and guidance.

THE FUTURE OF THE HOTGAS POST

17. Judging by the contribution it appears to be making and indeed could make the HOTGAS post is over-graded by at least one grade. But the heads of the Government Economic and Statistical Services are also at Second Secretary level. Downgrading the post might cause morale problems in the GAS and markedly adverse criticism outside Government. This is not an overriding consideration, but it should be recognised. Sir Ian Bancroft also believes that, presentational points apart, downgrading the HOTGAS post by one or perhaps two grades would make it harder to push through the re-structuring of the Government Accountancy Service, on which Mr Sharp has spent much of his time and which represents a degree of achievement by him.

18. The present incumbent is ill-fitted to make a bigger contribution by his business experience, which is limited to a provincial professional practice. Although personally agreeable and pleasant, he lacks the intellectual edge needed at his level and by the importance of the subject. But his contract was renewed last autumn and does not expire until October 1983.

19. There are three possible courses as follows.

(1) Leave things as they are

20. We could clearly leave things as they are and make the best of them. This is the least troublesome course. It would require that, although left in the Department of Industry, HOTGAS should be brought into closer touch with the Treasury and encouraged to make a contribution to financial matters generally but that he should mainly concentrate on the management of the GAS and offer advice on policy when it is needed.

(2) Termination of contract

21. At the other extreme, we could grasp the nettle and end Mr Sharp's contract. This would be difficult, as it would have to be done on the grounds of a personal failure less than a year after renewing his contract until October 1983 and within a year of bringing the GAS into being (in 1982). It would certainly mean compensation, possibly a tribunal, although the sweetener of an honour appropriate to the rank of Second Secretary might help.

22. The full logic of this second course would be to remove the HOTGAS post to the Treasury; downgrade it by two grades to Under Secretary; re-title it "Director of the GAS"; and put it in charge of the Accounts and Purchasing Group, including AFA. As that Group is now headed by a generalist Under Secretary, it would be desirable either

(1) to recruit from outside the Service a temporary occupant for the post with appropriate qualifications and experience, in the meantime bringing on one of the accountants already in the Service to succeed him; or

(2) to put in the post an existing official with the right qualifications, experience and aptitude. (Such a person might be Mr Peter Kemp, the Under Secretary in charge of the Treasury's central unit, a very able chartered accountant who entered the Civil Service in mid-career. He chaired the official working group which helped me greatly on repayment for property services.)

23. In business, I would favour this second course and putting Mr Kemp in charge. But we are not dealing with a

business here. An apparently tough, apparently unfair, handling of the situation could cause trouble for the Government in Parliament, the media, the accountancy profession inside and outside Whitehall and the relevant civil service trade union, the Institute of Professional Civil Servants. Sir Ian Bancroft believes that, rightly or wrongly, it would be seen as a step backwards and would be attacked as lowering the status of accountants in Government just when it should be raised.

(3) Make a change in 1983

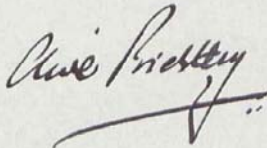
24. We might leave things as they are on the basis noted in para. 20 above but plan a substantial change in arrangements to take effect on Mr Sharp's end of contract in October 1983. The aim would be to have taken a decision well before October 1983 whether there is a continuing need for the post of HOTGAS, in particular for the work now done by Mr Sharp as head of profession.

25. If it was decided that the post was still needed, careful thought would need to be given to its grading and whether it either should or could be filled by an outsider. My own view is that the following steps should be taken:

- (1) Downgrade the post of HOTGAS to Under Secretary and convert it into a post of (say) "Director of the GAS". It would head up the Accounts and Purchasing Group (including AFA) in the Treasury and would be marshalled under the appropriate Deputy Secretary now Mr Littler.
- (2) Give the DOI Under Secretary who heads up the Secretary of State's accountants the duty of being his "Accountancy Adviser".

26. In the circumstances the correct course is one such as that outlined in para. 25 above. If you agree, Sir Douglas Wass will make the necessary arrangements in consultation with Sir Ian Bancroft and Sir Peter Carey.

27. I am copying this to the Chancellor of the Exchequer, Sir Ian Bancroft, Sir Douglas Wass and Sir Peter Carey.



DR
Derek Rayner
16 July 1981

Prepared by Sir Derek Rayner before his departure for Canada and submitted on his instructions.

Enc: Annex

FUNCTIONS OF THE HEAD OF GOVERNMENT ACCOUNTANCY SERVICE

1. The post has two main functions, to be "head of profession" for the Government Accountancy Service and Accountancy Adviser to the Department of Industry.

2. The aspect of "head of profession" work which has taken most of HOTGAS's time and energy has been bringing the "Government Accountancy Service" into being. The plan is, next year,

- (1) to merge the Professional Accountant Class (consisting of nearly 400 qualified accountants) with the Administration Group (which includes some 250 management accountants, mainly in MOD);
- (2) so to establish within the Administration Group a functional specialism, to be called the "Government Accountancy Service", consisting of staff who are now or usually employed in jobs making use of their professional qualifications; and
- (3) to give HOTGAS a small management unit to promote co-operation between departments on recruitment, training, personnel management and similar issues.

3. The proposals for an "Accountancy Service", so headed, derived from a report by Sir Ronald Melville and Sir Anthony Burney on the use of accountants in the Civil Service (published July 1973). The report, and the job specification, also envisaged that HOTGAS would advise departments on such functions of financial management as the provision of financial information in the formulation of policy; the internal control of expenditure; and the financial aspects of procurement.

4. In fact, that part of the role has not developed strongly. Nor, as I understand it, has the role of Accountancy Adviser to the Department of Industry. This job was intended to consist of:

- advice on accountancy and related management techniques
- contributions to high level planning and policy work
- responsibility for the department's 80 accountants, now deployed as a common service for the Departments of Trade and Industry, under an Under Secretary.

Prime Minister

wm
20/7/81

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

The draft white paper rejects the PAC's recommendations for extending the C & AG's responsibilities, for transferring the ExAD into an Audit Office, and for bringing the new system under tighter

15 July 1981

The Rt. Hon. Francis Pym, MC MP
Chancellor of the Duchy of Lancaster

Dear Francis

mf

control. But it will promise a further Statement on building up the role of the name, and the establishment of an Audit Commission for Local Government.

wm
16/7

WHITE PAPER ON THE ROLE OF THE C & AG

.... We have said in the House that we expect to publish a White Paper on the Role of the C & AG before the Recess. I enclose a draft. Before circulating it to Cabinet colleagues I should bring to your attention certain aspects which will be of particular interest to you.

The White Paper responds to the PAC's report (First Special Report, Session 1980-81) published in March. That in turn commented on the Government's Green Paper (Cmd 7845) of March 1980.

The C & AG's present responsibilities are concerned mainly with the audit of central Government Departments, though they also embrace a number of non-departmental bodies. He is constitutionally independent of both Executive and Parliament.

The PAC want to extend his responsibilities to the whole of the public sector, including nationalised industries and local authorities, and beyond that to many bodies in the private sector. Their concern is with accountability to Parliament, and they argue that the C & AG should be empowered to follow public money wherever it goes.

They propose that the C & AG himself should become a servant of the House, and subject to direction by the PAC. His staff in the Exchequer and Audit Department (E & AD) would be increased in numbers, and would be transformed into a new National Audit Office which would also be brought under direct control of the House of Commons and managed by a new panel of backbenchers to be called the Public Accounts Commission.

/The PAC



The PAC proposals are radical. Similar proposals were put forward in the last Parliament by the Expenditure and Procedure Committees. John Garrett and Michael English have been exponents of these ideas in recent years.

The central thesis is plausible, but I do not believe the PAC's proposals would contribute to the efficiency of the public sector. In the important cases of nationalised industries and local authorities, they are right to say that there is a need for more public accountability. But I question whether the E & AD, even if strengthened and enlarged, is the right body for efficiency audit of the nationalised industries; we already have the MMC for that purpose and I would prefer to build on that. The White Paper promises a further statement on this in the near future: the idea is that this will be based on the outcome of the current CPRS review of the nationalised industries and of some further work that is being done by the Official Committee on Nationalised Industry Policy. Similarly, as regards local authorities, E Committee have accepted Michael Heseltine's alternative of building on the existing instruments of audit by establishing a new Audit Commission for local authorities in England and Wales.

The draft White Paper therefore rejects the PAC's main proposals for extending the range of the C & AG's activities. It sets out three basic reasons for doing so - the audit arrangements should reflect the degree of Ministerial responsibility; private sector auditors have a valuable contribution to make in the public sector, and their contribution should be increased; as a first priority, the C & AG should be able to carry out his present responsibilities as effectively as possible.

The PAC's proposals would lead to a substantial shift in the balance of power between Parliament and the Executive, and within that the Committee is seeking to extend itself at the expense of other Select Committees, and to fill the gap left by the demise of the SCNI. The PAC suggest that it would have to increase the number of its members, and one could foresee sub-committees being formed, for example on nationalised industries and local authorities, to meet the increased workload.

You will also be concerned about the proposal that the PAC should have power to give directions to the C & AG. The PAC recognised that this raised the question whether the E & AD should be available to assist other Select Committees, and concluded that the PAC alone should have the power of direction, while leaving open the possibility that it would use that power on behalf of other Committees. This has implications for the staffing of E & AD and relations between



E & AD Departments. From the point of view of the Select Committee system, it raises in another form the relations between the PAC and other Select Committees, and perhaps more important the implications of giving other Select Committees access to the substantial and experienced staff of the E & AD.

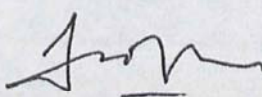
The draft White Paper rejects this proposal, and the case for bringing the C & AG, and his staff in E & AD, formally under Parliament. The previous PAC, under Edward Du Cann, took the opposite line to their successors. I believe the previous Committee were right. As well as the reasons given in the draft White Paper, I am not, as you know, impressed by the way in which Parliament manages the staff already on its pay-roll, so that I should be reluctant to see a growth in that direction. The C & AG has written to me arguing against a power of direction. If it was necessary in debate I think that we could consider some concession in respect of the staff in E & AD, although change would, in any case, require legislation.

The Green Paper argued that it was desirable to update the Exchequer and Audit Acts, but said that if the role of the C & AG was not to be fundamentally changed, the need for new legislation was not pressing. The PAC's proposals would, of course, require wholesale revision to the legislation. The White Paper says that the Government leaves open the possibility of legislation during this Parliament, but that there should first be a substantial consensus about its content; and other developments in Parliamentary procedure will need to be taken into account.

We shall have to offer a debate on the draft White Paper in Government time, presumably in the autumn. While the White Paper has been drafted to avoid confrontation with the PAC as far as possible, and to emphasise the areas of agreement, it will be clear that it substantially rejects the views of the PAC. Those views may attract support. Other Committees have previously put forward similar proposals. However, I believe that the PAC's proposals are not the right way to improve efficiency in the public sector, and we shall have sound alternatives to offer for the nationalised industries and local authorities.

I should be grateful to know that you are content with the line the draft White Paper takes on these matters.

I am copying this letter to the Prime Minister, Christopher Soames, Michael Heseltine and Sir Robert Armstrong.

G —


DRAFTWHITE PAPER ON THE ROLE OF THE C & AG

1. In their First Special Report⁽¹⁾ for the 1980-81 Session, the Committee of Public Accounts (PAC) make a number of recommendations for extending the scope of the work of the Comptroller and Auditor General (C & AG), and for changing his status. The PAC took as their starting point the Government Green Paper (Cmnd 7845) published a year earlier, and recommendations on the same subject by the Expenditure, Procedure and Public Accounts Committees of the last Parliament.⁽²⁾
2. This White Paper sets out the conclusions which the Government have reached after careful consideration of the Committee's Report and the substantial body of evidence submitted to the PAC in connection with their enquiry.

I THE GENERAL ISSUES

3. The Government's general approach to the Committee's Report is based on three guiding principles which the Government believe must be taken into account in determining the role of the C & AG. The first is the principle of Ministerial responsibility to Parliament, set out in the Green Paper. This constitutional convention does not fit all cases neatly but remains the only effective means by which Parliament can hold to account those to whom money is voted.
4. The second principle is the need for high standards of financial stewardship and prudence in handling public money. The Government agree with the many comments on the Green Paper in this sense, and recognise the contribution which can be made to this by audit in all its forms. But the Government do not share the Committee's implicit view that, apart from internal audit, this contribution should be made for the whole of the public sector only by the C & AG. It is beyond question that the private accountancy profession has the competence to do such work, bringing to it experience of auditing private firms, and this is of great value to the audit of many public sector bodies.
5. The third principle derives from the evidence that standards of audit, both external and internal, of Government Departments require improvement. The Government wish to

(1) 'The Role of the Comptroller and Auditor General' (HC 115)

(2) Eleventh Report from the Expenditure Committee, Session 1976-77, (HC 535)
First Report from the Select Committee on Procedure, Session 1977-78, (HC 588)
Second Special Report from the Committee of Public Accounts, Session 1978-79,
(HC 330)

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work with the PAC and the C & AG to achieve this. The scope for achieving this improvement will be reduced if the C & AG's work is extended into large new areas of administration with which his Department is at present unfamiliar. The first priority, in the Government's view, is to ensure that the C & AG is able to carry out his present substantial responsibilities as effectively as possible.

New Legislation

6. It remains the Government's view that it would be useful to introduce legislation to provide an up to date prescription of the C & AG's functions. But this is not a pressing need. Experience of the past two years suggests that the existing legislation need not in fact inhibit further desirable changes in the work of the C & AG and the PAC.

7. The Government will keep under review the possibility of legislation within the lifetime of this Parliament. They believe there should be a substantial consensus within the House about its content. Debate on the White Paper may provide an indication how far there is wide agreement in the House on particular legislative changes. Other prospective developments in Parliamentary procedure and Government Accounting may need to be taken into account in framing any new legislation.

II THE NATURE OF THE C & AG's AUDIT

8. The Government agree with most of the Committee's comments and conclusions in Chapter 2 of the Report about the nature of the C & AG's audit. They welcome the Committee's endorsement of the systems-based approach for audit reporting in the field of value for money (VFM) examination. The Government think the Committee are right to say that VFM investigations by the C & AG should be audit-based. The Committee's discussion of effectiveness audit shows that there is agreement on the important point that the C & AG should refrain from raising the merits of policy objectives.

III THE RANGE OF THE C & AG's AUDIT

9. The recommendation that "new legislation should establish the principle that the C & AG should either audit, or have access to, the books of all bodies in receipt of money voted by Parliament"⁽³⁾ is applied by the PAC to nationalised industries, other public corporations, local authorities, and many commercial bodies in the private sector. The Government agree that an essential part of the role of the C & AG is to ensure accountability to Parliament for public money, but as mentioned above they wish to see

(3) HC 115, para. 8.8

more, not less, involvement of the private sector in the audit of public spending and to avoid over-loading the C & AG. They believe that in defining the range of activities of the C & AG account should be taken of the principle and extent of Ministerial responsibility to Parliament. Audit arrangements should reflect the constitutional relationships between central government and the various bodies in receipt of public funds. Accountability to Parliament cannot be created simply by changing the auditing arrangements.

(a) The Nationalised Industries and Other Public Corporations

10. The Government fully share the PAC's concern about the need to promote the efficiency of the nationalised sector. Not only do the nationalised industries represent a significant proportion of the economy, but to a considerable extent they are insulated from competitive pressures. For this reason Parliament recently legislated (in the Competition Act 1980) to allow the Monopolies & Mergers Commission (MMC) to undertake efficiency investigations into the nationalised industries. The MMC has made a good start. Their investigations, of which 4 have been completed in the last 12 Months, have identified a number of areas of weakness in the industries' operations.

11. The Government are not convinced that it would be fruitful to replace this framework so soon after its inception. The better course in their view is more vigorous use of the instruments that already exist. With this in view the Government are currently considering how the role of the MMC in the field of efficiency audit can be strengthened and supplemented. A further statement will be made in the near future.

12. As the auditor of the accounts of the sponsor departments, the C & AG has access to reports submitted by the MMC and by the industries' auditors to the responsible Ministers. He can report on any inadequacies in the monitoring and control arrangements, and in the scope or validity of the information available to those Departments. The Government would welcome PAC examination, on the basis of C & AG reports, of departments' exercise of their responsibilities in this area. But they do not think the case has been made out for the further step, at this stage of development of arrangements for efficiency audit of the industries, of involving the C & AG directly in the industries' affairs. They note that to extend his role in the way envisaged by the PAC would result in a substantial increase in the work of the C & AG and his Department in a novel area.

13. Similarly, the Government do not favour systematic extension of the C & AG's role to the water authorities or to other public corporations. But they agree with the PAC that the fact that a body's activity is in whole or part commercial in character is not in itself an obstacle to giving the C & AG any form of audit responsibility for the body's accounts.

(b) The National Enterprise Board (NEB)

14. Under its present guidelines, the NEB is required to work in partnership with private sector capital wherever possible. Its operations depend for their effectiveness on co-operation and free exchange of commercially sensitive information with private sector companies and investors. The prospects of such co-operation would be impaired if the C & AG were to be given access to the books and records of the NEB.

15. The Government have announced recently their intention of bringing the NEB and the National Research Development Corporation closer together. If this leads to their eventual amalgamation, the question of accountability of any new body to Parliament will be considered when legislation is introduced.

(c) Local Authorities

16. The Government agree with the Committee that some reform is needed of local authority audit arrangements, but do not believe that the right solution is to put the District Audit Service under the control of the C & AG. For those functions relating to local authority activities for which Parliament has given them responsibility, Ministers are already fully accountable to Parliament. The Government do not consider that the C & AG needs for that purpose access to more information than is available to the Departments under audit.

17. The Government attach particular importance to the value for money content of local authority audit, and agree with the PAC about the desirability of further developing co-operation on technical matters between the District Audit Service and E & AD. The Government see an important role in local authority audit for auditors with private sector experience. They believe that the interests of all parties concerned, including local electorates, will best be served by the establishment of an Audit Commission for local authorities in England and Wales [as announced by the Secretary of State for the Environment on]. The C & AG can be associated with the Audit Commission as he is now with the work of the Advisory Committee on Local Government Audit. The Government propose that present arrangements for the Commission for Local Authority Accounts in Scotland should continue but will wish to consider in due course whether experience of the new arrangements in England and Wales suggests that the arrangements in Scotland should be reviewed.

(d) Non-departmental Public Bodies (NDPBs)

18. Most NDPBs are advisory or judicial and do not spend money on their own account; in almost all cases their expenses are borne on the Votes of their sponsoring Departments and are therefore audited by the C & AG. It is only a minority of bodies which spend money on

their own account; they generally exercise executive functions and are listed as "executive bodies" in 'Non-Departmental Public Bodies: Facts and Figures 1980' (HMSO, 1981). Paragraphs 19 to 21 apply only to these bodies, apart from the water authorities and the NEB which are considered separately in paragraphs 13-15.

19. Irrespective of their functions, size and the degree of Ministerial control over them, the Government are determined that all these bodies should achieve high standards of effectiveness, efficiency and economy. They recognise and welcome the contribution which the C & AG can make to achieving these standards and to proper accountability to Parliament.

20. The Government agree generally with the policy suggested by the PAC concerning NDPBs,⁽⁴⁾ but doubt the need to give the C & AG formal audit responsibility for all bodies mainly or wholly financed by Government. In many cases the requirements of accountability to Parliament can be met by ensuring that the C & AG has access to the books of the bodies concerned without requiring him to undertake full certification audit. In this way, the useful links which have been established between many bodies and their private sector auditors can be retained.

21. Most NDPBs are already subject to C & AG audit or access. Ministers will, however, be conducting periodic reviews of the bodies they sponsor and will consider in the course of these reviews whether audit arrangements are satisfactory.

(e) Private Sector Recipients of Government Grants and Loans

22. The Government do not agree with the PAC's proposal that the C & AG should have access, "where he considers it necessary",⁽⁵⁾ to the books and records of private sector companies in receipt of Government grants or loans. Should the C & AG and his staff become involved in this way, such companies would be understandably concerned about disclosure of details of their commercial affairs.

23. The C & AG has access to departmental files in the course of his audit and can consider papers relating to companies receiving public funds. He is therefore already able to examine reports made by private sector accountants whom Departments may employ in assessing requests for support from private sector companies. Since Departments monitor the use companies make of loans and grants, he can also report on this aspect of departments' activities.

(4) HC 115, Ch.3 and paras. 8.10(a) and (b)

(5) Hc 115, para. 8.10^d(~~e~~)

(f) National Health Service

24. As the PAC recognised, the "statutory" auditors of the NHS are an integral part of the oversight of the NHS by the Accounting Officers of the Health Departments. If the "statutory" audit were transferred to the C & AG as the PAC recommend, the Health Departments would have to make other arrangements for the internal audit of the NHS, thus in large measure duplicating the C & AG's work. The C & AG already has access to NHS papers at all locations enabling him to pursue his enquiries where he wishes. The Government agree that there should be the fullest co-operation between the staffs of the E & AD and the "Statutory" audit, but are not persuaded of the case for more fundamental changes.

IV THE STATUS OF THE C & AG AND OF HIS STAFF

25. The PAC proposed that the C & AG should become an Officer of the House appointed by the Queen by letters patent on the recommendation of the House of Commons; that the PAC should be able to give the C & AG directions to investigate particular programmes or projects; that the existing staff of E & AD and the DAS should become servants of the House and transformed into a new National Audit Office; and that a Public Accounts Commission of the House should be established with responsibility, among other things for determining the number of staff in the National Audit Office and their pay and conditions of service.

26. The Government are not convinced by the PAC's proposals as to the status of the C & AG or as to the question of powers to give him directions. There are as good reasons in the public sector as in the private sector for regarding independence as one of the essential attributes of an auditor. The Government believe that within the framework of specific legislative provision the C & AG should continue to be totally independent of any form of external influence or direction in the performance of his duties. The C & AG himself expressed this view in evidence to the Committee. The same view was taken by the PAC of the last Parliament.⁽⁶⁾ The PAC already have a working relationship with the C & AG which has proved effective over many years and to which both the Government and the Committee attach considerable importance.

27. The established method of appointment of the C & AG is by letters patent by the Queen on the advice of the Prime Minister. The Government are not persuaded of the case for changing it, but reiterate their view that when a new appointment is in contemplation, it will be appropriate for the Government to consult the Chairman of the PAC. This was done

(6) Second special Report from the Committee of Public Accounts, Session 1978-79, (HC 330), para. 15.

in regard to the new appointment recently announced.

28. In the Green Paper, the Government said that they would be ready to consider some form of control by the House of Commons Commission as an alternative to the oversight of the C & AG's budget and the staffing costs of E & AD currently exercised by CSD. That remains their position, but the Government consider that the balance of advantage lies in retaining the present arrangements. As the Committee acknowledge, the E & AD have been exempted from the recent cuts in Civil Service numbers; indeed, the C & AG has reached agreement with CSD on a substantial programme to increase staff numbers over the next five years to enable the Department adequately to fulfil its existing responsibilities. The Committee acknowledges that the present administrative arrangements work.

PERSONAL

Mr Rickett

OK for 10 minute

Note

*I have spoken to Clive
Preston. Send Rayner with
minutes accordingly*

Govt Mach

wh 1/7

INTERNAL AUDIT AND FINANCIAL CONTROL (Case study of financial management)

1. I have had a call from Mr Pestell, the Head of CSD's Manpower Group. Among other things, he looks after the annual scrutiny of departmental running costs. He rang me about the reference in Mr Whitmore's letter of 22 June to Sir Douglas Wass to bringing in two Ministers and their Permanent Secretaries, with management consultants, to examine the outcome of their scrutiny.

2. Mr Pestell is not clear what the management consultants would do before and at the meetings. (I assume that there would be one for each department.) I should be grateful for an early word with you about this. In the meantime, you might find the following thoughts helpful.

PURPOSE OF THE SCRUTINY AND OF THE PM'S MEETING

3. I attach a copy of Sir Derek Rayner's letter to the Home Secretary of 22 February 1980 which launched the scrutiny. May I draw your particular attention to its enclosed Note 1, especially:

- possible questions about the cost of the department as a whole (Note 1, paras 18 - 21); and
- information about parts of the department (Note 1, paras. 22 - 26).

4. Those paragraphs bring out the essential points that Ministers can address themselves to questions of relative simplicity about the costs of the department as a whole (the pounds, if you like) but that they need to get down to some detail in order to understand and query its composition (the pence).



5. You might also like to look at Sir DR's minute to the PM of 18 May, copy also attached for convenience.

6. I doubt whether management consultants could do much to improve on the purpose of the scrutiny or the questions in which that purpose is expressed, although they might be able to comment usefully on:

- the underlying information systems
- the allocation of and the accountability for costs
- the seriousness with which the scrutiny is taken.

7. But of course they could do nothing without spending some time in the department which - to judge by the Coopers & Lybrand study in MAFF - would be quite expensive. (We might have a word about who would pay for this.)

8. As for the purpose of the meetings, Sir DR suggested in his minute to the PM of 20 January this year that a "presentation" by those at the key levels in the management chain would be a very helpful technique. If one included a department like DHSS, those in the management chain might include the Permanent Secretary and a local office manager, for example.

9. I am not quite sure how it is envisaged how the management consultants would be used at the meeting. Putting in the crudest possible terms, would they be playing the part of the prosecutor and the department that of the defendant? My own feeling is that the PM would get as much value, if not more, out of her meetings with Ministers if she asked each of them what he received by way of information, what he did with it and what had happened as a result and each Permanent Secretary how he organised the control of departmental running costs, including the parts played by himself, his PEO

PERSONAL



and PFO and his line managers.

10. I think also that the PM might have Sir DR along instead of or in addition to management consultants, not least because of his scepticism about whether enough of them have their feet on the ground.

11. We shall be glad to brief, whatever happens.

WHICH DEPARTMENT?

12. With an administrative expenditure of £1,132m (1980-81, cost per employee of £11,745) DHSS would be a good candidate to include. Other "big system" departments are the Inland Revenue and Customs and Excise.

13. Another possibility would be DOE. Mr Heseltine has taken a close personal interest in the running of his Department. The latest manifestation of this is his current scrutiny of the control of overheads. This is being undertaken by a good Economic Adviser, Mr Joubert, who might be included in the party.

14. If the PM wanted a much smaller department, I understand that GCHQ takes its running costs very seriously and has operated a system of "local cost centres" for some time.

15. May we please speak?

C

C PRIESTLEY
29 June 1981

Encs: Sir DR's letter of 22 February 1980 and his minute to the PM of 18 May 1981



CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-~~27334222~~ 233 8224

22 February 1980

The Rt Hon William Whitelaw MP
Secretary of State for the Home Department
50 Queen Anne's Gate
London SW1

For Home Secretary,

THE SCRUTINY OF DEPARTMENTAL COSTS

(Earlier reference: Mr Whitmore's letter to Private Secretaries of 17 October)

1. Cabinet decided last autumn that it should have an annual statement on the cost of government and that departmental Ministers should examine the cost of running their department.
2. This letter offers advice on how to proceed. Note 1, enclosed, deals with the scrutiny of costs and is the basis for action now. Also enclosed is a paper (Note 2) which sets out my personal views on the sort of full departmental account of assets, costs and receipts which I regard as the goal to be reached in due course and towards which I regard Note 1 as an interim step. Note 2 is for information, not action.

General

3. The management of resources in government tends in my experience to be an amalgam of macro-economics and cash accounting. The purpose of Note 1 is, by contrast, to help Ministers to develop management accounting appropriate to the place they occupy at the top of their organisations.
4. Like other top managers, Ministers have to delegate much of the day-to-day responsibility for ensuring that resources are used effectively and that claims for extra resources are justified and cannot be met elsewhere. But so that delegation is not abdication, Ministers want information which enables them to survey and appraise their costs, notably but not only in the PESC/Estimates cycle, and to dig down selectively throughout the year.

5. They also need appropriate staff support. In my view, those best qualified to examine the consumption of resources on behalf of Ministers and their Permanent Secretaries are people with professional training in management accountancy. I believe that a Minister and his Accounting Officer should be served in the capacity of Principal Finance Officer by the kind of man or woman who in the private sector has overall responsibility for the financial affairs of his company. This would represent a change in the basic concept, but I make no apology for this. I regard it as especially important because the range of responsibilities carried by the typical Accounting Officer is usually very wide and formidable and he will not be able to go into all departmental expenditures in detail nor personally follow up all the questions that will be raised. It is therefore essential in my judgment that in dealing with the scrutiny of costs Accounting Officers are increasingly served by experienced accountants who have direct access to them and that these accountants have staff who are numerate and carry sufficient authority to probe in depth in any area where in their view it is imperative to ask more questions.

6. It will be said with some truth that awareness of costs has not necessarily in the past brought expenditure under control nor eliminated the desire of some departments to have what they would like without regard to cost. This will continue to be inevitable as long as there remains a lack of awareness and of involvement by senior people in making sure that the resources available are used to the best advantage. It will also continue if there is no real penalty for those who are extravagant, providing the rules have been obeyed and budgets not exceeded.

Scrutiny of departmental running costs - the "expenditure account" (Note 1)

7. I have consulted the Secretary of State for the Environment, the Chief Secretary and the Minister of State, CSD, in preparing Note 1. Agencies responsible to them will supply departments with some of the data required, while the CSD is ready to help departments in giving effect to the proposals contained in it. I am grateful to these Ministers for this.

8. The first year in which departmental costs are scrutinised in the way suggested in Note 1 is bound to be a little rough and ready, with some gaps in the information available to Ministers. I suggest we accept this and that, in setting up the proposed system, it is essential to ensure that the best is not made the enemy of the good nor that it becomes an annual ritual which accepts that extra expenditure is permissible because of slippage in timing or accelerates activity by costly overtime to keep in line with forecasts.

9. I should like to stress two points. First, in developing means of informing themselves Ministers should not in my view feel constrained to follow the strict rules of cash accounting but should instead use approximation where necessary: orders of magnitude and a picture of the movement of costs are what is necessary. It is essential also that in the first instance the information presented to Ministers is sufficiently brief and clear so that the relevant questions will come easily to mind. Ministers will need to seek further information to answer some of these questions. The back-up data lying behind what is first put to Ministers must therefore be of a kind which enables such questions to be answered.

10. Secondly, the enclosed Note 1 discusses information for the annual scrutiny by departmental Ministers on which Cabinet agreed. But I am sure that in present circumstances and for the foreseeable future Ministers will need some of it more than once a year if they are to assure themselves that the substance and movement of costs are according to plan. I recommend that Ministers set aside time each month for the examination of some part of the resources they use or have in their keeping.

11. Ministers in charge of departments will no doubt want to take the lead themselves at PESC and Estimates. But it may be helpful to them and to their junior Ministers to look to one or more of their Ministerial team to continue the scrutiny throughout the year. That would increase familiarity with the data and with the issues against the time for deciding bids and forward plans for resources and enable Ministers to plan both for reducing costs and for the better use of those resources which do have to be consumed.

A full account of assets, costs and receipts (Note 2)

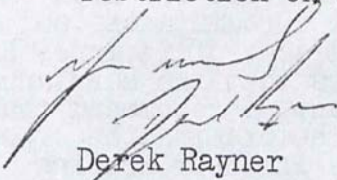
12. What I have termed the "expenditure account" is only a first but an important step towards providing cost information for Ministers. The enclosed Note 2, Thoughts on a departmental account, outlines very roughly the sort of account which might be the target to go for with the help of experience.

13. This would be an account for each Minister (and on this foundation for the Cabinet as a whole) of his costs, his receipts, if any, and the assets in his keeping. It will take a little time to produce such an account, because data on the value of land and buildings among other assets are not, I understand, readily to be had. So I should repeat that Note 2 is not intended to be and cannot be actioned now. I include it, however, to show the direction I believe the development of cost information should take.

Next steps

14. I hope that Ministers will be able to move ahead on the basis recommended in Note 1. If I can help I will do so gladly. I recognise that the arrangements proposed will mean some additional work, but I believe it can produce nothing but good since such extra effort as is required will be of positive advantage to Ministers and their departments.

15. I am copying this to the Prime Minister, your Cabinet colleagues, the Minister of Transport, the Minister of State, CSD and to Sir Ian Bancroft, Sir Robert Armstrong, Sir Douglas Wass, Sir Kenneth Berrill and Mr K J Sharp. I ask for no restriction on its circulation.



Derek Rayner

Encs: Note 1 Annual scrutiny of departmental running costs -
the expenditure account

Note 2 Thoughts on a departmental account

NOTE 1

ANNUAL SCRUTINY OF DEPARTMENTAL RUNNING COSTS

1. I recommended last year and it was agreed that "each Minister in charge of a Department should at the appropriate point in the PESC/Estimates cycle, scrutinise the overheads of his Department as well as his staff costs". This is because in order to run anything, one needs first to know and then to question his costs. But I also believe that Ministers should avoid excessive detail - they are not in the business of accounting for the petty cash.

Scope of the information needed

2. This note is about providing and using information on the cost of having a Department, that is, of its staff, of its buildings and of supplying it with goods (eg stationery, furniture and equipment for scientific research) and services (eg water and electricity) which it uses. In offering it to Ministers, I acknowledge that some departments may already have sophisticated information systems, especially those which have Trading Funds; the latter should not, in my view, be excluded from the scrutiny, but it may be that their costs are already displayed in enough detail in their accounts for there to be no need to assemble them again as suggested below (paragraph 11) and in the Annex.

3. I also recognise that the detailed day-to-day responsibility for good management cannot and should not be exercised by Ministers themselves but by their officials. However, officials' authority for making good use of manpower, goods and services is delegated to them by and they discharge it under and on behalf of Ministers. I see the peculiar responsibility of Ministers here most clearly represented by two inalienable tasks, approving their Estimates of Expenditure and satisfying themselves, by selective examination, that the manpower, goods and services used in their name are used efficiently and well.

4. It may not at first be clear what information on the cost of manpower, goods and services should include and exclude. I offer the following thoughts on this.

5. First, the information to be provided should be only for the manpower, goods and services used by Ministers in running their own operations and administration, ie those operational and administrative expenditures whose form, scale and deployment are under the direct personal control of Ministers.

It may be helpful if I offer some comments in extension of that view:

a. I would exclude those "running costs" expenditures by such large public sector bodies as local authorities, the National Health Service and nationalised industries, since - although these are partly funded through departmental Votes - they are not under the Minister's personal control or within his management responsibility.

b. I would exclude grant-in-aid bodies, other than the Manpower Services Commission, Health and Safety Commission and the Advisory, Conciliation and Arbitration Service, since these are staffed by civil servants. I am writing to the Secretary of State for Employment about this. However, when in such cases the Minister's Accounting Officer is required to ensure that the body has an "appropriate financial regime", I recommend that it should be his responsibility also to assure himself that the head of that body has available to him a satisfactory management information system.

c. There may be problems of interpretation over the general aim, which is to include all relevant operational and administrative costs of the Minister's department. It might be argued that in some cases there is an unclear dividing line between, on the one hand, staffing, housing, maintaining and servicing a function and, on the other, the function itself. One example which has been mentioned to me is that of the Home Office's Prison Department, the question being where administration and "overheads" end and the function itself begins. I am firmly of the view that, for the purposes of the first year of this exercise, one need not strive to draw over-nice boundaries. In the case of the Prison Department, I would regard administration, "overheads" and function as forming a single cost centre and I would consider that all of this should be included as being part of the cost of running the operations of the Home Office.

d. By contrast, I would exclude expenditure not related to the operational management of the Department, even though it is spent on functions for which the Minister is directly responsible. Examples are intervention buying of agricultural produce, the development costs of Concorde and the government's contribution to teachers' superannuation. I would exclude also the cost of grants, loans or benefits to associations, organisations or individuals outside the department.

e. I understand that a particular problem may occur over agency or contractors' services. I suggest that where these are an essential part of the activity within the Minister's management responsibility, for example Post Office agency services, they should be included. However, where they go well beyond this (eg the use of local authorities as agents for trunk roads programme) they should be excluded.

f. I recognise that there may be special problems in the Ministry of Defence, owing to the difficulty of separating Civil Service from HM Forces costs.

6. Secondly, provided there is a broad consistency of treatment between departments, I do not think it matters much if in the first year in which Ministers scrutinise their departmental costs the exercise has rough edges and is to a degree experimental. I expect we shall all learn from the experience and I do not have a ready-made specification which will indicate with precision the exact scope and content of the data to be provided.

7. Thirdly, however, that "broad consistency" will be very much helped by the fact that it is already possible to specify with reasonable accuracy many of the constituent parts of a department's expenditure (see paragraph 11 below).

8. Fourthly, I suggest that the types of expenditure to be included should be determined not according to who pays, but who consumes. Whether or not repayment is introduced for those services currently provided on allied service terms, I suggest that Ministers will wish to manage their use and consumption of, for example, accommodation and PSA supplies as if they were a direct charge upon their Votes. Indeed I believe that the Treasury guide, Government Accounting, already asks departments so to behave. While the Property Services Agency is responsible for the management of the Government's

office estate as a whole, I see the consuming Departments as exerting a very powerful influence on the planning, allocation and control of such resources and, of course, as determining the total demand for them. Similarly, they determine the demand for other types of accommodation.

9. On this basis, I recommend that the information to be assembled should cover the following three broad categories of cost:

a. Those staff and other costs of running a department which are paid for out of its Votes and for which the Minister is accountable to Parliament.

b. The cost of those "supporting services" which are a charge upon the Votes of others and provided free to the department on allied service terms.

c. Those costs which do not entail actual expenditure by the department but which, I suggest, should nevertheless be taken into account when calculating the total cost to the taxpayer of running it. These costs are the pension and gratuity liability which accrue because staff are employed and the equivalent market rental of the offices the department occupies.

10. The Supply Estimates and associated tables provide some useful information on costs in those categories. But it is in my view an inadequate form for management purposes. For example, the information there given on "supporting services" is not presented on a departmental basis; the degree of detail about direct departmental costs is not sufficiently defined to enable the various components of the department's running costs to be managed individually; and the comparison with the previous year only does not offer an adequate span of time for effective monitoring.

Information about the Department as a whole

11. I have set out in the Annex relevant types of expenditure and the period the data should cover. The types are in brief:

- A. Staff (including pension and gratuity liability)
- B. Other services
- C. Personnel overheads
- D. Office and other accommodation costs
- E. Office services
- F. Other non-office expenditure

12. I recommend that all Ministers should have information prepared for them on this basis.

13. The costs are gross and expressed in money terms. Capital and current expenditures are separately identified (although in an ideal management information system capital expenditures would be displayed in an annualised form, depreciation and interest charges being the cost of the resources consumed each year).

14. In the case of services not paid for out of departmental Votes (paragraph 9b above), data on costs not already available to Ministers from within their own departments may be obtained from the Property Services and other agencies which supply those services. A list of contact points is given at the end of the Annex. If such costs are not at once available in the form required, they will be provided in the course of the coming year for incorporation in the schedule later. This procedure will apply to the PSA, Central Office of Information and Rating of Government Property Department and to HMSO and the CCTA in respect of expenditure before the move to repayment on 1 April 1980. It is another case where Ministers may need to accept that there will be some rough edges in the first year.

15. The cost of office accommodation (paragraph 11D above) can be charged at an equivalent market rental, by rental zones, whether it is leased or Crown freehold. This will put all departments on a comparable basis in monitoring accommodation costs. The cost of specialised buildings (Crown Courts, Prisons, Laboratories etc) is, I am informed, harder to assess. The PSA tell me that this is because there will often be no

market rent for such property and that it may be difficult to arrive at a capital value. In these cases, I propose, for the present, that only the capital cost of new construction undertaken each year should be shown. (Such projects will already have appeared in the department's PESC and will appear in Estimates.) For the future, it should be possible to devise a suitable method of capital valuation, possibly a form of depreciation based on initial or replacement cost. I have asked the PSA to advise me on this, as I am anxious that Ministers should have available to them a valuation of the capital assets in their hands. I intend to go separately into the questions of repayment for or attribution of PSA expenditure on behalf of user departments. The treatment of accommodation costs can accordingly be considered again in the light of the outcome.

16. I attach some importance to the question, covered by A in paragraph 11 above and the Annex, of how much pension liability as well as wage-salary and other cost liabilities a Minister accepts when he recruits staff. A career civil servant is a substantial investment from the moment he/she is taken on to the moment his/her working life ends, but pension liability is as much a cost of employing a civil servant as his/her pay. This point is covered by my recommendation on the inclusion of pension and gratuity liability at paragraph 9 above.

17. In case officials need help in interpreting the intended scope and coverage of the cost information, I have agreed with Mr Channon that they should write to Mr A R Williams, Manpower 1 Division, Civil Service Department.

Possible questions about the cost of the Department as a whole

18. In the first instance I suggest that information needs to be brought together and displayed for the department as a whole. It will provide Ministers with answers to such simple, but important questions as:

- What is the total cost of running my department now and how does it compare with costs in previous years?

- Which particular costs make a significant contribution to the total? What efforts is the department making to keep those under control?
- How much has inflation caused expenditure to rise and how is my department improving efficiency to off-set its effects?
- Are my non-staff costs moving in line with what would be expected in the face of changing staff levels?
- Where have I failed to achieve planned changes in my costs?
- Are the savings I am achieving merely at the margin or am I operating on the main bulk of my costs?

19. In addition to the information set out in the Annex, to provide Ministers with a feel for what they are buying for the taxpayer, I suggest that some of the expenditures should be supplemented vividly by notes on quantities, eg numbers of staff employed, square footage of office space, amounts of paper and energy consumed, numbers of staff trained, number of cars in the transport fleet.

20. I attach special importance to two things, firstly the level of staff wastage. If high, it means a significant wastage of resources, notably in the costs of recruitment, training and supervisory time, in addition to unrealised investment in wages and salaries. Similarly, it is necessary to give a clear breakdown of staff by grade. In my own business, I need to know how many managers, assistant managers, supervisors and sales staff we have and how many specialists, technologists and technicians. This is because, without careful scrutiny, the relative proportions of the various types of employee tend to change unpredictably and it is all too easy to make economies, not by cutting back on the numbers of senior grades, but on those whose jobs can most easily be measured.

21. Secondly, the cost of stocks. The "non-office expenditure" covered by paragraph 11 F above may include the purchase and storage of various kinds of stocks and stores. Where these include supplies that are expensive both to buy and to store, I suggest that it would be helpful to have a separate analysis to provide data on purchase and storage costs, so that Ministers can enquire why, for example, the level of purchase and stockholding has gone up or down.

Information about parts of the Department

22. Information about the department as a whole can only take Ministers part way along the road to effective management. To plan and control the costs of running their departments I suggest that they will need to ask, and to have information available to answer, such questions as:

- Why are the costs of particular items at the levels that they are and changing in the way they are?
- Where in my department do the cost of particular items mainly arise and the changes originate, eg HQ or Local Offices; Policy/Advisory or delivery of the services; desk staff or support staff?
- What is the rate of staff turnover or wastage, with particular reference to grades that matter to my operations?
- What grades does my staff consist of and in what numbers? Which are expanding or contracting and why? What change in the pattern of skills employed by my department does this represent and why?
- What is the cost to the department of running a particular programme?
- Are the staff and other costs of a particular programme moving in the same direction as my policy in relation to the programme? If not, why not?
- Where in my department have my economy drives failed to bite?
- How much have this year's policy initiatives affected the cost of running my department?
- In what areas could I achieve savings in the longer term by increasing expenditure in the short term?

23. I suggest that providing answers to such questions will mean underpinning gross information on the department as a whole with similar information on its component parts.

24. It will be necessary for costs to be got together in relation to organisational units and, if Ministers so desire, expenditure programmes or particular activities. The definition of the "organisational units" and of "activities" will be for Ministers to determine in the light of their own departmental circumstances. For example, in some cases it might be satisfactory to specify a Deputy Secretary command as an "organisational unit", whereas in others an Assistant Secretary (or lower) command would be appropriate. An example of an activity could be training across the whole department.

25. Ministers need not have this supplementary information presented to them in its entirety unless they wish. Its main purpose should be as a source of information which can be tapped so as to explain the data presented on the whole department and in answering Ministers' specific questions. It should also, of course, sharpen the awareness of costs and bring home the need to control them at all levels of management.

26. Having the wherewithal to examine the cost of a particular activity is the precondition for enquiring into value added for money spent. That enquiry should not and cannot be confined to appraising staff and running costs - it is bound to extend to the appraisal of the outcome of policies on the ground and therefore to the search for effective ways of assessing outcome. This may apply just as much to the expenditure of public bodies other than the department when Ministers are evaluating policies and considering the total cost of implementing a programme, but this note is addressed to the cost of departmental administration, not to the cost of policies.

Timing of the scrutiny

27. I suggest that Ministers should have an opportunity to scrutinise the cost of running their department in good time for the decisions they need to take each year on the level and direction of change of such costs in the next and coming years. I recommend therefore that departments should prepare

their analyses in April of each year for presentation to Ministers in early May. The decisions taken by Ministers on the detailed expenditures should then be reflected in the preparation of the next year's Estimates. In November each year, when these Estimates are being prepared for the following financial year, I suggest that Ministers will then wish to ensure that their management decisions have been taken on board and make further adjustments as necessary. But I should emphasise that I see the information as being just as if not more helpful to Ministers in relation to planning for later years as for the next following year. This is because, in my view, it bears heavily on the medium-term management policy of the department, as well as upon the scrutiny of costs here and now and to decisions on the administrative budget for the next year.

28. I recommend that the information should be scrutinised by the Minister in charge of the department. However the responsibility for taking the first look at the data might be delegated to a Minister of State or a junior Minister. He/she could also be responsible for any follow-up after the scrutiny.

29. The data listed in paragraph 11 and set out more fully in the Annex will also provide the base for an annual statement on the cost of running central government. This will be prepared by CSD Ministers for the Cabinet, who will consider it at about the same time as the PESC report. I understand that Mr Channon would like to receive returns from Ministers by the beginning of June, together with a commentary indicating each Minister's conclusions as a result of his scrutiny.

30. I recognise that all the information necessary to meet the management needs of Ministers may not be available in this first year of operation. It is important however that Departments begin now to refine their cost information systems with a view to its being fully operational in 1981-82. I therefore recommend that the scrutiny for 1980-81, although it should be done for real, should be regarded as a pilot run, so that the new procedures can operate smoothly in and from next year. I recognise that there could be problems of timing in this first year. If necessary,

in order to get a reliable test, the submission of trial analyses to Ministers could be put back, provided that Mr Channon received all returns by the end of September to allow enough time to consider the lessons to be learned from this first attempt at the scrutiny of costs.

31. I shall be glad to do what I can to help with the trial.

Summary of recommendations

32. Principal Accounting Officers should assure themselves that heads of bodies funded through departmental Votes have available to them a satisfactory management information system (paragraph 5b).

33. The information to be assembled should cover (a) staff and other running costs paid for out of the department's Votes; (b) the cost of supporting services provided on allied service terms; and (c) notional expenditure (paragraphs 9-12 and Annex).

34. Departments should prepare their analyses each April for presentation to Ministers early in May, beginning this year. Ministers' decisions on the detailed expenditures should then be reflected in preparing the next year's Estimates (paragraph 27).

35. The information should be scrutinised by the Minister in charge of the Department, although the first look and follow-up action might be delegated to a junior Minister (paragraph 27).

36. The 1980-81 scrutiny, although done for real, should be regarded as a pilot run (paragraph 30).

Derek Rayner
Cabinet Office
Whitehall SW1

22 February 1980

TOTAL DEPARTMENTAL COSTS

	Last year -		This year		
	Penultimate Year (Actual) Gross	Last Year (forecast Outturn) Gross	This year (Estimate) Gross	Increase/Decrease + or -	% Change + or -
A. Staff					
1. Average Numbers of permanent staff					
2. Costs	£	£	£	£	
Wages and Salaries (including Insurance contribution)					
i. Permanent Staff (UK based)					
ii. Overtime					
iii. Casuals					
iv. Period Appointees; staff on loan from outside bodies (paid for by the department)					
v. Staff locally engaged overseas					
vi. Employers' superannuation contributions					
vii. Other pay costs					
3. Pension and gratuity liability (1)					
TOTAL WAGES AND SALARIES					
B. Other Services					
1. GIRO and other banking services					
2. Post Office Agency charges					
3. Other agency charges, cost of staff employed by contractors, consultants and fee paid staff					
[Note: this item is intended to include the employment of contract labour eg cleaning staff but not the direct labour element in government contracts]					
4. Payments to other departments for 2 services provided (eg establishments or common support services)					
[specify each department separately]					
TOTAL OTHER SERVICES					

(1) Notional expenditure only.

	Penultimate Year (Actual) Gross	Last year (forecast Outturn) Gross	This year (Estimate) Gross	Last year - This year	
				Increase/ Decrease + or -	% Change + or -
	£	£	£	£	
C. <u>Personnel overheads</u>					
Travel					
Subsistence					
Entertainment					
Removals					
Catering Subsidies					
Protective Clothing, Uniforms etc					
External training, seminars etc					
TOTAL PERSONNEL OVERHEADS					
D. i. <u>General Office Accommodation Costs</u>					
Equivalent market rents (1)					
Rates (2)					
Heating, lighting(2)					
Maintenance (2)					
Furniture and fittings (2)					
ii. <u>Other Accommodation Costs</u>					
Rates (2)					
Heating, lighting(2)					
Maintenance (2)					
Furniture and fittings (2)					
Capital Costs - New Construction (2)					
TOTAL ACCOMMODATION COSTS					

(2) Expenditure borne on other departments' Votes (also applies to stationery, printing, office machinery and administrative computers before 1980-81).

			Last Year-This Year		
	Penultimate Year (Actual) Gross	Last Year (forecast outturn Gross	This Year (Estimate Gross	Increase/ Decrease + or -	% Change + or -
	£	£	£	£	
E. <u>Office Services</u>					
Carriage, freight					
Transport-own depart- ment (inc.vehicle maintenance)(3)					
Transport-PSA(2)(3)					
Telecommunications (5)					
Postage					
Office Machinery(3)					
Stationery					
Photocopying					
Printing & Publi- cations (3)					
Publicity and advertising (2)(3)					
Library Services					
Administrative Computers (3)					
Minor Administrative Expenses [separately annotated where substantial]					
TOTAL OFFICE SERVICES					
F. <u>Other Non-Office Expenditure</u>					
i. <u>Capital Expen- diture</u>					
Land					
Plant & Equipment					
Vehicles					
ii. <u>Running Costs</u>					
Land					
Plant & Equipment					
Vehicles					
iii. <u>Other Current Costs</u>					
TOTAL OTHER EXPENDITURE					
TOTAL EXPENDITURE A-F borne on own Votes					

NOTE 2

THOUGHTS ON A DEPARTMENTAL ACCOUNT

1. I believe that each Minister in charge of a Department should have available at the right moment in the PESC/Estimates cycle an account of the capital and human resources which he and his senior officials use.

2. A structure for this account might in outline be as follows. The presentation of data on costs etc should cover the previous year, the current year and the forthcoming year (estimates), with a projection to the end of the PESC period.

A. ANNUAL CAPITAL ACCOUNT

1. Estates and buildings: value of investments (which should be periodically revalued).
2. Plant and machinery: value of investments, less depreciation.
3. Costs of capital (eg interest charges and depreciation).
4. Stocks and stores.

B. ANNUAL EXPENDITURE ACCOUNT

1. Cost of staff salaries, wages and overtime.
2. Liability to pay future pensions in respect of present staff.
3. Cost of overheads related to staff, eg stationery, telecommunications.
4. Cost of overheads related to estates, buildings, plant and machinery, eg maintenance, heating, lighting, cleaning.

C. ANNUAL CONSOLIDATED ACCOUNT

The accounts at A and B above combined as appropriate.

	Penultimate Year (Actual) Gross	Last Year (forecast outturn) Gross	This Year (Estimate) Gross	Increase/ Decrease + or -	% Change + -
	£	£	£	£	
TOTAL EXPENDITURE A-F borne on other depts' Votes (2)					
TOTAL EXPENDITURE A-F which is notional only (1)					
GRAND TOTAL A-F					

- (1) Notional expenditure only
- (2) Expenditure borne on other departments' Votes (also applies to stationery, printing, office machinery and administrative computers prior to 1980/81).
- (3) Please separate expenditure between Capital Costs and Running Costs where possible.

- Notes:
- (a) Pension and Gratuity Liability is to be calculated on the latest rates notified by the Treasury [currently 19% for Non-Industrials and 16% for Industrials].
 - (b) Substantial costs will also need to be subdivided by organisational units (eg locations, functions, Under Secretary Commands etc). The precise nature of the breakdown will need to reflect the internal organisation of the department itself. All staff costs will require this treatment; the separation of other costs will depend upon a number of factors eg practicability, materiality and whether cost control will be facilitated.
 - (c) Expenditure figures should be shown gross. A separate note analysing receipts may also be required in order to present a full picture.
 - (d) Current year figures should be reconcilable with those shown in Supply Estimates after allowing for notional items. Figures for last year should be as near as possible to the final appropriation account figures. Penultimate year figures must be exactly reconcilable with that year's Appropriation Accounts.
 - (e) Any goods or services provided free to the department on allied service terms should be marked. The expenditure to be shown under these items should be obtained from the relevant allied service department.
 - (f) The contact points in these departments are as follows:
 - Property Services Agency: Mr P B Overton,
20 Albert Embankment, London SE1(211 3254)
 - Central Office of Information: Mr D J Etheridge,
Hercules Road, London SE17(928 2345 ext 8114)
 - Rating of Government Property Department: Mr P S Mewes,
69 Notting Hill Gate, London W11
(229 9841 ext 46)
 - HM Stationery Office: Mr P Jefford, Sovereign House,
Botolph Street, Norwich (0603 22211)
 - Central Computer and Telecommunications Agency: Mr D Fowler, Riverwalk House,
157-161 Millbank, London SW1 (211 0327)

D. ANALYSIS OF EXPENDITURE ACCOUNT

This should include a commentary on such items as:

1. Breakdown of staff by grade and skill.
2. Level and incidence of staff turnover.
3. Level and incidence of absenteeism and uncertificated sick leave.
4. Stockholding compared with stock usage; cost of stock handling and distribution.
5. Maintenance and cleaning.
6. Level and incidence of costs of services (heating, lighting, water etc).

E. ACCOUNT OF INCOME

This should include an analysis and account of receipts.

3. The structure outlined in para. 2 is about the cost of the Department as a whole. The assemblage of the necessary data would, however, enable accounts to be prepared for management in respect of particular activities, functions or organisational units and thus enable Ministers to examine certain areas of their Department in detail.

4. For example, it should be possible to cost expenditure on a research establishment and to value its assets in respect of:

- the Capital Account, estate, building, plant and machinery
- the Expenditure Account, staff and staff overheads; overheads related to the maintenance and upkeep of the estate, buildings etc; purchase of goods etc.

5. It would also be possible to analyse expenditure and income (if any) for the establishment as noted in D and E above. Indeed, I would regard this less as a possibility than as a requirement for line management.

6. As far as Ministers are concerned, I regard information of the kind outlined above as serving two main purposes in respect of a research or similar establishment. First, it enables them to make a reality of that management task which is appropriate to their status by providing them with statements of values and costs. They need this in order to know what they have in hand and to be conscious of cost.

7. Secondly, when Ministers are faced with the need to retrench as well as to manage expenditure, the information will enable them to pose pertinent questions on the overall movement of expenditure and to make such decisions as these:

- to keep or to sell land (capital receipts plus savings in associated recurrent expenditure)
- to keep to existing levels of upkeep and maintenance or not
- to keep or discontinue or not enter upon a particular or a preferred activity
- to keep or to reduce levels of stockholding
- to keep or reduce levels of fees and charges

8. Another example is of the administrative/executive/clerical activity, function or organisation. Again, I think that the inquiring Minister needs information in respect of such items as:

- Capital assets, if any (D above)
- Rental charges in respect of leasehold accommodation and equipment

- Staff costs
- Overheads related to staff and to non-staff items.

9. Such information, again, will help Ministers responsible for good management and for retrenchment by giving them knowledge of costs and enabling them to ask such questions as some of those in paragraph 7. Here some of the main questions should, I suggest, be addressed to the question of excellence. If Government has to provide a service, Ministers will want it to be a first class service. So the questions which arise include: the issue whether productivity and effectiveness can be increased by simplification of procedures; mechanisation; removing the causes of staff instability; and devising a management structure which is appropriate to the task in hand and is not oppressively long.

Derek Rayner
29 January 1980

PRIME MINISTER

1980 SCRUTINY OF DEPARTMENTAL RUNNING COSTS: RESULTS OF FURTHER ANALYSIS

1. On my return from Toronto I have seen the Lord President's minute to you of 11 May, reporting on the results of the inquiries he made after the Cabinet discussion on 29 January. The purpose of this minute is to offer comments which I hope may be helpful to you and your colleagues.

General

2. As the 1980 exercise was very much a pilot run, I am very glad to see (Annex B) that most Ministers find the scrutiny useful. I hope that those few who have expressed doubts will find them allayed by experience.

Technical development and relationship with other management information

3. The technical refinements that have been made to this year's scrutiny, on which Mr Hayhoe has written to Ministers, will help to increase its usefulness. Even so, I would expect further developments as other improvements occur in financial control and management information. Accordingly I am glad that the Financial Management Co-ordination Group (FMCG) is to take the lead in its development. If the annual scrutiny of running costs is to be of real value to busy Ministers duplication must be avoided. I would see that as an important objective of the FMCG, as well as the dissemination of good practice (see below).

Value of the exercise for Ministers in charge of departments

4. As the Lord President says, and this is a point which appears in some of the Ministerial reactions, the main value of the exercise is for departmental rather than central Ministers. But some Ministers have expressed doubts which deserve a response.

5. The primary purpose of the scrutiny is to provide departmental Ministers with information which enables them to appreciate and then to probe the costs at their hand. Detailed questioning; the selective digging down that ensues; and specific control are always in my experience most effectively done at the point of consumption. This emphasises the importance, not just of the departmental Minister and his most senior officials, but also of the very numerous line managers who, from day to day, consume and regulate the consumption of resources. But it is of course essential that what is served up to a Minister should be appropriate to his position in departmental management. He is entitled to manageable and intelligible digests of information, in which the main trends and issues are clearly identified.

6. I very much agree also with those Ministers who have said that the rather aggregated information provided in the scrutiny pro forma may need, for them, to be supplemented by disaggregated information (eg by function and unit of management). I would generally expect such information to be presented to Ministers in response to, and in support of, their questioning of costs rather than automatically in a first, weighty and possibly daunting batch of data. It follows that such underpinning data must be available if Ministers and senior officials on their behalf are to be able to control costs effectively.

7. In this context (and in support of what the Lord President says about the need to improve management accounting information), I suggest that a good general question for Ministers to ask is:

"Does my departmental management information system enable me and my senior management readily to identify where my costs are rising and (for example) where economies might be made with the least damage to my objectives?"

The Secretary of State for the Environment's current scrutiny (of the methods used to estimate, monitor and control expenditure on running costs and how they might be improved, including the scope for greater delegation of financial responsibility) promises a substantial read-across in this area to other departments. I hope that opportunities for the dissemination of good practice will be seized by the centre (see below).

Collective value of the exercise

8. Whilst the first line of attack on running costs is in departments, there is also value in a collective consideration. The administration of Government is very big business at £8300m a year. I believe that it is important for Ministers collectively to have an opportunity to see these costs (and how and where they arise) alongside other potential claims on resources and to satisfy themselves that the sum of the parts is an acceptable whole. This year the aim is to have this consideration in October, at about the same time as the consideration of public expenditure generally.
9. The follow-up exercise, on which the Lord President now reports, was intended primarily to help individual Ministers, in the light of the total picture, to satisfy themselves as to the reasons for their own rising costs, that there exist adequate systems of control and that action was being taken to keep costs down.
10. Annex A of his report offers a quite encouraging picture of what is happening on the control front. I noted in particular the efforts to control overtime spending, travel costs (including the use of local budgets), energy use, postage, stationery and telephones. There is variation between departments, though this may reflect variation in reporting rather than in practice. I also have no real feel, except in a few cases, for the effectiveness of departmental efforts at keeping costs down and achieving specific savings.

11. I would advise Ministers to take the opportunity offered by Annex A to consider the efforts of other departments to bring specific items of expenditure under control, for example:

the Inland Revenue's 90% use of 2nd class post;

the Treasury's 10% reduction in the volume of mail last year;

the Home Office's 20% cut in printing and publications; and

the Civil Service Department's 25% reduction in telephones etc.

12. For this and subsequent year's scrutinies I would also advise Ministers to call for a commentary by officials on the data at the time it is first presented to them, to cover the sort of ground set out in the recent follow-up questionnaire. In addition to the questioning of the detail to ascertain why costs are moving as they are, I would place particular emphasis on:

the need for a clear statement of the positive measures being taken to effect cost reductions;

the savings achieved as a consequence, for each type of expenditure; and

knowing what had been done to improve the systems of control in the department, to learn from the experiences of others and to what effect.

13. The Lord President mentions the need to reduce the volume of administrative expenditure by using cheaper procedures in areas where prices are rising. Departments are in the best position to identify opportunities for this. But the central departments also have a key role to play through firm budgetary control and the dissemination of 'best practice'.

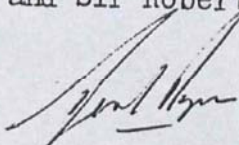
14. Despite the Government's efforts to control expenditure on administration, it increased by £1657m (25%) last year, £1100m of this going to wages, salaries and pensions and the rest to non-staff administrative costs. The Government is seeking a substantial limit on the increase in wages and salaries costs. But the increase in non-staff costs - upwards of £500m - is also very substantial. It represents a large claim on resources. I would advise Ministers to consider this in this year's scrutiny and the PES round. A good question might be:

"What would happen to the running of my department if I made a 10% cut in non-staff administrative costs over and above that which will occur as a result of the reduction in staff numbers?".

Publication

15. The Lord President recommends that the detailed results of the 1980 exercise should not be published unless specifically asked for. This is a matter for political judgment. May I just say that the Treasury and Civil Service Select Committee will probably want to know the costs of running Government when it comes to consider the question of efficiency in Government and that, on the principle that it is always better to initiate than to respond, there might be something to be said for meeting this in advance? The Government's White Paper on Efficiency might be a suitable vehicle for publishing pie charts and a summary table.

16. I am copying this to Ministers in charge of Departments and Sir Robert Armstrong.


Derek Rayner
18 May 1981

CONFIDENTIAL



10 DOWNING STREET

File AH

ccs csd

co

Isy

David Wolfson

Govt Mach Review of Exch & Bank
May 79
BF

From the Principal Private Secretary

22 June 1981

Dear Douglas,

INTERNAL AUDIT AND FINANCIAL CONTROL

I am sorry that I have not replied sooner to your letter of 11 June 1981 about the case studies of departmental internal audit and financial control systems, but as I told you on the telephone last week, when the Prime Minister saw your letter, she wondered whether it would be better to conduct the second case study in the Ministry of Defence rather than in the Department of Industry.

You drew my attention to the fact that, quite independently of the present exercise, the Ministry of Defence already had in hand two studies of their financial systems and procedures in which management consultants (Arthur Anderson and Company) were taking part, and you kindly let me have some material about them.

I have now been able to consult the Prime Minister again and, in the light of the information about the Ministry of Defence's studies, she agrees that there would be no point in mounting a further exercise in that Department and that instead the second case study should be carried out in the Department of Industry, as you proposed.

You also dealt in your letter of 11 June with the Prime Minister's earlier misgivings about the suitability of the Ministry of Agriculture for the first study. She is now content for this study to go ahead as planned but she hopes that the Treasury and Sir Derek Rayner's unit will be associated with the reviews which the management consultants have suggested Sir Brian Hayes should carry out with them at the end of the first and second stages of the study. She would also like David Wolfson from here to take part in these discussions.

Finally, the Prime Minister has been reflecting further on the idea that there might be a link between the case studies and her wish to follow up the results of the 1981 scrutiny of departmental running costs by calling in the Ministers and Permanent Secretaries of a couple of departments, together with

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BF. management consultants, to examine the outcome of the scrutinies for their departments. She has decided that, on balance, there would be advantage in keeping these two exercises separate and she would be grateful if you, in conjunction with Ian Bancroft, could advise her on which two departments she might choose for the departmental running costs exercise and how best to set it up.

I am sending copies of this letter to Ian Bancroft, Derek Rayner and John Wiggins.

Yours etc,

Alvin Shinn.

Sir Douglas Wass GCB

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PRIME MINISTER

Internal Audit and Financial Control

You suggested that the second departmental case study on internal audit and financial control systems should be carried out in the MOD rather than in the DOI, as Sir Douglas Wass had proposed. (Please see your comments on my minute at Flag A).

I have discussed your proposal with him, and he has confirmed that the reasons why he thought it sensible to avoid very large departments for the second study were to save time and money. At a guess he thought that to mount an exercise in the MOD might cost £1m (since the cost of the MAFF study is £200,000) and that it might last a year. And he had ruled out the MOD in any case because, quite independently of the present exercise, they already had in hand two studies covering much the same essential area as the MAFF study. I attach the details of these two studies. Arthur Anderson and Company are represented in both the study teams.

The first study was in fact completed by the end of March of this year, and its report contained a number of recommendations for changing and improving the MOD's financial systems. These are now being considered by the MOD.

The second study, which deals with financial accountability in the MOD, is due to be completed by 30 September.

Since the financial systems ~~of~~ the MOD are, as it happens, already under review, are you content to let the second of the new case studies be done in the DOI?

In commenting on my minute at Flag A you also said that with regard to your wish to discuss the 1981 scrutiny of departmental running costs with the Ministers and Permanent Secretaries of a

/ couple of

Yes
ms

couple of departments, it would seem sensible to choose different departments from those covered by the audit study. The reason why it was suggested that we might use for this purpose the same two departments as were involved in the audit study was to save money, given that the studies of internal audit and financial control systems will embrace departmental systems for controlling running costs. But if you would like to use two different departments for the departmental running costs exercise, do you have any preference as to which are chosen? Or shall we seek the advice of the Treasury on which departments it might be sensible to alight on? *Yes*

ms

JAW

19 June 1981

CONFIDENTIAL

SIR DOUGLAS WASS

CONTROL OF DEFENCE EXPENDITURE

I promised to let you have brief details of the two financial studies which MOD have mounted with the help of management consultants.

2. The first was set in hand late in December 1980 with the terms of reference at Annex A.
3. The Study Team, which was led by Mr W Reeves, an Assistant Secretary in MOD, included two representatives of Arthur Anderson & Co (Mr Vincent Watts and Mr Dolby). The Study was completed by the end of March 1981, and its Report contains a number of recommendations for improvement and change, with which we are in general agreement, and which are now being considered within MOD. The Report, or a summary of it, together with the Departmental response, is likely to be published later this year.
4. The second study, of financial accountability in MOD, has also started. Its terms of reference are at Annex B.
5. Again, the team is led by Mr Reeves, and Arthur Anderson are providing the same two representatives (Mr Watts and Mr Dolby) to assist him. Mr Reeves also has a Treasury representative on the team (Mr Griffiths of AFA) and he has already had one meeting with Mr Littler and his Steering Group on financial control and management in Departments which was set up as a consequence of the proposals in Cmnd 8170 (The Future of the CSD). The Study Team are coming to see me and others in the Treasury on Monday afternoon.
6. I hope this will give you the information you require.


(J E HANSFORD)

19 June 1981

42-19-6

- "1. The object of the study will be:
 - (a) to review the present arrangements for monitoring expenditure, for forecasting the outturn, and for providing explanations of variations, both in volume and cash, from estimates and cash limits during the course of the financial year;
 - (b) to review the present arrangements for controlling expenditure against cash limits and the efficacy of available control measures;
 - (c) to propose improvements.

2. At 1b the study should take full account of the advantages of the block cash limit concept from which are derived the present arrangements for central monitoring and control of cash flow and which allows maximum flexibility for adjustments to be made on a defence basis during the financial year. But the case for applying the cash limit discipline to particular vote or management areas should also be considered.

3. Particular attention should be given to expenditure on goods and services supplied by industry, and to the problems of forecasting and control in changing economic circumstances, which may affect industry's performance of defence work. The present policy and practice of block adjustment should be reviewed, and account taken of the examination being given within the Department to the introduction of cash limits for firms as a means of controlling industrial capacity paid for by the defence budget and any scheme that may emerge.

4. The study should seek to establish to what extent the objective of value for money and the control of cash flow against an annual limit may necessarily be in conflict in the procurement area. It should consider whether there are trade-offs between these objectives and whether there is scope and need for change to align ordering and contracts policy and the system of annual control of cash flow more closely. Account should be taken of the present arrangements for project management in the Procurement Executive, of the way in which the Department's procurement and contract procedures contribute to the objective of securing maximum value for money and of the effect of drastic programme cuts and/or continuing uncertainty about the future programme.

5. Continuation of the PES, supply and cash limits systems and of the present rules for government accounting should be assumed but

changes in these areas may be recommended. In particular account should be taken of the consideration which has already been given, within the Department and elsewhere, to flexibility between financial years and of the extent to which innovations in this area might permit improved effective control over expenditure.

6. Account should be taken of the work so far done to analyse and quantify the reasons for the forecast overspend against the defence cash limit in 1980/81.

7. The study is to be completed by 31 March 1981."

ANNEX B

1. The main purpose of the study will be:
 - (a) to analyse the present financial procedures of the department;
 - (b) to consider clarification of responsibilities, including responsibilities for implementing PUS's directive of April 1977 (vide PUS/77/329 dated 6 April 1977 and enclosures);
 - (c) to establish the scope for simplification;
 - (d) to propose improvements.

2. At 1b, it will be necessary to take into account the full range of financial responsibilities: for approval of new requirements, for keeping under review requirements already approved, for achieving the most cost effective means of satisfying approved requirements, for the economic management of activities and the efficient use of existing resources, and for the oversight of the financial machinery of the department. The study should take account of requirements for all kinds of real resources (ie goods and services - including the services of military and civilian personnel), whether or not these requirements can be directly related to specific commitments to spend money from the defence budget and defence votes. Activities should be interpreted broadly to include, for example, training, supply systems, logistics, movements, education, hospitals. The study should in particular seek to identify those fields where the existing framework of financial control is not fully effective and those tasks which are at present neglected. Account should be taken of the development of management accounting and the ABC system and of the results of Rayner Studies. Wherever possible recommendations under this head should be in the form of the allocation of specific authorities and responsibilities to specific people.

3. At 1a, appraisals should be made:
 - (a) of the different organisation of financial responsibilities in each of the Service departments and the Procurement Executive, and of the arguments for and against similar organisations and procedures across the board;
 - (b) of the existence of parallel hierarchies and the need for them;
 - (c) of the relationships between vote management and target heading management, between line managers and specialist finance staffs (including senior finance officers), and between all these and PUS's representatives on Central Committees (Defence Equipment

Policy Committee, Operational Requirements Committee, Principal Personnel Officers' Committee, Principal Administrative Officers' Committee, etc);

(d) of the constitution and effectiveness of the Financial Planning and Management Group.

4. The study should assume continuation of the Public Expenditure Survey and Supply Systems (including cash limits) and of the present rules for Government accounting, but changes in these areas may be recommended. It should also be assumed that the present arrangements for the allocation of responsibilities of accounting officers in the MOD will remain unchanged.
5. So far as possible, account should be taken in the study of the corresponding financial procedures of our allies, particularly the USA and France.
6. The general aim of the study will be to clarify, simplify, and improve the present procedures of the department with specific reference to authority and accountability. The introduction of new procedures in particular areas is not precluded. But the study is not intended to lead to the establishment of an entirely new system of financial management throughout the department.
7. The study is to be completed by 30 September 1981. It is recognised that within that timescale detailed recommendations for change in all areas cannot be expected, but the general principle which should guide follow-on work should be firmly established.

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Mr RICKETT

16/6



INTERNAL AUDIT AND FINANCIAL CONTROL

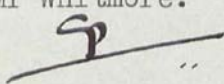
TPM
(CAW)

1. Sir Douglas Wass copied his letter of 11 June to Mr Whitmore to this office. I then obtained from the duty clerk copies of Mr Whitmore's and your letters of 1 and 3 June to Sir D Wass and his private secretary respectively. As Sir D Rayner was involved in the PM's meeting on internal audit last month which gave rise to the case studies and this office was involved in subsequent consultations, I should be grateful if any further correspondence could be copied here.

2. If the Prime Minister went ahead with the proposal to call in the Ministers and Permanent Secretaries of two departments to look into the results of their scrutinies of departmental running costs, we should be glad to contribute to the briefing in the light of our reading of the "running cost" and other evidence.

3. With regard to the DOI/Trade common services to which Sir D Wass refers in his letter of 11 June, you may like to know that a review is at present in train of at least part of those common services, namely arrangements for personnel management, including the relationships between Establishment Divisions and line management on the one hand and between the four Divisions responsible for Establishments and central finance on the other. This, for staff side reasons, is not formally part of the scrutiny programme but is in effect being treated as such. Sir D Rayner and this office have an involvement in it.

4. Finally, you should know - for your private knowledge only - that I had a long talk with one of the directors of Coopers and Lybrand, accompanied by three of his senior people, including Messrs Burnham and Plowden who will respectively be leading and assisting with the MAFF study. This was useful and I am glad to see it reflected in the letter sent to Sir Brian Hayes by Coopers and Lybrand on 5 June and now copied by Sir D Wass to Mr Whitmore.


C PRIESTLEY
15 June 1981

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Reference would be the best choice. I should be possible. A good letter could do it. I should be possible. I should be possible. I should be possible.

PRIME MINISTER

INTERNAL AUDIT AND FINANCIAL CONTROL

When you saw Sir Douglas Wass's recent progress report on the establishment of a case study on departmental systems of internal audit and financial control, you expressed reservations about the choice of MAFF for the first exercise because you felt that it was a comparatively small department with relatively low expenditure. You went on to say that we should do a pilot study in a department with high expenditure as well. I passed on your comments to Sir Douglas Wass.

He has now replied in the attached letter. He accepts that MAFF may not be a typical department but doubts whether there is such a thing as a truly representative department as far as internal audit and financial control are concerned. And he goes on to suggest that the second case study should be conducted not in one of the very big spending departments such as the DHSS or the MOD but in the Department of Industry. Sir Douglas Wass does not say so in his letter, but I imagine that one of the objections to doing a case study in one of the very big departments is that if the study was to be accomplished in a reasonable period of time and at not too great a cost (the MAFF study is costing £200,000), it would not be possible to review the totality of the department's systems but only a part of them. On the other hand, if a middle sized department is picked, the whole of its internal audit and financial control system can be looked at as a piece.

One particular attraction of doing a case study in the DOI is that you have often expressed concern that officials there do not do more when considering financial proposals from the nationalised industries than "check the arithmetic" and fail to ask basic questions about why the expenditure is needed at all, whether it is going to give value for money and what the alternative options are. A case study of the kind proposed

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- 2 -

ought to expose this kind of weakness in the DOI's system.

I have discussed Sir Douglas Wass's letter with David Wolfson and he sees advantage in doing a study in the DOI. Are you content for it to go ahead ?

David Wolfson and I have also looked at the specification for the MAFF study attached to Sir Douglas Wass's letter, and we think that this is generally on the right lines. You will see that the exercise is broken down into three stages (paragraph 7 of the specification), and it is proposed that there should be a meeting between the consultants and Sir Brian Hayes and, possibly, Mr Walker at the end of the first and second stages. David and I think that it would be a good thing if the Treasury, Sir Derek Rayner and he took part in these intermediate reviews. Do you agree ?

DR would have written

When you saw the Lord President's latest report on the 1980 scrutiny of departmental running costs, you said that you would like to see the Ministers and Permanent Secretaries from a couple of departments to discuss the results of their 1981 scrutiny and that you would like to have the help of management consultants for this purpose. We suggested to the Treasury that this was something which might be linked with the case studies of internal audit and financial control since the studies would be bound to cover, amongst other things, departmental systems for controlling running costs. Sir Douglas Wass agrees that this is a feasible way of proceeding and suggests that we here should let the Ministers concerned know that you wish to proceed in this way. May we do this with Mr Walker and, if you agree that the second case study should be done in the DOI, with Sir Keith Joseph ?

12 June 1981

*I just haven't time
before the recess. But it would
seem sensible to choose different
departments for a whole wider
audit study. not*

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H M Treasury

Parliament Street London SW1P 3AG

Switchboard 01-233 3000
Direct Dialling 01-233 3620

Sir Douglas Wass GCB
Permanent Secretary

Clive Whitmore Esq
10 Downing Street
LONDON
SW1

11 June 1981

Dear Clive,

INTERNAL AUDIT AND FINANCIAL CONTROL

Thank you for your letter of 1 June about the case study of departmental control of expenditure.

It may well be that MAFF is not representative of all departments or even of departments generally. I doubt whether there is a truly "representative" department, since each Ministry is distinctive so far as its outgoings are concerned. I suggested MAFF because it seemed to me to be reasonably typical of the generality of those departments which disburse money to achieve particular objectives of Government policy. I rejected departments like Overseas Development Administration, Foreign Office etc, because they are fundamentally different from the ordinary run of spending departments; I decided against departments like the Scottish and Welsh Offices because of their heterogeneity. I thought that the Department of Health and Social Security, the Ministry of Defence and similar giant departments were too big for a pilot study. MAFF fell into a middle, moderately typical, group which included the Department of Industry, the Department of Transport and the Home Office, to name three.

Now that we are reasonably far along the road of launching the MAFF study we can turn our attention to the selection of a second case study. I propose - and I think that David Wolfson agrees with me - that the Department of Industry would be a good department to take and I have been discussing this with Peter Carey. Peter is content to take this assignment on and would handle it in the same way that Brian Hayes is handling his. The terms of reference would be much the same and the consultants would be invited to review the whole apparatus of the department's financial control. Special emphasis would be placed on expenditure under Sections 7 and 8 of the Industry Act (including Section 7 operations in Scotland and Wales) and on regional development grants. As for the firm of consultants, Peter Carey proposes to approach Touche Ross; we agree

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that they would be well suited to this task.

As you will see from the preliminary specifications of the MAFF study, a copy of which I enclose, the costs of that study will be not far short of £200,000. But it promises to be a thorough study, and one which will closely examine the role and effectiveness of internal audit and the efficiency with which departmental programmes are administered. Peter Carey will want these points covered in his case also.

So much for the case studies themselves. In his letter of 3 June to Jonathan Taylor, William Rickett has drawn my attention to the Prime Minister's idea of following up the results of the 1981 scrutiny of departmental running costs by calling in the Ministers and Permanent Secretaries of a couple of departments, possibly plus some management consultants, to examine the outcome of the scrutinies. He asks whether the case studies exercise could be linked with this.

It could certainly be done, and this aspect of costs will be examined, as a relatively minor part of the full studies. You should note that a substantial proportion of Department of Industry running costs stems from the Common Services which are shared with the Department of Trade. So if the Prime Minister wished to examine the Department of Industry, the involvement of the Department of Trade would need to be borne in mind also. If she were disposed to follow this course it ought to be possible to ask the consultants who do the two case studies to take part in the Prime Minister's examination of each.

It will of course be for the Ministers concerned to agree to this procedure and the Prime Minister will no doubt wish to approach them or their Permanent Secretaries direct. But it certainly seems to me that there is no reason of principle or practice why the two exercises could not be linked.

I am sending copies of this letter to Ian Bancroft, Derek Rayner and John Wiggins.

Yours ever,
Douglas

DOUGLAS WASS

Sir Brian Hayes KCB
Permanent Secretary
Ministry of Agriculture, Fisheries and Food
Whitehall Place
London SW1A 2HH

our reference SH 703

5th June 1981

Dear Sir Brian

APPRAISAL OF FINANCIAL PLANNING AND CONTROL SYSTEMS

At our meeting on 21st May 1981, you invited us to put forward proposals for carrying out a study into the adequacy of the financial planning and control systems within the Ministry of Agriculture, Fisheries and Food, and the ways in which they are managed.

Terms of Reference

2 The terms of reference you suggested were:-

- (a) to examine the effectiveness and appropriateness of financial planning, control and monitoring systems in the Ministry of Agriculture, Fisheries and Food;
- (b) to identify any significant shortcomings by comparison with the highest commercial standards; and to note whether there are any features of Government operations which call for different standards;
- (c) to recommend any changes which appear to be desirable;
- (d) to report by the end of September 1981.

3 As agreed with you, we have now carried out a brief initial survey in the Ministry in order to identify the major issues to be addressed, to establish an appropriate method of working including staffing, and to prepare a preliminary estimate of our likely fee.

Issues to be Addressed

4 From the brief investigation we carried out during our initial survey, a number of major issues emerged which we suggest the main study should address, in order to meet the terms of reference. In summary, these issues are:-



- (a) the effectiveness of PES and Estimates as means of long- and short-term planning of Departmental programmes and resources;
- (b) the recording, processing, analysis, presentation and distribution of information for financial planning and control of expenditure and other resources;
- (c) the relationship between finance staff and programme/line management, including clarification of the responsibility of non-finance management for financial planning and control;
- (d) the inter-relationship between the various financial planning and control systems and other relevant initiatives (for example, scrutiny of Departmental costs and manpower targets);
- (e) the impact on the Department's financial systems of requirements by central Government and other bodies;
- (f) the adequacy of present systems for assessing the effectiveness of Departmental programmes and the efficiency with which those programmes are administered/delivered, and resources are utilised;
- (g) the effectiveness and value of internal control procedures;
- (h) the role and methods of internal audit and relationships with Departmental financial management and E & A D;
- (i) the levels of financial training and experience.

You will appreciate that our suggestions on the issues to be addressed can only be tentative at this stage. There may well be other aspects of the Ministry's operations which require consideration, which will only become apparent when the detailed work has begun. For this reason, among others, we have suggested a phased approach to the study. The first stage will provide an opportunity both to gain an understanding of the Department and also to confirm or revise our initial thoughts as to where the emphasis of the study should be placed in the subsequent stages.

Method of Working and Reporting

5 We propose that the study should be carried out in three consecutive stages, the objectives, principal work elements and target completion dates of which are described in the following paragraphs.

6 We believe that it is most important that you are apprised of progress on the study, and that we have an opportunity to discuss our findings and ideas with you during the course of the exercise. To that end, we suggested to you at our meeting that a Steering Group might be established to provide both guidance and a forum for discussion during the course of the study. We understand that you do not think a Steering Group would be appropriate but, instead, wish us to maintain close liaison with Mr Wilson and to see you at appropriate times throughout the study. This we will be pleased to do and suggest that, in particular, we should meet at the end of the first and second stages to ensure that the study is proceeding on the lines required. We also suggest that it would be appropriate to meet the Minister.

7 The suggested stages are as follows:-

Stage 1

Objective

To gain understanding of the Department, its activities and methods of operation, and to confirm the issues and areas for in-depth review in Stage 2.

Principal Elements

- (a) Programme of visits/discussions with senior and other officials and field staff, including those in other relevant departments.
- (b) Review of present planning and control systems and documentation.
- (c) Review relevant background information and reports.
- (d) Review internal audit strategy, reporting arrangements, relationship with E & A D, staffing and work plans.
- (e) Initial review of computer operations and controls.
- (f) Develop detailed programme for Stage 2.

Target Completion Date

Early July.

Stage 2

Objective

To examine the financial planning and control systems in detail, with particular reference to specific areas of the Department's activities, to identify the effectiveness in practice of the present systems and their strengths and weaknesses, and to draw conclusions.

Principal Elements

- (a) Critical in-depth review of the operation of the planning and control systems, with particular reference to the following sample areas (subject to confirmation at end of Stage 1):-

Programmes

Development and Grant Schemes
 Drainage and Flood Protection
 Research (ARC, ADAS and other)
 Other ADAS (part)

Management Unit

Region (one representative example)

Resources

Salaries
 Other Administration Costs (part)

- (b) Review internal audit procedures and documentation and samples of work and reports, including computer auditing.
- (c) Review of internal controls in selected areas, including computer operations and sample systems including planned developments.

Target Completion Date

Early September.

Stage 3Objective

To present our conclusions and recommendations on the main issues addressed during the course of the study in answer to the terms of reference.

Principal Elements

- (a) Finalisation and discussion of findings and conclusions.
- (b) Preparation and discussion of recommendations.
- (NB Precise form of consultations and reporting to be agreed.)

Target Completion Date

End September.

Staffing

8 In order to achieve the objectives of a study of this importance, we are putting forward a team drawn from our most senior staff. The study will be carried out under the overall direction of Mr Peter Burnham, the director in charge of our financial planning and systems division. Mr Burnham will be supported by Mr Francis Plowden, a senior managing consultant who assists in running that division, and Mr John Stuttard, an audit and investigation partner.

9 Mr Plowden's work will be concerned with the review of the planning, estimating and financial control systems. The detailed work on this area of the study will be carried out by Mr David Sanderson, a senior consultant, and Miss June Mulroy, a consultant, both experienced in financial planning and systems work.

10 Mr Stuttard will be primarily concerned with the internal control and internal audit aspects of the assignment, the detailed work on which will be carried out by Mr Ian Steere, a senior audit manager, assisted by an audit manager. In addition, both Mr Stuttard and Mr Steere will provide inputs to the overall review of planning and control systems with particular reference to the role that internal audit can play.

11 A specialist input to the study will be provided by staff from our computer audit group, headed by Mr Rod Perry, the partner in charge of the group. This work will be concerned with assessing the role and requirements of computer auditing and the problems of internal controls in a computer context.

12 In addition, in view of the importance of the study, we propose to make use of a consultative panel to provide overall guidance and advice to the consulting team. This will be led by our senior partner, Mr David Hobson, and comprise the senior partners from our management consulting, investigation and public sector auditing divisions.

13 We welcome the availability promised of Mr Brian Dickinson's time and the attachment to the team of Mr Paul Elliott. The provision of accommodation and secretarial duties, as discussed with Mr Wilson, are also of considerable importance.

Fee Estimate

14 At this stage we estimate that the assignment will take a total of just under 100 man weeks, split as follows:-

	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>	<u>Total</u>
A Planning, estimating and monitoring systems	11	25	12	48
B Internal control, internal audit procedures and strategy	6	16	4	26
C Computer controls and audit	3	5	1	9
D Direction and advisory	<u>3</u>	<u>5</u>	<u>4</u>	<u>12</u>
	<u>23</u>	<u>51</u>	<u>21</u>	<u>95</u>
	<u>=</u>	<u>=</u>	<u>=</u>	<u>=</u>

The detailed breakdown of those figures is shown in Appendix A to this letter.

15 You will appreciate that this time estimate is based on a short survey of a complex and specialist area. It is, therefore, subject to a number of uncertainties as to the depth required of certain areas of investigation and the emphasis to be placed on different aspects of the Ministry's operations. The detailed work programme to be prepared at the end of the first stage, and which would be discussed and agreed with you, is designed to clarify these areas of uncertainty and to confirm or modify the staff inputs suggested. Progress would then be monitored against that programme, which would be updated in the light of actual achievements and our findings as the study proceeds. Any further changes in inputs or major re-allocation of resources would also be agreed.

16 Our fees will be charged on the actual time spent on the assignment at the following rates:

	<u>£ per week</u>
Partner/Director	2,135
Managing consultant	1,625
Senior consultant	1,225
Consultant	1,025

These rates are our standard rates, which are revised every six months and notified to the Civil Service Department. A copy of our last letter to the CSD on that subject is attached. The next fee revision is due at 1st July 1981 and will be notified to the CSD. We have made an allowance in our fee estimate for the likely change in rate.

17 On this basis, our fee for the assignment will be of the order of £150,000, exclusive of VAT and out-of-pocket expenses such as any travelling and accommodation expenses, which are charged in addition. A copy of our standard terms and conditions is attached at Appendix B.

18 We are very pleased to have been asked to carry out such an important assignment and shall be pleased to provide any further information that you may require.

Yours truly

COOPERS & LYBRAND ASSOCIATES LIMITED

Ministry of Agriculture, Fisheries and FoodOutline Staffing Plan

	<u>Man weeks</u>			<u>Total</u>	<u>Fee</u>
	<u>Stage 1</u>	<u>Stage 2</u>	<u>Stage 3</u>		<u>Estimate</u>
					<u>£</u>
<u>A Planning, estimating & monitoring systems</u>					
F Plowden	4	4	2	10	
D Sanderson	-	7	4	11	
J Mulroy	5	9	3	17	
J Stuttard	1	1	1	3	
I Steere	1	4	2	7	
	<u>11</u>	<u>25</u>	<u>12</u>	<u>48</u>	63,000
<u>B Internal control, internal audit procedures & strategy</u>					
J Stuttard	2	3	1	6	
I Steere	4	1	1	6	
Audit manager(s)	-	12	2	14	
	<u>6</u>	<u>16</u>	<u>4</u>	<u>26</u>	34,500
<u>C Computer controls & audit</u>					
R Perry	1	1	1	3	
Senior manager	2	4	-	6	
	<u>3</u>	<u>5</u>	<u>1</u>	<u>9</u>	14,000
<u>D Direction and Advisory</u>					
PM Burnham	2	3	2	7	
Other	1	2	2	5	
	<u>3</u>	<u>5</u>	<u>4</u>	<u>12</u>	25,500
	<u>23</u>	<u>51</u>	<u>21</u>	<u>95</u>	137,000

Allowance for fee rate increase at 1/7/81 11,000

£148,000

COOPERS & LYBRAND ASSOCIATES
LIMITED
MANAGEMENT CONSULTANTS

MANAGEMENT CONSULTING SERVICES

Standard Terms

1. Unless otherwise agreed with the client, fees are charged for the actual time spent by the individuals working on the assignment at agreed hourly, daily and weekly rates.
2. Weekly fee rates for consulting staff are based on a working week of five seven-hour days. No charge is made for time worked in excess of normal hours, unless previous agreed with the client, or for absence due to sickness or holidays.
3. The fee rates quoted are subject to periodic review. Unless specified to the contrary, the fees quoted do not cover the cost of travelling, accommodation and other out-of-pocket expenses incurred in connection with the client's business, or the costs of preparing reports or specifications, including drawing office and printing costs. The actual costs incurred are therefore charged in addition to our fees.
4. Unless otherwise agreed, fees and expenses are invoiced monthly and are payable within seven days of the presentation of our invoice.
5. Experience has shown that it is in the client's own interest to ensure that our consultants are provided with the accommodation, facilities (including secure storage facilities for confidential data) and secretarial assistance normally available to the client's own senior executives.
6. Assignments are undertaken on the mutual understanding that clients will not offer employment to our staff and that we, on our part, will not induce the client's staff to seek employment with us.
7. C&L undertakes to treat confidentially any information it may obtain regarding the present or future business activities of the client. This obligation devolves upon all members of C&L individually and is a condition of their contract of service.

Govt Mail

CF Lhle



10 DOWNING STREET

cc: Mr Wadson.
Civil Service Feb 80
Scrutiny of Dept
running costs

From the Private Secretary

BF 10.6.81

3 June, 1981.

Dear Jonathan

Internal Audit and Financial Control

Clive Whitmore wrote to Sir Douglas Wass on 1 June about the setting up of a case study of department's systems of internal audit and financial control. Sir Douglas Wass ought to be aware of a link that has developed between this work and the "annual scrutiny of departmental running costs".

Sir Douglas will probably have seen my letter to Jim Buckley of 1 June reporting the Prime Minister's response to the Lord President's latest report on the 1980 scrutiny of departmental running costs (copy attached). In addition to the points set out in this letter, the Prime Minister has said that she would like to call in a couple of departments, and discuss with the Ministers and Permanent Secretaries concerned the results of the 1981 scrutiny. She has also said that she would like the help of management consultants in quizzing these departments on the results of the 1981 scrutiny.

Sir Douglas may like to consider whether this remit can be taken care of in the follow-up work on internal audit and financial control. The terms of reference of the case studies now being set up could be widened to include examination of the annual scrutiny of running costs within the departments concerned. The reports of the consultants would then help the Prime Minister to have constructive discussions with the Ministers and Permanent Secretaries involved on the results of the 1981 scrutiny. These discussions could perhaps be separate from those she will undoubtedly hold on the reports' conclusions on internal audit and financial control.

Perhaps Sir Douglas could comment on this suggestion when he replies to Clive Whitmore's letter of 1 June.

I am sending copies of this letter to John Wiggins and Jeremy Colman.

Yours ever
William Rickett

J.M.G. Taylor, Esq.,
HM Treasury.

RB



10 DOWNING STREET

From the Private Secretary

1 June 1981

Subject: Civil Service

File No: Scrutiny of Dept. Running Costs.

Dear Jim

1980 Scrutiny of Departmental Running Costs

The Prime Minister was grateful for the Lord President's minute of 11 May reporting the outcome of the analysis of the 1980 scrutiny of Departmental running costs that was commissioned at Cabinet on 29 January. She was also grateful to Sir Derek Rayner for his minute of 18 May, and to the Chancellor of the Exchequer for his minute of 28 May.

The Prime Minister attaches great importance to this scrutiny exercise. She considers it essential when Departmental running costs are rising at a rate of 25% a year. She recognises that the 1980 exercise was very much a pilot run. But she feels that there are a number of ways in which the scrutiny, and the subsequent analysis reported by the Lord President, could have been improved. She would like her comments to be taken into account in the 1981 scrutiny, now under way.

First, the Prime Minister feels that the scrutiny exercise should help to ensure that Ministers do all they can to reduce the running costs of their Departments, and that it should also ensure that Ministers learn from the practices of other Departments. She is therefore concerned to say that she agrees with Sir Derek Rayner that the Lord President's paper gives no real feeling for the effectiveness of Departmental efforts at keeping down costs and achieving specific savings. If Ministers are to learn from their colleagues, it is important to identify and disseminate the "best" practices within Departments. The Prime Minister therefore agrees with Sir Derek Rayner that for this and subsequent years' scrutinies Ministers should be given clear statements of the positive measures taken by their Departments to achieve cost reductions, together with details of the savings achieved. These statements should be reported collectively to Ministers by the Lord President.

She would also be grateful for the Lord President's advice on whether it would be possible to pick out from the figures produced by the scrutiny "key ratios" or "performance indicators" which could help Departmental managers assess their performance, and compare it, with other Departments. Perhaps the Financial Management Coordination group of officials could be asked to look at this in the context of their other work on the scrutiny (see below).

/ The Prime Minister

The Prime Minister recognises that the main value of the running costs exercise is to help Ministers improve practices within their Departments. But she also sees the exercise as enabling Ministers to consider collectively the demands made on Government resources by Departmental running costs. These costs, at £8300 million a year, are a significant demand on public funds, and the annual increases in these costs are also very substantial. The Prime Minister agrees with Sir Derek Rayner that Ministers should consider the possibilities of reducing non-staff administrative costs when they are taking decisions on public expenditure generally. She notes that Mr. Hayhoe has asked Ministers to submit the results of the 1981 scrutiny to him by mid-September; and she hopes that a paper can be circulated to Ministers collectively as soon as possible after that.

The Prime Minister acknowledges that there is a risk that the scrutiny of running costs will duplicate other management information systems. She therefore agrees to the Lord President's proposal that the Financial Management Coordination Group of officials should consider how the Departmental running costs exercise should be integrated with other work on management information systems.

Finally, the Prime Minister feels very strongly that the figures for running costs reported to Cabinet in January should be published. As I have already mentioned to you, she would like these figures to be annexed to the Government's White Paper on efficiency. She has agreed with the Lord President's recent proposal that we should aim to publish this White Paper by the end of June. It can then form the basis for the forthcoming enquiry by the Treasury and Civil Service Select Committee into efficiency in Government.

I am copying this letter to the Private Secretaries to Ministers in charge of Departments and to the offices of Sir Robert Armstrong and Sir Derek Rayner.

Yours sincerely

William Ricketts

Jim Buckley, Esq.,
Lord President's Office.

MINISTRY OF AGRICULTURE
FISHERIES AND FOOD



WITH THE COMPLIMENTS
OF
SIR BRIAN HAYES KCB

WHITEHALL PLACE
LONDON SW1A 2HH



Sir Brian Hayes, K.C.B.
Permanent Secretary

G. M. M. M.
Ministry of Agriculture, Fisheries and Food
Whitehall Place
London, SW1A 2HH

1 June 1981

*ALL
20*

Dear Douglas,

INTERNAL AUDIT AND FINANCIAL CONTROL

Perhaps I could comment briefly, and simply for the record, on one point you made in your letter of 27 May to Clive Whitmore.

You quote Douglas Henley, in his report of internal audit, as including MAFF "in a group of departments which he described as being among neither the best nor the worst". This is not in fact what Douglas said. He said in paragraph 9 of his memorandum: "I emphasise that the four units in Appendix B are mentioned purely for illustration, and not because they are notably better or worse than others". In his letter of 20 January to Anthony Rawlinson he said that the four units had been put forward "as illustrative of internal audit in central government, not because they are particularly good - or bad". Finally, in his evidence to the PAC on 6 April he said: "I hope that the Committee will not press me on naming departments. I have very particularly not done so in my memorandum, either from the point of view of those which exhibit what we would regard as good practice or those which are not so good".

I hope you will agree with me that by these statements Douglas has not placed MAFF internal audit in any particular category of quality, and in fact has been careful not to do so. I have of course no means of knowing where we rank, because I do not know enough of other Departments' practice. Nor do I know where Douglas would privately rank us. I suspect that he chose us because we were to some extent representative of the range of problems that internal audit faces - and that in turn, of course, makes us a good choice for an independent study. But that is a different matter from saying that we represent average quality: until Cooper and Lybrand have reported on us I hope we can stay out of any category, whether good, bad or indifferent!

I am sending copies of this letter to Ian Bancroft, Clive Whitmore, John Wiggins
and David Wolfson.

*Yours ever,
Brian*

BRIAN HAYES

Sir Douglas Wass GCB
HM Treasury
Parliament Street
LONDON
SW1





10 DOWNING STREET

File AH
cc Tsy
CSD
David Wolfson

From the Principal Private Secretary

1 June 1981

BF 10.6.81

Dear Douglas,

INTERNAL AUDIT AND FINANCIAL CONTROL

Thank you for your letter of 27 May 1981 reporting progress on the establishment of a case study of a department's systems of internal audit and financial control.

I have shown this to the Prime Minister. She is concerned that MAFF may not provide a representative case study. She has commented that it is a comparatively small department with comparatively low expenditure. She would like to see another case study done simultaneously in a department with a large budget. She accepts that Cooper and Lybrand would not be able to carry out this study in addition to the one in MAFF and that another firm of consultants would have to be used. I should be grateful for your views on the Prime Minister's proposal.

I am sending copies of this letter to John Wiggins and Ian Bancroft.

Yours ever,

David Wolfson.

Sir Douglas Wass GCB

AH



Prime Minister.

This now seems to be going well after the original wishes.

H M Treasury *Consent to proceed as Sir Douglas*
Parliament Street London SW1P 3AG *Wass suggests?*

Switchboard 01-233 3000
Direct Dialling 01-233 3620

Sir Douglas Wass GCB
Permanent Secretary

Clive Whitmore Esq
10 Downing Street
LONDON
SW1

R Whitmore O.V.

*I do not think that
MAFF is the right choice. It is
a comparatively small department with
comparatively low expenditure. We
must do a high expenditure
department as well. D.H.S.G?
Orkney's firm
to do it - not*

27 May 1981

INTERNAL AUDIT AND FINANCIAL CONTROL

You may like to report to the Prime Minister how we are getting on with the idea of a case study, first suggested at the meeting she held on this subject on Thursday 5 May.

Brian Hayes has agreed, with the support of his Minister, to institute a study in the Ministry of Agriculture, Fisheries and Food. He has approached Cooper and Lybrand, who have responded with great interest, and is now waiting for them to complete preliminary enquiries and give him an outline of the proposed study as they see it and an estimate of the likely cost. It is intended that the study should range widely over internal audit and other aspects of financial management, planning and control in the Ministry. What is to be required is primarily an appraisal, rather than a blueprint of any new system, but the consultants will be asked to indicate directions of desirable improvement wherever they have criticisms of existing arrangements.

I am sure that Cooper and Lybrand are as good a choice of consultants as could be made - they figured in both the recommendations given to the Prime Minister in response to her recent discreet enquiries.

I hope that MAFF will prove to be not only an interesting case on its own, but one capable of offering lessons of wider application. Douglas Henley in his report of internal audit included it in a group of departments which he described as being among neither the best nor the worst. It offers a suitable scale and variety of Government activities and financial responsibilities.

I decided against a wider coverage than one department for this case study - not least in the interests of speed. I gather that Brian Hayes is having to press Cooper and Lybrand quite hard to get them to agree to report by the end of September. Inclusion of a second

2/3

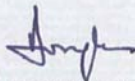
department would inevitably have lengthened and complicated the study, without necessarily producing more 'typical' evidence.

There could of course be advantage in getting wider and more varied coverage and I am considering the possibility of a parallel study in another department - probably using different outside consultants. I propose, however, to wait and see first how Brian Hayes gets on with the arrangements for his study, which may give us some useful guidance in approaching a second case.

I shall keep in close touch with progress, and either Brian or I will ensure that the Prime Minister sees the report which the consultants produce.

I am sending a copy of this letter to John Wiggins, Ian Bancroft and David Wolfson.

Yours ever,



DOUGLAS WASS



DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 6691
SWITCHBOARD 01-212 7676

K J Sharp TD

Head of the
Government Accountancy Service

12 May 1981

Clive Whitmore Esq
Private Secretary to the Prime Minister
10 Downing Street
London SW1

WM
N.A. 46

Dear Whitmore

I understand that at a reception last week to launch the Business Opportunities Programme the Prime Minister asked the President of the Institute of Chartered Accountants in England and Wales why there were not more good accountants ... in the civil service. She may find the attached briefing note on the subject useful.

I am sending copies of this to Ian Bancroft, Robert Armstrong and Derek Rayner.

Yours sincerely
K J Sharp

K J SHARP



THE USE OF ACCOUNTANTS IN GOVERNMENT SERVICE

There are approximately 1,150 qualified members of the six recognised UK accountancy bodies employed in the Home Civil Service. Of these about 665 are the direct concern of the Head of the Government Accountancy Service (HGAS), the others (detailed in the annex) being employed in the external audit services or in specialist departmental functions. In addition some 530 civil servants are training for full professional qualification (235 in the GAS, and 295 in the external audit services).

2 For a long time, and particularly since the publication of the Fulton Report, there has been pressure on the civil service from Parliament, the profession and the informed press, to achieve better and wider use of accountancy skills. In November 1975, Mr K J Sharp, the immediate past-President of the Institute of Chartered Accountants in England and Wales, was appointed as the first HGAS with the principal task of improving the input of accountancy skills in Government by the creation of a strong Government Accountancy Service. (He is also Accountancy Adviser to the Secretary of State for Industry.)

THE PROBLEM

3 The two main barriers to an increase in the accountancy input in Government were identified by Mr Sharp as:

- a) lack of commitment among officials to its achievement; and
- b) the separation of accountants between the Professional Accountant (PA) Class and the Administration Group, which frequently prevented the use of good accountants in areas such as finance traditionally reserved for administrators.

These combined to present the civil service as an unattractive career to many good accountants and did not encourage bright young civil servants to train to qualification as a route to career advancement.

THE PROPOSED SOLUTION

4 The solutions to these problems are interlinked. Much of top management is now committed to developing the use of accountants. They have endorsed a major initiative to overcome the structural problem by bringing members of the PA Class together with accountants in the Admin Group to form a "functional specialism" within the Admin Group. Negotiations are proceeding with the trade unions concerned and a target date of July 1982 has been set for implementation.



5 While the combination of more positive personnel management and wider career opportunities which the structural changes will permit is seen as the most practical means of achieving a lasting increase in recruitment and retention of good accountants for the service, top level commitment will continue to be necessary to achieve the better use of accountancy skills. Large sections of middle management remain sceptical, largely due to insufficient understanding of the contribution which a good accountant can make. (Finance is still regarded by many as a low level function and accountants as bookkeepers.) This problem will only decline as senior managers allow more accountants to demonstrate their value in wider financial areas and as they devote a more substantial effort to training able young civil servants to professional qualification.

PROGRESS TO DATE

6 Although the necessary fundamental changes must await completion of the negotiations referred to above, progress within the existing framework has resulted in:

- 1) more accountants in the GAS, more widely dispersed through the Service;
- 2) more senior accountancy posts (typically at Assistant Secretary level);
- 3) more secondments between the GAS and the private sector - inwards providing expertise, outwards to gain experience;
- 4) a greater emphasis on accountancy training for good numerate civil servants (though more still is needed);
- 5) a greater degree of central management of accountants;
- 6) substantial support from the accountancy profession at large for the efforts of HGAS;
- 7) better dialogue between Whitehall and the profession.

NEXT STEPS

7 Continued recruitment of accountants from the private sector, though not easy, should be enhanced under the proposals. In a highly competitive market pay and conditions on entry are reasonably in line. The wider and more interesting career opportunities which will become available should, in part, compensate for an inability to compete with the potential rewards and speed of advancement open to the most able in the private sector. In the short term, the recession has produced a surplus of qualified accountants. It

/should ...



should now be possible to fill outstanding vacancies and the need, recently confirmed by the Comptroller and Auditor General's memorandum to provide trained auditors for internal audit functions within departments can be met if the service can quickly identify its requirements.

8 In the longer term it is likely that good accountants will continue to be a scarce resource in the service for some time. Inwards secondment and the use of consultants may be a necessary interim measure until the introduction of an attractive and worthwhile career structure. Over time this will create a position where, as in the private sector, a significant number of top level posts are held by accountants and their influence is pervasive throughout Whitehall. This process has started but will need sustained effort over a long period to carry it to a successful conclusion.

G A S

12 May 1981

THE USE OF ACCOUNTANTS IN GOVERNMENT SERVICE: DETAILED STATISTICS

Number of Accountants Employed in the Service

Professional Accountant Class	384	Recruited as qualified accountants, and mainly employed in Government's dealings with industry and commerce, eg procurement, assistance to industry.
Administration Group Group	281	Mainly trained within the service and employed in line accounting posts in Trading Funds and other quasi-commercial activities.
Sub Total	665	The Government Accountancy Service
Exchequer and Audit Department	43	Out of an audit staff of about 650. E & AD now trains all its recruits to professional qualification.
District Audit Service	245	Out of an audit staff of about 350. DAS now trains all its recruits to professional qualification.
Dept of Trade Insolvency Service	54	Out of a professional staff of about 350. Accountancy training, but not full qualification, is a substantial part of the training for this group.
Inland Revenue Tax Inspectorate	140	Professional training in accountancy is not essential but is one means of entry to the Tax Inspectorate.
Sub Total	482	
Total	1147	

2 Government Accountancy Service Analysed by Grade

	<u>Total</u>	<u>PAClass</u>	<u>Admin</u>
Open Structure	2	2	-
Principal Director	1	1	-
Assistant Secretary	27	15	12
Senior Principal	51	26	25
Principal	165	105	60
SEO	285	218	67
HEO	111	17	94
EO	23		23
	665	384	281

3 Government Accountancy Service: the Main Employing Departments

	<u>Total</u>	<u>PAClass</u>	<u>Admin</u>
Defence	351	156	195
Industry	95	84	11
Inland Revenue	41	33	8
Environment/PSA	28	13	15
Scottish Office	21	15	6
MAFF/IBAP	18	17	1
CSD	16	6	10
HMSO	16	16	-
DHSS	14	7	7

4 The Accountancy Institutes

The six UK accountancy institutes, whose members are eligible for entry to the PA Class, are:-

- The Institute of Chartered Accountants in England and Wales
- The Institute of Chartered Accountants of Scotland
- The Institute of Chartered Accountants in Ireland
- The Association of Certified Accountants
- The Institute of Cost and Management Accountants
- The Chartered Institute of Public Finance and Accountancy

These institutes act in association, through the Consultative Committee of Accountancy Bodies, in making representations to Government.

The GAS regards each of these institutes as having a contribution to make to Government Service and does not regard any as having special status.



10 DOWNING STREET

From the Private Secretary

11 May 1981

C/7 file RB
cc: As below +
Mr Wolfson
Govt Mail

At the meeting last week on internal audit and financial control, it was suggested that the help of outside management consultants should be sought.

The Prime Minister had a word with the Governor about this last week. She asked in particular if he could suggest which firms could best help with improving our computer audit arrangements. The Governor has since telephoned me and, for what it is worth, I thought I should pass on to you what he told me. He said that, on the basis of advice he had taken from within the Bank, the following firms, and in the following order of merit, could help the Government:-

Cooper and Lybrands;
Ernst and Ernst;
Deloitte's;
Peat Marwick; and
Thomson McLintock.

I am sending copies of this letter to Ian Bancroft and Derek Rayner.

T. P. LANKESTER

Sir Douglas Wass, G.C.B.,
H.M. Treasury.

A

cc to Mr. Wolfson

SUBJECT

JS

cc CSD
CO
Mr. Wolfson



10 DOWNING STREET

From the Private Secretary

7 May 1981

INTERNAL AUDIT AND FINANCIAL CONTROL

The Prime Minister held a meeting at 1700 hours on Tuesday 5 May with Sir Douglas Wass, Sir Ian Bancroft, Sir Derek Rayner and Mr. David Wolfson. The purpose of the meeting was to review the programme for improving the quality of internal audit within the Civil Service described in the letter of 20 March from Sir Douglas Wass and Sir Ian Bancroft to Sir Brian Hayes and other Heads of Departments. This programme had been prompted by a memorandum from the Comptroller and Auditor General reviewing Departments' internal audit systems, completed in February 1981.

The Prime Minister expressed her concern at the apparently tentative nature of the proposed programme. She recalled that Mr. Whitmore had written to Mr. Wiggins on 20 March emphasising the need for all Departments to review their audit systems. She was therefore concerned at the apparent lack of urgency in the deadlines set out in the letter to Heads of Departments for reviewing the objectives of their internal audit sections, for deciding the job descriptions of the heads of these sections, for agreeing the composition of these sections, and for reviewing computer audit systems. To make progress quickly outside consultants should be retained to scrutinise internal audit systems within Departments, and perhaps to look as well at the wider question of financial control systems as a whole. It was not enough for Departments to concentrate on simple accountancy and the detection of abuse: there was a clear need for greater efficiency in the use of resources. This suggested that there was perhaps a need to review not just audit systems but also investment appraisal techniques, and for giving finance staff within Departments a stronger voice in decisions on investment control.

Sir Douglas Wass and Sir Ian Bancroft explained that the system of Cabinet Government delegated considerable responsibility to Ministers and Departments, and this limited the freedom of the Treasury and the CSD to require Departments to take action. But they had impressed on Heads of Departments the urgent need for action on internal audit and they believed that their words had been heeded. Moreover, the fact that there were deficiencies in internal audit systems did not necessarily mean that control

/ systems

HC

systems generally were inadequate. The criticisms of the Comptroller and Auditor General had been confined solely to departmental internal audit systems. There was a group within the Treasury headed by Mr. Littler studying resource and financial management. There was also the Accountancy, Finance, and Audit Division of the Treasury, which could provide Departments with a management consultancy service. The deadlines set for the review programme on internal audit might appear long, but Departments were large and the task was considerable.

Sir Douglas Wass said that political and other considerations sometimes meant that decisions on investment issues were not based strictly on financial factors. It was the duty of departmental Finance Officers and the Treasury, to ensure that Ministers were aware of the financial consequences of their decisions. It was not necessarily the case that investment appraisal systems were inadequate or that finance staff did not have sufficient expertise.

Sir Derek Rayner said that in his experience it was not possible to rely on line management, even in large companies, to introduce internal audit systems. Outside advice on systems and instruction on how best to use them were needed. Such training was required at all levels, but it was particularly important for senior management to recognise the value of internal audit. The Civil Service was lagging behind the best practices outside. The necessary training and advice could perhaps be best provided by a group of outside consultants retained by the Treasury for one or two years. They would help build up the small central unit that would be needed to give Departments the leadership they would require when introducing and keeping up to date the best internal audit practices.

As regards investment appraisal, the assumptions used were often over-optimistic. On other occasions, Principal Finance Officers were over-ruled for political reasons. There might be a case for giving Principal Finance Officers the option of reporting to the Treasury when decisions were taken by their Departments against their advice.

The Prime Minister, summing up the discussion, said that it would be helpful if Sir Douglas Wass, in conjunction with Sir Derek Rayner, could arrange for case studies to be carried out of internal audit systems as they operated now in one or two Departments. The agreement of the Ministers and Permanent Secretaries concerned would need to be sought. The help of outside management consultants should be used. Mr. Wolfson would consult Sir Arnold Weinstock to see whether he could suggest suitable consultants.

I am copying this letter to Jeremy Colman in Sir Ian Bancroft's office and to Clive Priestley in Sir Derek Rayner's unit.

(SGD) W. RICKETT

J.M.G. Taylor, Esq.,
HM Treasury.

cc Mr Wolfson A type

WR
7/5

DRAFT LETTER TO PRIVATE SECRETARY TO SIR DOUGLAS WASS

Internal Audit and Financial Control

The Prime Minister held a meeting at 1700 hours ^{on Tuesday 5 March} yesterday with Sir Douglas Wass, Sir Ian Bancroft, Sir Derek Rayner, and Mr. David Wolfson. The purpose of the meeting was to review the programme for improving the quality of internal audit within the Civil Service described in the letter of 20 March from Sir Douglas Wass and Sir Ian Bancroft to Sir Brian Hayes and other Heads of Departments. This programme had been prompted by a memorandum from the ^{Comptroller} ~~Controller~~ and Auditor General reviewing Departments' internal audit systems, completed in February 1981.

The Prime Minister expressed her concern at the apparently tentative nature of the proposed programme. She recalled that Mr. Whitmore had written to Mr. Wiggins on 20 March emphasising the need for all Departments to review their audit systems. She was therefore concerned at the apparent lack of urgency in the deadlines set out in the letter to Heads of Departments for reviewing the objectives of their internal audit sections, for deciding the job descriptions of the heads of these sections, for agreeing the composition of the sections, and for reviewing computer audit systems. ^{To make progress quickly} ~~She said that in her view this demonstrated that there was a need for outside consultants to~~ ~~be retained to scrutinise internal audit systems within Departments, and perhaps to look at the wider question of financial control systems as well.~~ ^{as well} ^{a whole} It was not enough for Departments to concentrate on simple accountancy, and the detection of abuse; there was

/a clear

a clear need for ~~a~~ greater efficiency in the use of resources. This suggested that there was perhaps a need to review not just audit systems, but also investment appraisal techniques, and for giving finance staff within Departments a stronger need ~~will~~ ⁱⁿ for decisions on investment control.

Sir Douglas Wass and Sir Ian Bancroft explained that the system of Cabinet Government delegated considerable responsibility to Ministers and Departments, and this limited their freedom ^{of the Treasury and the CSD} to require Departments to take action. But they had impressed on Heads of Departments the urgent need for action on internal audit. Moreover, the fact that there were deficiencies in internal audit systems did not necessarily mean that control systems ~~overall~~ ^{generally} were inadequate. The criticisms of the ^{sup} Controller and Auditor General had been confined solely to departmental internal audit systems. There was a group within the Treasury headed by Mr. Littler studying resource and financial management. There was also the ^{of the Treasury} Accountancy, Finance, and Audit Division which could provide Departments with a management consultancy service. The deadlines set for the review programme on internal audit might appear long, but Departments were large and the task was considerable.

~~On the question of investment appraisal raised by the Prime Minister,~~ Sir Douglas Wass said that political and other considerations ^{sometimes} occasionally meant that decisions ^{on investment cases} were not based strictly on financial ^{factors} considerations. It was the duty of ^{departmental} finance officers, and the Treasury, to ensure that Ministers

/were

and they believe that their words have been heard

were aware of the financial consequences of their decisions. It was not necessarily the case that investment appraisal systems were inadequate or that finance staff did not have sufficient expertise.

Sir Derek Rayner said that in his experience it was not possible to rely on line management, to ^{introduce} implement internal audit systems. Outside advice ^{on systems} and instruction ^{how best to use them} on ~~methods of~~ ^{systems} ~~was~~ ^{needed} ~~needed~~ at all levels, but it was particularly important for senior management to recognise the value of internal audit. ^{The Civil Service was lagging behind the best practice outside.} The necessary training and advice could perhaps be best provided by a group of outside consultants retained by the Treasury for one or two years. ^{Mr. Wolfson agreed with Sir Derek Rayner that there must be pressure on Departments from the Treasury and the CSD, and that Departments must be encouraged to take expert advice.}

When in large companies,

They would help build up the small central unit that would be needed to give Departments the necessary leadership and co-ordination and help up to date with internal audit practice.

^{As regards} On the question of investment appraisal, ~~Sir Derek Rayner~~ said that there was often a problem of optimism in the assumptions used for appraisal. ^{As Sir Derek Wass had said,} Finance Officers were occasionally overruled. There might be a case for ^{highlighting} the importance of financial considerations by allowing Finance Officers to deny accountability for decisions taken against their advice.

to be carried out
*
from 14

The Prime Minister, summarizing the discussion, said that it would be helpful if Sir Douglas Hogg, in conjunction with Sir Derek Rayner, could arrange. In conclusion it was agreed that outside consultants should be retained to study the financial control and internal audit departments. ^{for case studies of internal audit systems as they operated now in one or two departments.} The help of ^{external} management consultants should be used. The Controller and Auditor General's memorandum would give an indication of which Departments

should be chosen so as to give a representative sample.

*
to Mr. Wolfson

The agreement of the Ministers and Permanent Secretaries

concerned would need to be sought. ~~But as the first step~~

Mr. Wolfson would ^{consult} talk to Sir Arnold Weinstock ^{to see whether he could suggest} on the

~~question of suitable consultants. Sir Derek Rayner also~~

~~agreed to advise on suitable candidates. Sir Douglas Wass~~

~~agreed to discuss the terms of reference of these studies~~

~~with Mr. Wolfson and Mr. Priestley.~~

Since this meeting, } the Prime Minister has also }
approached Sir Gordon Richardson and Mr. Raisman of Shell }
for advice on suitable } outside consultants. }

I am copying this ^{with} to Jeremy Colman & in Sir Ian Bancroft's
Office ^{at} to Clive Priestley in Sir Derek Rayner's unit ~~and to~~
~~David Hoffman.~~

PRIME MINISTER

Gov head

ms

Internal Audit

Papers:

Flag A: A brief offered by Mr. Priestley, which brings together the main issues.

Flag B: The note from Mr. Priestley which led you to call this meeting.

Flag C: The Wass/Bancroft letter to Permanent Secretaries.

Flag D: The Chancellor's minute, covering the C&AG's paper on internal audit.

/

CAW

10 April 1981

CONFIDENTIAL

cc Sir Derek Rayner

Mr WHITMORE

BRIEF FOR MEETING ON INTERNAL AUDIT, 18 00, 10 DOWNING STREET,
13 APRIL 1981

DOCUMENTATION

1. I attach the relevant correspondence together with a copy of the final version of the Comptroller and Auditor General's recent report.

BACKGROUND NOTES

2. I also attach background notes on:

(1) The function, status and state of internal audit, including the C&AG's criticism.

(2) Internal audit in perspective.

THE PURPOSE OF THE MEETING

3. The purpose of the meeting might be:

(1) to invite Sir D Wass and Sir I Bancroft to report on the intended programme of reform;

(2) to register the importance the Prime Minister attaches to internal audit as one part of good financial management; and

(3) to indicate how the Prime Minister's interest should be served in future.

← 4. The Prime Minister might like to open by asking Sir D Wass and Sir I Bancroft to bring her up to date. She might then invite observations from Sir D Rayner.

5. The Prime Minister will no doubt wish to emphasise at some point that she sees internal audit as only one part of financial and other resource management. It needs to be set in perspective as but one aspect of the Government's interest in and plan of reform for the totality of management, including its financial basis; the systems for planning, controlling and evaluating the use of resources; and the development of people with the right combination of experience and training to take responsibility for management, both in the line and at the centre within departments. The Rayner "lasting reforms" package is highly relevant to this as is the recent expression of the Prime Minister's decision on the future of the CSD.

THE INTENDED PLAN OF REFORM

6. The essential elements in the letter issued jointly by Sir D Wass and Sir I Bancroft on 20 March are:

- (1) The Treasury will lead. It is the Department principally concerned at the centre with the design and maintenance of the overall system of resource control. The line of responsibility descends from Sir D Wass, through Sir A Rawlinson (Second Secretary), Mr Littler (Deputy Secretary) to Mr Carey (Under Secretary) whose charge now includes Accountancy, Finance and Audit Division (Mr Walker, Assistant Secretary), just transferred from CSD. The Treasury will have a particular responsibility for defining requirements, for example in computer audit, and for driving the programme forward.
- (2) The CSD will help, particularly on matters of training, recruitment and pay.
- (3) Departments (on whom the main responsibility for good management falls) are asked to agree



with the Treasury:

- by 30 September the objectives of their internal audit
 - plus the job description of the head of the unit
 - plus proposals for filling it;
- by 30 June 1982 the composition of their units, if only provisionally;
- by 31 December 1981 a course of action to bring computer audit up to scratch in three years.

POINTS FOR THE PRIME MINISTER TO MAKE

7. I suggest that the Prime Minister might make these points:

- (1) Picture painted by the C&AG not wholly black. But dark enough to be very worrying. Ministers must be able to rely on Permanent Secretaries to ensure that all their management arrangements, not just internal audit, are beyond reproach. But internal audit specially sensitive where it is a matter of money going astray: that is bad in itself but it also makes for lack of confidence in government management as a whole.
- (2) Therefore very disappointed to learn that Treasury and CSD accept as valid the C&AG's criticisms, meaning that systematic abuse would probably go undetected.



(3) But all that is water under the bridge. We are now at least facing in the right direction. Accept, too, that there ^{are} genuine difficulties. Computer audit is a new science, outside as well as inside Government. And good accountants have not been easy to recruit.


(4) Have two main interests here. First, see internal audit as just one part of good financial and resource management. Do not want to get it out of perspective. Would therefore like a free-ranging report on where we now stand on improving management as a whole in the light of Rayner "lasting reforms", eg the management job of Permanent Secretaries, training of Principal Finance Officers. Look to Sir D Rayner to supply this.

(5) Secondly, on internal audit itself, the question is, how fast and determined will the new departure be? Would like the following:

- A particular Treasury official to be designated as leader of the exercise and to report via the Chancellor during the summer on progress made. What would be the right experience and qualifications of this officer?
- The programme should be driven forward with determination. Is the timetable in the joint letter appropriate for this?

[NB I understand that the determination is there at working levels and that Principal Finance Officers in general want to make progress. The Treasury is

now engaged in devising a programme of work. The timetable looks leisurely, but I understand that the Treasury is encouraging departments to get on without waiting for the target dates noted above.]

-  What about using a firm of professional accountants with the appropriate expertise? Even if it is not a matter of devising one single model of internal audit for the whole government service, how about using a firm or firms in particular departments, both to help with their problems and to provide read-across?

- (6) Send good wishes to AFA Division on its transfer from CSD to Treasury.

[NB This Division, consisting mainly of professional accountants, is pretty blameless. It has been doing its best for a long time, with somewhat fitful support and encouragement until comparatively recently. A word of support from the Prime Minister would be both a welcome boost for the staff concerned and helpful to their immediate superiors.]

- (7) While the Treasury should not needlessly harry departments, it should monitor their progress with the reform programme. Look to Sir D Wass to put appropriate pressure on Permanent Secretary colleagues.



HEAD OF THE GOVERNMENT ACCOUNTANCY SERVICE

8. The Prime Minister may like to be reminded that she invited, some weeks ago, a joint report from Sir D Wass and Sir D Rayner on the location of the Head of this Service (known as HOTGAS). This report is in hand.

9. HOTGAS is being consulted on the programme but feels very strongly, as does Sir D Rayner, that it should be driven forward by a designated leader in the Treasury.

SP

C PRIESTLEY
10 April 1981

Encs: Background notes

Chancellor of the Exchequer's minute of 11 March
to the Prime Minister

Mr Whitmore's letter of 20 March to Mr Wiggins,
HM Treasury

Mr Wiggins's reply of 2 April, covering joint letter
from Sir I Bancroft and Sir D Wass of 20 March to
Permanent Secretaries

C&AG's report

FUNCTION, STATUS AND STATE OF INTERNAL AUDIT INCLUDING THE
C&AG's CRITICISMS

1. When a Permanent Head of Department signs the Appropriation and other Accounts which he submits to Parliament on behalf of his Minister in his capacity as "Accounting Officer" for his Department's Votes, he takes personal responsibility for their correctness.

2. The basic function of internal audit is therefore to provide a Permanent Head with a means, independent within his organisation, of assessing control systems to show whether or not they prevent fraud or misappropriation.

3. However, the wider function of internal audit is to:

- review the administrative, accounting and other procedures operated day in-day out to ensure their efficiency
- appraise parts of the organisation in a way which the line managers responsible for them may be unwilling or unable to do
- help external auditors do their job more economically.

4. Permanent Heads are advised by the Treasury (1) to employ an internal audit unit and (2) on its role, staffing and working methods. But there is no statutory or mandatory requirement here. How far each Permanent Head goes has until now been left for him to decide.

5. In Government, the emphasis has so far been mainly on "regularity and propriety audit", ie on the avoidance of fraud and misappropriation. There has been a relatively slow movement into "systems-based audit", ie placing more

emphasis on systems of control and management than on checking individual transactions. The business of computer audit is new for everyone, in both Government and outside.

6. On the regularity/propriety front, Sir I Bancroft wrote to Permanent Heads in July 1980 about evidence which suggested an increase of fraud within the Civil Service, saying that cases notified for the periods 1970-80 totalled about £1.2m, some involving more than £30,000 each. He asked them to take a look at

- (1) In particular, control over travel and subsistence claims; and
- (2) the adequacy of their internal audit arrangements generally.

(In an article on Tuesday last, the TIMES recalled a fraud on the FCO by one of its bookkeepers involving £384,000 and the judge's comment that it had been made possible by lack of competent supervision.)

7. The previous Public Accounts Committee emphasised the importance of internal audit "in maintaining an effective system of financial control, particularly where large and complex schemes of financial support are involved" (Third Report 1979-80). The Chairman of the present PAC, Mr Joel Barnett, has told Sir Derek Rayner that he intends to keep a firm grip on the subject. He and his colleagues are now considering a report by the Comptroller and Auditor General which, as the Chancellor warned the Prime Minister in his minute of 11 March, has attracted adverse publicity.

8. The C&AG's broad assessment is that:

- (1) Despite much useful work and recent efforts to up-rate their performance, "the overall standard of internal audit units is substantially

below the level needed" (para. 10).

- (2) The "almost universal absence of an adequate capability to audit computer-based systems" is particularly disturbing.
- (3) No other weakness is so prevalent, but "the standard of audit varies sharply from unit to unit, and the differences of philosophy between departments are implicit in varying degrees of independence and scope allowed to internal audit".
- (4) There are other differences in staffing, professionalism and working methods, eg in the use made of the "systems-based approach" (see above).

8. The C &AG believes that "three underlying factors tend to militate generally against improvements" (paras. 11-14):

- (1) Although one or two departments have established high level audit committees to oversee internal audit, "there appears to be a fairly general failure by senior management within Departments to appreciate the potential benefits of an efficient, modern internal audit".
- (2) There is a general lack of professionalism in the approach to staffing. Of the 1,650 staff in the thirty-seven departmental units covered by the report, about 60% of all internal auditors are very junior, being Executive or Clerical Officers. Tours of duty are too short, which diminishes the incentive to be proficient, especially in computer audit as this "necessitates more intensive training over a longer

period". (As I observed in an earlier minute, the problem is thus essentially one of amateur financial controllers being advised by amateur auditors.)

- (3) There is no Service-wide career structure for internal auditors.

INTERNAL AUDIT IN PERSPECTIVE

1. Internal audit is just one part of good financial and other resource management.

2. The White Paper on The Future of the CSD said that the Government intended to "press forward vigorously with measures to improve financial control and management in Departments. These measures include:
 - more effective planning and control of the cash cost of programmes of public expenditure

 - further development of financial responsibility and accountability in line management

 - better matching of the financial information needed for the Public Expenditure Survey and Estimates with that need for management

 - the strengthening of internal audit in Departments" (Cmnd 8170, para. 27).

3. An equally important measure is ensuring that Finance Branches are staffed with "full regard to experience, in-Service training and external qualifications" (para. 31).

4. Sir Derek Rayner is shortly to take a meeting of Treasury and CSD officials on the subject of training for financial management. Other relevant work in the "lasting reforms" programme includes defining the responsibilities of Permanent Heads and top officials for good management, including those of Principal Finance Officers and line managers.

5. As Sir Anthony Rawlinson (HM Treasury) told the Public Accounts Committee on 6 April, the Treasury has set up a Financial Management Co-ordination Group to push all these measures forward and to assist Sir Derek Rayner. It consists of:

Mr J G Littler, Chairman (Deputy Secretary, HM Treasury)
Mr K J Sharp (Head of the Government Accountancy Service)
Mr J P Charkham (Under Secretary, CSD, Head of the
Management and Organisation Group)
Mr C Priestley (chief of staff to Sir Derek Rayner)

INTERNAL AUDIT IN CENTRAL GOVERNMENT

Memorandum by the Comptroller and Auditor General

Paragraphs

- 1 - 6 The role of internal audit
7 The relationship between external and internal audit
8 E&AD review of internal audit
9 - 14 (i) General findings.
15 - 18 (ii) Audit of computer based systems
19 (iii) Small organisations
20 Conclusions
21 - 22 - On the role of internal audit.
23 - On the need for substantial change
24 - 29 - On centralised Service-wide action
30 - On action by individual Departments
31 - 32 - On the relationship between internal audit and E&AD
33 Summary

Appendix

- A Results of E&AD's review of internal audit in central government
B Internal audit in four major Departments

Audit House
Victoria Embankment
London EC4

February 1981

INTERNAL AUDIT IN CENTRAL GOVERNMENT

Memorandum by the Comptroller and Auditor General

The role of internal audit

1. The Treasury's letter of appointment which is sent to each new Accounting Officer provides a full statement of his responsibilities and draws attention inter alia to his traditional duties for the safe-guarding of public funds and property and the propriety and regularity of the expenditure from those funds. The guide on Government Accounting which is issued by the Treasury for use in all Government Departments states that it is desirable that systems of control established to ensure the propriety, security, completeness and accuracy of departmental activities and transactions should be subject to objective review. The guide concludes that the Accounting Officer will normally employ an internal audit branch or section to undertake this work.
2. The guide also recognises that the internal audit section will normally assist the Accounting Officer in meeting his responsibility for ensuring that his Department's business is conducted economically and efficiently, that is, by undertaking "value for money" audit. But in this area the Accounting Officer will often also deploy other skilled staff, eg management services and staff inspection teams, which will affect the degree to which he calls upon internal audit for such assistance.
3. It may be noted that the Institute of Internal Auditors in the United Kingdom has defined internal auditing as an independent appraisal function established within an organisation to examine and evaluate its activities as a service to that organisation, with the objective of assisting members of the organisation in the effective discharge of their responsibilities.
4. In 1973 the Civil Service Department (CSD), in consultation with the Exchequer and Audit Department (E&AD) and the Treasury, issued guidance to all departments in the form of a booklet

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entitled "Internal Audit in the Civil Service". The booklet provided advice on such matters as the organisation and training of internal audit units; the audit approach and methods to be adopted; and the principles of internal control. CSD regarded an internal audit operating on the lines recommended as an essential feature of good departmental management. In 1977 CSD supplemented that guidance by issuing minimum standards for internal audit in departments. These are consistent with standards subsequently issued by the Chartered Institute of Public Finance and Accountancy and the Institute of Internal Auditors. The CSD standards specify the requirements for internal audit's independence, training, unrestricted scope, limited responsibility for safeguards against fraud, and quality of management and of reporting. The salient points of CSD's guidance and standards have been embodied in the Treasury's guide on Government Accounting.

5. In signing the Appropriation and other Accounts rendered to Parliament, the Accounting Officer takes personal responsibility for the correctness of (or true and fair view exhibited by) those Accounts. He is advised by the central Departments to employ an internal audit unit to help him discharge his responsibilities: and he is given advice about the role, staffing and working methods most appropriate for such a unit. Internal audit in central government is thus an accepted concept. But the establishment of an internal audit unit is not governed by any statutory or mandatory administrative requirement, and how far each Accounting Officer goes in accepting the central Departments' advice is left to him to decide.

6. An internal audit unit will be expected to earn its keep in terms of a cost-effective contribution to financial control and the economic use and management of resources. The direct cash savings achieved by internal audit may be significant but they are not the only, or indeed the main, criterion. It has for long been found by large and complex organisations in both public and private sectors that the existence of an independent unit which reviews the administrative, accounting and other procedures which are operated day by day throughout the business is necessary to ensure that they remain efficient and

/do not

do not become either top heavy or inadequate. The unit should also assess control systems to consider whether they provide an adequate deterrent to fraud or misappropriation. Furthermore it can be valuable in providing top management quickly with an objective appreciation of sectors of the organisation of a kind which cannot be obtained from line management. Finally, an efficient internal audit can and should enable external audit to perform its work more economically. Some or all of these factors also apply to smaller organisations, and the provision of internal audit support to smaller Government departments and non-departmental bodies is one of the matters dealt with below.

The relationship between external and internal audit

7. The statutory role of the C&AG as external auditor in central government is to provide an independent assurance for Parliament regarding the accuracy of the accounts prepared by departments, and on the regularity of expenditure recorded therein. The C&AG is required to report to Parliament on his audit. In giving his audit opinion on accounts he takes note of work done to an acceptable standard by the internal auditor, and normally designs his audit work to avoid duplication of the work carried out by the latter. The basic difference between the two audit roles is that the external auditor reports to Parliament whereas the internal auditor reports to the Accounting Officer. But given the measure of independence properly accorded to internal audit within Departments it is entirely right and economic for E&AD to determine its own work programme in the light of its assessment of the adequacy of standards of internal audit and knowledge of its work.

E&AD review of internal audit

8. Internal audit units at present exist in 43 departments, including all the major departments. During 1980 my officers undertook a broad review of all the units in major departments and a number of those in smaller departments and non-departmental bodies. This aimed to provide an initial analysis of performance

/by different

by different units on a uniform basis. The review covered 34 organisations, with annual transactions, (expenditure plus receipts) totalling in excess of £130,000 million; total staff, including military personnel, of about 1,180,000; and internal audit staff totalling about 1,650 in 37 internal audit units. This represented more than 95 per cent of internal audit activity in government departments, though excluding the Department of Energy because internal audit there has been under separate examination in pursuance of PAC's recommendation in their Third Report of Session 1979-80.

(i) General findings

9. In Appendix A I summarise the general results of the review by reference to the generally accepted main ingredients of a fully effective internal audit, and in Appendix B I give brief details about four internal audit units to illustrate the present stage of development of internal audit. I emphasise that the four units in Appendix B are mentioned purely for illustration, and not because they are notably better or worse than others.

10. My broad assessment of the results is that, although much useful work is undertaken, and despite recent efforts in many Departments with CSD guidance and encouragement to improve their performance, the overall standard of internal audit units is substantially below the level needed to fulfil the role recommended by the CSD and Treasury. A particularly disturbing feature is the almost universal absence of an adequate capability to audit computer-based systems (see below). No other weakness is so prevalent, but virtually all units show other specific shortcomings which limit their effectiveness. As indicated by the factors itemised in Appendix A, the standard of audit varies sharply from unit to unit, and differences of philosophy between departments are implicit in the varying degree of independence and scope allowed to internal audit. Other differences exist in staffing, professionalism and working methods; for example, in the use made of the systems-bases approach.

11. In my view, three underlying factors tend to militate generally against improvements.

12. First, there appears to be a fairly general failure by senior management within Departments to appreciate the potential benefits of an efficient, modern internal audit providing the accounting Officer with the full range of assistance referred to in paragraph 1 above. In this context, however, I welcome the establishment by one or two departments of high-level audit committees to oversee internal audit activity: this implies an encouraging recognition of the important contribution which internal audit can make and I hope the practice will be followed widely.

13. The second point is the approach to staffing. There is a general lack of professionalism. About 60 per cent of all internal auditors in departments are Executive Officer or Clerical grade staff. Both these and staff in higher grades are assigned to tours of duty in internal audit work, in many cases 3 years or less - too short a time to become adequately trained and effective auditors before they are transferred to non-audit duties elsewhere in their departments. This factor impedes the use of modern audit methods. Moreover, staff who know they are likely to move out of audit will have less incentive to become proficient auditors. The rapid turnover is of special relevance to computer audit because the nature of that work necessitates more intensive training over a longer period, and existing arrangements have seriously impeded units' efforts to train their own computer auditors to an effective level.

14. Third, responsibility for the duties, structure and staffing of internal audit units rests mainly with individual departments; and there is no service-wide career structure for internal auditors. It seems questionable whether the needs of individual departments are sufficiently different, or their knowledge of audit methods sufficiently great, to justify this fragmented approach. And, despite the guidance available from the CSD, and the experience and knowledge which individual Departments have in their own fields, it is now extremely

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difficult for them to provide and maintain the increasing expertise they require for fully effective internal audit work.

(ii) Audit of computer based systems

15. The rapid pace of computerisation, and of technological developments in the computing field, poses new and challenging questions to all auditors. In central government most major accounting systems are now computer based, and purely manual systems of any great significance will soon be a thing of the past. The capability to undertake computer audit is therefore absolutely essential for effective internal audit of most Departments.

16. Moreover, the complexity and scale of, and potential risks involved in, computer operations are such that the auditor needs to be involved from the start in the development of all new computer applications if he is not to risk being left stranded by a system which he does not understand and cannot examine. Thus, E&AD has found it necessary to establish and, in recent years, considerably expand a specialist computer group equipped with the skills needed to evaluate computer installations and systems and to develop and operate computer audit software.

17. During 1979 and 1980, as part of a wider examination of computer installations and systems in departments, the E&AD computer group reviewed the performance of internal audit on computer systems audit. In 29 cases where it was possible to reach conclusions as to the general standard in the department as a whole, the group found that computer audit was non-existent or poor in 20 cases, of variable quality in 8 cases and quite good in one case only. Several departments were taking action to improve the position, but the group concluded that there were insufficient trained computer auditors in internal audit, that the frequency of staff changes often frustrated plans for improvement, and that it was unlikely that an acceptable level of computer audit would be attained while staff spent only a limited period in internal audit.

18. These conclusions are wholly consistent with the results of two studies in selected departments which CSD completed during 1980. CSD found that an unduly low proportion of internal audit effort was devoted to computers, and that training fell so far short of needs that there were few if any internal auditors equipped to undertake an effective audit of computer based systems. Not surprisingly, they concluded that the general standard of computer audit was poor.

(iii) Small organisations

19. There are 28 small departments where Accounting Officers are responsible for Appropriation Accounts but have no internal audit unit. These departments have total annual voted transactions in excess of £450 million, and some of them also deal with trust funds or other non-voted moneys. Similarly, some small non-departmental central government bodies have no internal audit. While the scale and nature of these organisations' transactions may make them more straightforward to audit, there can be a relatively higher degree of risk because small organisations cannot so easily achieve effective accounting controls based on separation of duties, nor do they always command a very high standard of accounting expertise. These problems and dangers become even more acute with the continuing spread of computerisation of accounting systems.

Conclusions

20. The main questions raised by this review appear to be:

(i) Is the important role for internal audit which is set out in the guidance given by the Treasury and CSD generally accepted?

(ii) Is it agreed that substantial changes are essential if internal audit is to play that role effectively throughout central government?

(iii) Would some of the necessary action be best tackled on a centralised Service-wide basis?

/(iv)

- (iv) What are the main priorities for action by individual Departments?
- (v) What are the implications for the relationship between internal audit units and E&AD?

21. On the role of internal audit, all major Departments clearly accept in principle the suggestion by the Treasury and CSD that Accounting Officers should arrange for objective review of their systems of financial control, etc, and have set up internal audit units. But setting up the unit is only the first step. It does not appear to be generally appreciated that for the unit to be effective it needs to use modern methods and techniques and to apply them over the whole field (paragraph 1 above). Accordingly internal audit should not be regarded as an optional extra or as a lower level of audit activity. It should be treated as an essential departmental requirement; be applied to the full range of financial activities - though in a structured manner having regard to risk and materiality; and be managed and to a significant extent conducted by staff as well qualified as external audit staff.

22. It must be emphasised that there is a world of difference between the mechanical or half-informed application of routine audit processes, and skilled auditing by well-trained staff who adopt the systematic but flexible approach with which modern methods are intended to be used, and who can apply experienced audit judgement to their findings. A mechanical audit, systems based or otherwise, is not a near-substitute for such work. If, at the extreme, it were to waste the time of both management and audit staff, and give an unjustified feeling of assurance that all was well, it would be worse than useless.

23. On the need for substantial change, there seems to be very little room for doubt. This conclusion is supported by the attention already being devoted to the subject in a number of Departments, though not always in those where this review

/indicates

indicates the greatest need for change. The nature and scale of change needed appears to vary somewhat from one Department to another. It is not possible on the basis of this review to provide an overall estimate of the desirable changes in the numbers and gradings of staff. The dominant impression, however, is of a need for a greater proportion of more professional, highly graded, staff, but not necessarily for larger numbers overall.

24. On centralised, Service-wide action, there is scope for extension of the role hitherto played by the CSD both in issuing general guidance and through training provided at the Civil Service College. In February 1981 the Government announced in Cmnd. 8170 that they agreed with the Treasury and Civil Service Department Committee's suggestion that CSD's Accountancy, Finance and Audit Division should be transferred to the Treasury, and that they intended to press forward vigorously with measures to improve financial control and management in departments, including the strengthening of internal audit. If substantial changes are to be achieved across the Service, Departments will expect and require some vigorous central co-ordination; it is here that the Treasury and CSD will wish to consider with Departments how this should be developed. For the objective goes beyond a straightforward expansion of numbers of staff in order to increase the volume of routine checks on transactions or on systems of control: it is a more sophisticated process of improving efficiency and cost-effectiveness in audit work by the application of modern systems-based audit methods which are constantly developing and are not widely understood outside the auditing profession.

25. There would seem to be a particularly urgent need for a revised Service-wide understanding of the qualifications and training required for internal auditors. There will also be a need for the Treasury and CSD to establish criteria to assist Departments to specify the work to be done by their internal audit units and to assess, at least provisionally, the numbers and grades of staff required. Until provisional decisions are taken on these matters it will hardly be possible to organise

/the necessary

the necessary training or to prepare plans for the various changes which it will inevitably take several years to implement fully.

26. The need for early action on computer audit poses a special problem, again seeming to call for a co-ordinated approach and for additional training facilities. The Treasury and CSD will no doubt have this in mind in the light of their own reviews of computer audit (paragraph 18 above).

27. But it is questionable whether an extension of CSD's traditional role on guidance and training is all that should be undertaken centrally. There is clearly a case to consider for the establishment of a Service-wide cadre of internal auditors, who would be subject to centralised professional oversight. The main objectives would be to enable each Department to obtain an adequate number of fully trained staff; to secure the maintenance of a high level of professional standards; and to provide a career structure in internal audit which would facilitate the recruitment and retention of suitable staff. Individual Departments would no doubt also wish to include in their internal audit units other staff from their own departmental sources who, after training, would be assigned for tours of duty and then return to non-audit work.

28. The establishment of a Service-wide cadre of internal auditors could make a major contribution towards the particular problem of improving computer audit. For it would provide the conditions under which those staff could remain on audit work long enough to acquire and use the necessary skills and knowledge; and for those with the right aptitude to specialise and become expert and, over a period, gain wide experience at a variety of computer installations. Such strengthening of Departmental internal audit units might need to be complemented by the establishment in the Treasury of a small central corps of computer audit experts to provide training and advice and carry out special assignments. But computer audit should not be entirely hived off from the Departmental units and undertaken centrally: the objective should be to create arrangements under

/which

which the bulk of computer audit is undertaken as an integral part of the work of the Departmental units.

29. As for those Departments and other bodies who consider themselves too small to set up their own internal audit units (paragraph 19 above), it should be possible to establish in the Treasury a central internal audit unit to provide not only this service but also the additional accounting expertise which some of them lack.

30. The main priorities for action by individual Departments will have to be considered by Departments themselves in the light of their particular circumstances. I would offer the following general comments:

- (a) The Accounting Officer and his Principal Finance Officer (or equivalent) should provide, and be seen to provide, active support for internal audit units. The status of these units and the impact of their work depend critically on that support. The establishment of high-level audit committees to oversee their work and periodically to consider their results is well worth consideration. On the other hand, "raiding" them when staff is temporarily short elsewhere in the Department not only indicates that a low value is placed on their work but is inimical to the necessary development of highly skilled auditing.
- (b) Most of the possible central developments mentioned in the previous paragraphs will take time to mature: some may require lengthy consultation before decisions are taken. Action by individual Departments should have regard to these possibilities but cannot wait for them to be dealt with first. A number of Departments have recently reviewed their own internal audit units; others might usefully do so in the light of this Memorandum and against the standards and guidance which CSD have already issued, with the objectives of specifying the work to be done by the units and assessing the staffing needs. E&AD would be willing to assist in this process.

/(c)

- (c) Changed attitudes to staffing these units could be implemented without delay. Staff should be selected carefully, taking account of aptitude and potential for a more professional approach to audit work in the future. Even those not seeking a career in internal audit should expect to remain on audit work long enough to be adequately trained and to operate as fully experienced and effective auditors. The period could vary, but anything less than 4 or 5 years is unlikely to be worthwhile. Promotion on internal audit work should be possible.
- (d) As is emphasised throughout this Memorandum, modern accounting systems and audit methods demand a high degree of expertise in the auditor. A marked change of emphasis towards the employment of high quality staff is therefore essential; and increased attention should be paid to training.
- (e) In many units, the method of auditing needs revision. Too much emphasis tends to be placed on routine checking of transactions and too little on the evaluation and testing of systems of control. In practice, however, a suitable and properly structured systems-based approach is unlikely to be devised and introduced successfully unless expert guidance is obtained.

31. The formal relationship between internal audit and E&AD will not be affected by changes to improve the effectiveness of internal audit. As remarked in paragraph 7 above, their responsibilities differ: an internal audit unit reports to the accounting Officer, the external auditor reports to Parliament. But if the internal units were staffed and conducted as envisaged in this Memorandum, and contributed to an effective evaluation of those authorisation and control systems which are material to the C&AG's audit opinion, and the assurances he has to give to Parliament, E&AD would be able to place greater reliance on them and by avoiding duplication could reduce the overall resources devoted to financial and regularity audit.

32. The opportunities for fruitful cooperation should also be enhanced. This is desirable and I believe acceptable between E&AD and the central Departments on general aspects of audit approach, method and training; and between E&AD and internal audit units on the operational planning of audit work and on its detailed execution in individual Departments. Good working relationships exist at present, and there is already a fair degree of useful cooperation. A greater similarity in the staffing and general approach to financial and regularity audit should make close cooperation possible on a much wider basis and enable the objectives of internal and external audit to be met more fully and more cost-effectively in the future. I would welcome similarly increased cooperation on the value for money work undertaken by E&AD and internal audit units, notwithstanding the need for the C&AG to report on certain matters to Parliament.

Summary

33. In this Memorandum, I have recorded the results of the review carried out by E&AD in 1980 and my conclusion that the overall standard of internal audit units is substantially below the level needed to fulfil the role recommended by the CSD and Treasury. I have suggested a package of remedial measures for consideration. The key points are general recognition of the potential role of internal audit and new staffing arrangements for the units. Progress on these would clear the way for general improvements. But without such progress, I consider that the underlying problems will continue to detract from the effectiveness of internal audit.

Exchequer and Audit Department
February 1981

APPENDIX A

RESULTS OF E&AD'S REVIEW OF INTERNAL AUDIT
IN CENTRAL GOVERNMENT

The results of the E&AD review of internal audit are presented under 7 headings, and indicate the more significant points on which actual performance was found to deviate from the CSD's or other generally recognised standards for internal audit.

(A) INDEPENDENCE AND STATUS

- (1) A few internal audit units were located in Accounts Branches, or otherwise subject to management direction or restriction. Over one-quarter of the units had non-audit responsibilities which detracted from their effectiveness on audit.
- (2) The majority of heads of internal audit were of Principal or lower grade, whereas line division heads were usually of Assistant Secretary grade. This relatively low status reduced the impact of their reports unless internal audit was seen to have the full and enthusiastic backing of the Accounting Officer and his Principal Finance Officer.

(B) SCOPE

- (3) about one-quarter of the units examined did not cover all of their organisations' financial activities, and the responsibilities of a similar number were not defined in writing.
- (4) About half the units did not give the Accounting Officer specific assurances before he signed formal Accounts for rendition to the C&AG.

(C) STAFFING

- (5) Internal audit staff numbers vary considerably in relation to the scale of different departments' financial transactions. These variations reflect factors such as the nature and complexity of the Departments' transactions and geographical organisation and the extent to which they fund outside bodies subject to other forms of audit. There appear nevertheless to be some inconsistencies in staffing levels.
- (6) Internal audit staff were heavily concentrated (over 60 per cent) in the Executive Officer (EO) or clerical grades; these grades undertook the bulk of the basic audit work. By contrast, E&AD has found that the bulk of such work needs to be undertaken by staff of higher Executive Officer or Senior Executive Officer grading and calibre.
- (7) Postings to internal audit were usually part of general career patterns. Tours of duty were frequently less than 3 years, too short a time to become adequately trained and effective auditors.

(D) TRAINING

- (8) Only about 2 per cent of central government internal auditors were professionally qualified: many units had no professionals at all.
- (9) Nearly all units made use of CSD's basic training courses for internal auditors. However these courses were of short duration and limited depth and were not intended as a substitute for professional qualifications.
- (10) Few internal auditors had training adequate to enable them to undertake the audit of computer installations and systems.

(E) PLANNING

- (11) About half the units examined had no long-term plan to ensure that all areas subject to audit were covered in a defined period.
- (12) The overall quality of planning varied widely, and in about half the units it did not indicate relative priorities and risk areas.

(F) AUDIT OPERATIONS

- (13) In about one-third of the units the work was based on examination of individual transactions rather than primarily on systems: many units made little or no use of aids to audit such as flowcharting, ICQs and statistical sampling.
- (14) The quality and maintenance of audit programmes and standing files varied considerably; there was therefore a risk that staff, especially those with limited training or experience, did not spend their time to best advantage.

INTERNAL AUDIT IN FOUR MAJOR DEPARTMENTS

Appendices B(1)-(4) give some brief details about internal audit in 4 departments:

- B(1) - Ministry of Agriculture, Fisheries and Food
- B(2) - Department of Education and Science
- B(3) - Home Office
- B(4) - Property Services Agency (Department of the Environment)

Between them, these illustrate most of the points listed in appendix A and show that they do not apply equally to all units. These examples are intended to be illustrative; they do not signify that internal audit is necessarily more or less effective in these 4 departments than in central government generally, nor are they presented as complete evaluations.

The structure and responsibilities of the 4 departments, and the scope of their internal audit units, vary considerably. For these reasons, the apparent variations between their audit staff numbers in relation to the values of payments/receipts do not necessarily indicate significant differences in standards of audit. It should also be noted that in addition to internal audit, the Departments also employ staff on management services and staff inspection duties which may affect the extent to which the Accounting Officers call on internal audit for assistance in ensuring that departmental business is conducted economically and efficiently.

- (15) Although about half the units examined made some use of computer interrogation, over half accepted that they could not cover computer based systems effectively.

(G) PROGRESS MONITORING, REVIEW AND REPORTS

- (16) About one-third of the units did not systematically monitor progress of audit work.
- (17) In a few cases, senior officers did not review audit work to assess the validity of conclusions; in other cases, review did not always cover the supporting documentation.
- (18) A few organisations did not require their line managers to reply in writing to all internal audit reports, and some units did not invariably pursue their reports to determine whether satisfactory action had been taken.
- (19) A few units did not report regularly to the Accounting Officer or the Principal Finance Officer on the results of their work, and a larger number did not have periodic meetings with the AO, PFO or senior line managers.
- (20) In about half the organisations examined it was not the practice for internal audit representatives to attend meetings held to plan and progress changes in systems of internal control.

Ministry of Agriculture, Fisheries and Food

Payments and receipts total about £580 million.

The internal audit unit is headed by an Assistant Secretary, who reports to the Principal Finance Officer but has a right of direct access to the Accounting Officer. The audit branches are free from management restriction. A separate branch within the unit undertakes costings and management accountancy but has no audit duties.

In September 1980 the unit's staff complement was 188 and the numbers in post were 156, of whom 74 were EOs and 28 were of lower grades. Following a recent staff inspection the unit is moving towards a complement of 160 including 80 EOs and 24 lower grade staff. Of these about 27 are employed in the costings branch, and the equivalent of 33 staff undertake audit and verification work on behalf of the Intervention Board for Agricultural Produce. As a result the staff in post engaged on audit of the Ministry headquarters and regional organisations and of its associated non-departmental bodies (to which there is an appropriate degree of access) was 96. This number may fall further as a result of the departmental-wide manpower economies which the Ministry is required to achieve during the next 3 years. Tours of duty average upwards of 5 years. The unit contains a number of professional accountants (16 in September 1980), but has difficulty in recruiting and retaining them.

In the past, the unit has not operated standard planning procedures to control the audit work, but it is currently adopting a more consistent basis. Similarly, the unit has previously based much of its audit on examination of a standard proportion of transactions, but is now adopting the systems based approach. The unit submits an annual report to the Principal Finance Officer and examines formal Accounts to be rendered to the C&AG.

All of MAFF's transactions are brought to account through a computerised system. Internal audit use the computer to select transactions for their audit tests and they have started to evaluate the computerised processes. The unit is taking steps to improve its computer audit expertise, including a three-months training attachment of one member of its staff to E&AD's Computer Group.

Department of Education and Science

Receipts and payments total about £3,420 million (including those of the Office of Arts and Libraries).

The internal audit unit has 10 staff, headed by a Senior Principal (part-time). The unit has a full-time Principal with audit experience who is supported by a part-time SEO, 3 HEOs and 4EOs. The two part-time staff have other responsibilities relating to matters which are subject to audit examination, while the remainder of the unit is concerned solely with internal audit duties. The unit also calls on the services of the Department's professional accountants. Its terms of reference are clearly defined and it generally operates independently. It does not report on formal accounts to be signed by the Accounting Officer and rendered to the C&AG.

The Votes for which the DES and OAL are responsible include payments to 7 bodies with their own Accounting Officers for the grant in aid account. Apart from universities where, by convention agreed by PAC, the DES Accounting Officer need not normally be involved, the grant-aided bodies employ about another 25 internal auditors. For some of these bodies DES internal audit has only limited access.

Before 1980 the unit's audit work was transactions-based. In preparation for a change in approach an interim programme of work gave priority to those accounts involving large payments, frequent transactions or problems of control where the risks were thought likely to be the greatest. The programme was approved in advance, reports were issued on each audit and a summary of progress was included in the unit's annual report. In June 1980 the unit introduced a systems-based approach and the audit assignments have been selected with regard to a detailed analysis of risk. The unit is also seeking to establish detailed planning of each assignment against which progress

/can be

can be monitored. At the time of surveying the audit field the unit estimated that with existing resources it would take over 3½ years to deal with the Department's own accounts (excluding visits to grant-aided bodies), and they intended to develop a long range plan to cover the most critical areas on a cyclical basis.

DES operates large scale computerised accounting systems, but the internal audit unit contains no fully trained computer auditors and has not been able to cover these areas adequately. An officer with computer experience has recently been appointed to help deal with this aspect.

Home Office

Payments and receipts total about £1,860 million. (This figure includes some £140 million audited by the internal audit unit of the Lord Chancellor's Department on behalf of the Home Office).

The internal audit unit is headed by a Principal and forms part of the Accounts Branch, where it sometimes undertakes work on behalf of line management. In 1979-80 the staff complement was 34, but the actual numbers in post averaged only 22, including 18 of EO or lower grade. The complement has since been reduced to 29, but with a higher proportion of grades above EO. The unit includes no professional accountants. The average tour of duty has been about 3 years. The unit does not examine the whole range of the Home Office's financial activities, and does not report on formal accounts.

Examination is not systems-based, resources being applied mainly to checking of transactions arising at outstations such as prisons. The unit contains no trained computer auditors and although it has made a contribution on at least one developing system it does not have the expertise or resources to cover the Department's full range of computerised accounting systems.

The above position is in the course of change. At the Home Office's invitation, CSD examined the internal audit arrangements in the Home Office during 1978-79 and in a report at the end of 1979 recommended significant changes. These include:

- The internal audit unit to be organised as an independent entity, separate from the Accounts Branch.
- Internal audit's scope to extend to all financial matters.

- Establishment of a section to specialise in computer audit, headed by an "appropriately qualified" SEO.
- Chief Internal Auditor and two other staff to be professional accountants.
- More emphasis on systems-based audit.

Most of these and other recommendations have been accepted by the Home Office. A number of substantial changes in line with the report have already been made and other recommendations will be implemented as the necessary staff can be recruited and trained. This will inevitably be a gradual process.

Property Services Agency (Department of the Environment),
excluding PSA Supplies

Receipts and payments total about £1,750 million, including some payrolls for other departments.

In November 1979 the internal audit unit was separated from the Accounts Division following a recommendation of the PSA Management Review Steering Committee. Under the new arrangements, the unit comes within PSA's Professional Accountants Unit (PAU); the Director Accountant in charge of the PAU is the Head of internal audit and he reports to the Principal Finance Officer, with the right of direct access to the Accounting Officer.

The unit's staff (excluding staff on Supplies audit) averaged about 65 in 1980, including 35 EOs and 4 COs. The Head of internal audit and two of his senior staff are professional accountants. The unit's responsibilities extend to all relevant PSA financial activities, and it operates independently of management, but it does not report on formal accounts. A high-level Internal Audit Committee, chaired by the Principal Finance Officer, reviews the unit's work regularly.

The unit bases its work on annual and long-term audit plans. Much of the work is becoming systems-based, making use of modern techniques including flowcharting and statistical sampling, but the unit has not yet been able to deal fully and effectively with computerised functions. PSA operates a major computer installation at Hastings, which processes a high proportion of its financial transactions and deals with a variety of large-scale accounting functions, but the unit's computer audit has suffered from staff shortages and lack of expertise, and it had experienced some difficulty in obtaining places on specialised training courses. As a result, up to the beginning of 1980 the unit had carried out no systems audit on the main Vote accounting function for more than 4 years. The only previous review, in 1975, had not been fully documented. The unit has made some progress in the use of computer interrogation

A joint PSA/Treasury review of the internal audit function
in PSA is due to start in April 1981.

CONFIDENTIAL

Prime Minister

Mr WHITMORE

(Can I talk with D-R and with Sir) - W. 21.11.82

You said the letter from the Chancellor's office which today. Contact for me to write on the lines of the draft reply or 'yes'?

INTERNAL AUDIT: Mr Wiggins's letter of today's date

at the same time. This sequence of events includes 2iv

all that is wrong with the Civil Service spreadsheet. I cannot Whittaker if we are to achieve anything. Not

1. Your letter of 20 March to Mr Wiggins said that the Prime Minister "would like to be informed of the main elements in the programme of reform preferably before officials appear before the PAC" She also hoped that a firm of professional accountants might be used.

2. Central department officials appear before the PAC on Monday 6 April.

Atmosphere

3. There is a certain irony about the references in Mr Wiggins's letter to urgency and the issue by the Treasury of "specific instructions":

a. Both the Prime Minister and Sir Derek Rayner queried the tentativeness of the language to be used in the letter from Sir Ian Bancroft and Sir Douglas Wass of 20 March.

b. Sir Derek Rayner queried the timetable (see especially the reference to 30 June 1982 in para. 9(iii)).

c. In replying to Sir DR's last letter on the subject, Sir Douglas Wass particularly observed that he and Sir Ian Bancroft felt that they should not go so far as to "instruct" their colleagues in respect of audit committees (para. 9(i)) and the interpretation of "really able staff" for internal audit units (para. 11).

4. Although the letter as issued was stiffer than the draft on which Sir DR commented, a strong whiff of "might be" lingers about it and about the meeting of Permanent Secretaries, to which Mr Wiggins referred. The brief discussion took place at the end of a meeting at which, on other items, much resentment at "pinpricks" from the centre was expressed. At least some of this appears to have been due to the disgust of right-minded departments (so far as internal audit goes) at the centre's latter day repentance and evangelism.

The intended programme

5. The Treasury will lead, CSD will help. The centre's job is specifying suitable standards and co-ordinating in respect of recruitment, pay and training.

6. Departments are asked to agree with the Treasury

- the objectives of their IA by 30 September, plus the job description of the head of IA plus proposals for filling it;



- the composition of their IA units by 30 June 1982, if only provisionally;
- by 31 December 1981 a course of action to bring computer audit up to scratch in three years.

7. You may like to note that:

- a. The requirement to agree certain things with the Treasury is new. It is an important development, welcome to this office.
- b. There is a touch of the chicken and the egg about the present situation: Permanent Secretaries complained at the meeting that the letter of 20 March was not clear enough about the precise functions and objectives of internal audit.
- c. The timetable is a bit leisurely. This is partly because the centre's policy-makers are having to learn their lessons step by step in order to stay ahead.
- d. There are genuine difficulties: computer audit is a new science, outside as well as inside the Service, and good accountants have not been easy to recruit.
- e. But at least we are facing the right direction.
- f. The outsider would find it very odd that the Head of the Government Accountancy Service is not leading the programme.

*Prime Minister's
The trouble is that the
Head of the Accountancy
Service is not very good
Adv. Advice*

*Then we
must find one
who is good.*

8. The content of the programme is acceptable. The timetable has now been promulgated, which is a pity. But I think that it should now be left alone.

9. The crucial point is whether the programme is driven forward with determination and success. My impression is that the responsible Deputy Secretary in the Treasury, Mr Littler, is addressing the task with vigour. He met with the PFOs on Tuesday; I gather that they were responsive. But he has of course many other duties. Both Sir DR and the Head of the Government Accountancy Service had made the case for a designated project leader.

10. Your letter of 20 March was a powerful expression of the Prime Minister's views. I suggest that the Treasury should now be encouraged to provide firm and appropriate leadership and to report back on progress.

CONFIDENTIAL



11. I attach a possible private secretary letter.

DM

P C PRIESTLEY
2 April 1981

Enc: Draft letter

DRAFT OF 2 APRIL 1981

A J Wiggins Esq
HM Treasury

The Prime Minister has seen your letter of 2 April, together with that sent to Permanent Secretaries by Sir Ian Bancroft and Sir Douglas Wass on 20 March.

The Prime Minister is content with the substance of the programme outlined in the letter to Permanent Secretaries, but is concerned less the intended timetable for action should be interpreted as less urgent than the case requires. She would be grateful if the Chancellor would kindly arrange for her to receive a first report during the summer on the progress made by the Treasury and by other departments.

The Prime Minister welcomes Treasury leadership. She thinks that this requires a considerable part of the time of a senior officer suitably qualified by training and experience and will be glad to know how this is to be provided. She would also like to know what professional assistance the Treasury is looking for from outside the Service, if any (my letter of 20 March refers).

Finally, the Prime Minister has asked me to say that she would like conveyed to the Accountancy, Finance and Audit Division her good wishes on their change of department and for the important work which lies before them.

I am copying this to Jim Buckley (CSD) and Sir Derek Rayner.

C A WHITMORE



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

2nd April 1981

Clive Whitmore Esq.,
10 Downing Street
LONDON
SW1

Handwritten initials

Dear Clive,

You wrote on 20 March expressing the Prime Minister's interest and concern on the question of internal audit.
..... You may like to show the Prime Minister the attached copy of the letter which Sir Ian Bancroft and Sir Douglas Wass have sent to Permanent Secretary Heads of Major Departments.

The letter makes clear the importance of the subject and the determination of the Treasury and the CSD to pursue urgently improvements in departments and at the centre. Specific instructions to this end are given. This is, however, only a beginning. Particularly in the matter of qualified staff, but also in the definition of some particular requirements and methods, a programme of training, recruitment and developing advice and instructions is needed. Needs of different departments will vary, as do existing standards of performance. When, imminently, the Accountancy, Finance, Audit Division is transferred to the Treasury, the Treasury will be arranging regular reviews of progress with departments generally, and will be reporting to the Chancellor from time to time. At a recent meeting of Permanent Secretaries after they had received the attached letter, it was briefly discussed, and while many expressed concern over the problems of mobilising effective staff quickly, there was widespread recognition of the importance of the problem and the need for urgent action on the lines proposed.

I am copying this letter to Jim Buckley and to Sir Derek Rayner.

Yours ever

John Wiggins

A.J. WIGGINS
Private Secretary

TREASURY
Parliament Street
LONDON
SW1

CIVIL SERVICE DEPARTMENT
Whitehall
LONDON
SW1

20 March 1981

Dear Brian,

INTERNAL AUDIT

We are writing jointly to you, after consultation with the Head of the Government Accountancy Service, about the general problem of the quality of internal audit service-wide, in the light of three recent indications of the need for fresh attention and action in this field.

2. Of particular importance is the Memorandum submitted by the C & AG to the Public Accounts Committee, analysing a recent survey by the Exchequer and Audit Department of internal audit in departments. It is subject to Parliamentary privilege until the PAC publishes it, but we enclose a copy, with Douglas Henley's agreement, on a confidential basis. The Memorandum is highly critical. Its message is that the general standard of internal audit units is too low and is particularly inadequate in relation to the audit of computer-based systems. These faults are attributed to insufficient involvement at senior levels in departments, a lack of professional skills and management within the audit units, personnel policies which result in staff being engaged in internal audit for too short a period, and inadequate direction from the centre.

3. The two other pieces of evidence are the results of surveys commissioned by the CSD last year on aspects of computer audit. Copies of these are also enclosed. They also report serious deficiencies.

4. These criticisms do not apply with equal force to all departments. We have already seen some comments from those who feel that they are not wholly fair. There will be opportunity later, when the report is published, to deal with its contents in more detail. But we believe that the need is demonstrated to bring the performance of internal audit up to an acceptable standard.

5. This is not just a matter of defence against criticism. Effective internal audit is an essential service for departmental management. The investigations of the Exchequer and Audit Department are no substitute for an efficient internal audit. They fulfil a different purpose; the C & AG reports to Parliament, whereas internal audit serves departmental management.

6. The range and purpose of internal audit are set out in paragraphs C 21-24 of Government Accounting. This makes clear the

Sir Brian Hayes KCB
Ministry of Agriculture, Fisheries and Food
Whitehall Place

importance of an effective system to the department, particularly to the Permanent Secretary and his senior management. It is the business of internal audit to report not only on propriety, security, completeness and accuracy of departmental activities and transactions, but also on the reliability and efficacy of financial control systems. In short, internal audit is a potent weapon to help us control our businesses, look after our assets, and secure value for money. The Head of Internal Audit should have direct access to the Principal Finance Officer, and where necessary to the Head of the Department; and get real and visible backing from them.

7. The Treasury, with the help of the CSD, has an important part to play in bringing about improvements in internal audit. The imminent transfer from the CSD to the Treasury of the Accountancy Finance Audit Division will bring together, under Treasury leadership the responsibility for setting standards and procedures in Government financial control, including internal audit, and the professional capability of developing and monitoring the standards and procedures, and helping departments to make cost effective use of their own internal audit resources. Work has already begun on producing fuller audit standards and guidelines, an audit manual, and a wide range of specimen documentation. A new computer audit manual will be produced.

8. Help from the centre must extend beyond issuing written guidance. The Treasury and the CSD are reviewing the range of assistance they can provide, including help on recruitment and training.

9. Much must depend on action by individual departments themselves. Specifically we ask you, and the Permanent Secretaries of all major departments:-

- (i) To take a personal interest in reviewing and improving your internal audit arrangements and in ensuring that their importance is understood by, and recognised in relations with, Principal Finance Officers and Line Managers. You may wish to consider establishing an Audit Committee, chaired at senior level. Some departments have found this useful.
- (ii) To ensure that your Head of Internal Audit is suitably experienced, of appropriate grade, and preferably professionally qualified. We ask you to review the statement of objectives of internal audit in your department, and the job description of the Head of Internal Audit, and to submit them to the Treasury for approval by 30 September 1981. Where the description or grading of the job is to be altered you should also let us have your proposal for ensuring that the post is appropriately filled at the earliest possible date. All new appointments to the post should be cleared with the Treasury, and this will become the standard practice in future.

(ii) To agree with the Treasury on a provisional basis, at latest by 30 June 1982, the composition of your internal audit section. The development of these sections will have to be progressive, and it is unlikely to be completed until an appropriately qualified Head of Audit has been in post for some months and has brought his judgement to bear.

(iv) Where the department has substantial computer operations, to agree with the Treasury by the end of this year a course of action to bring audit to an acceptable standard within three years.

You may want to consult the Treasury and the CSD on these actions, well ahead of the dates given, and we would welcome your doing so. On items (ii) and (iii) the point of contact will be Geoffrey Littler in the Treasury. On more technical audit questions and on computer audit, your people should get in touch with Edwin Walker, in AFA Division, Treasury. Where new posts above delegated levels or other matters affecting the CSD are involved, that department should be consulted in the normal way.

10. We recognise that the necessary improvement in the standards of internal audit in all departments will be a very large exercise. However the C & AG concludes that the need is not necessarily for larger numbers overall, but for a greater proportion of more professional, highly graded staff. We cannot do everything at once, but it is important to set and keep up momentum.

11. There will be much to be done in developing and placing adequately qualified people to work in internal audit. We think you should ask yourself whether your personnel management arrangements will ensure that adequately qualified people are available to be posted to internal audit, receive any further training that is necessary, and are retained in the internal audit section for sufficient periods (normally not less than four years) to meet the needs of the work. The current proposals for a functional specialism are relevant, as they provide some central involvement in the management of staff trained and experienced in accounting-type work, and our hope is that it will provide a substantial impetus to the input of professional accountancy skills. We believe that the importance of internal audit justifies allocating to it a due share of really able staff, both accountants and others. Periods of duty in internal audit should swell the cadre of people from whom senior financial staff can in the future be drawn.

12. The key posts are those of the Head of Internal Audit and the senior staff who help him to plan and supervise the work. It must be our aim to produce and train officers who can occupy these posts with full competence within the Civil Service. This however will take time. In a number of cases it may be necessary initially to use outside consultants, particularly on computer audit, though we have to recognise that there is a nationwide shortage of people with the combination of computer and audit skills. When we know the size of the demand (see paragraph 9(ii))

o. We shall consider with you what needs to be done in
rd. to inform the unions, find appropriate candidates and
settle terms and conditions.

13. Training will be a particularly important part of our efforts, and we will welcome assessments from departments of their training needs, as soon as these can be made, so that we can provide the most effective assistance. The Treasury and the CSD, in consultation with departments, will specify minimum training standards. From this specification, and the forecast of needs which departments provide, we shall be able to build up a picture of the resources needed for development and training; and as departments develop their plans further, they should keep in close touch with the College and the centre so that training resources can be developed to meet departments' needs. The Civil Service College is already planning improvements in training, including seminars for senior audit managers and on the audit of more advanced computer systems and departments will be kept informed of all further developments in the training plans of the CSD and Treasury.

14. This letter is being copied to the Permanent Secretaries of major departments on the attached list. We felt that it was right to start with these departments, but a similar letter will be issued shortly to other, smaller, departments, in a slightly different form to recognise their particular problem.

Yours ever

Douglas Wass

DOUGLAS WASS

Ian Bancroft

IAN BANCROFT

Sir Brian Hayes KCB
Ministry of Agriculture Fisheries & Food
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Sir Donald Maitland GCMG OBE
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Sir John Garlick KCB
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Sir Patrick Nairne KCB MC
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T.P. Hughes, Esq., CB,
Welsh Office,



✓
MAD

88r

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

ACCOUNTING OFFICERS MEMORANDUM

With your approval, the Treasury have just issued to all Accounting Officers, and sent to the Public Accounts Committee, a revised version of the memorandum which sets out the responsibilities of an Accounting Officer.

You asked that copies should also be circulated to Ministers. The purpose of this minute, which I am copying to all Cabinet colleagues and to Sir Robert Armstrong, is to do that.

... A copy of the new text of the memorandum is attached.

By way of explanation to our colleagues, I record that this is the memorandum sent by the Treasury to those appointed as Accounting Officers for Appropriation and certain other Accounts. The version hitherto in use had been redrafted from time to time, but dated mainly from the early 1950s. The new version has been extensively rewritten. It is designed to be more precise and more accurate than the old on many points, and to deal more specifically with various special cases, such as the additional Accounting Officers appointed in certain major departments, and with certain non-departmental bodies. It sets the responsibilities of an Accounting Officer more specifically within the general framework of Ministerial responsibility and accountability, and avoids confusing implications of dual and possibly conflicting responsibility



to Parliament as well as to the Minister. An Accounting Officer does have responsibilities towards Parliament, but they are different from, and consistent with, his responsibilities towards his Minister. The supremacy of Ministerial authority is now stated unequivocally. This does not change the function of the Accounting Officer in relation to the Public Accounts Committee.

The new version omits the previously traditional reference to an Accounting Officer being personally liable to refund expenditure deemed by the PAC as improper. This had become an anachronism. The legal advice is that there is no basis for it in law or in House of Commons procedure. And in modern conditions the sums of money which in practice engage the attention of the PAC are too large to make it realistic.

In transmitting the new memorandum to Accounting Officers the Treasury have reminded them, as you asked, that they are expected to observe the spirit as well as the letter of the memorandum, and that the change in no way diminishes the personal significance of the responsibilities carried by an Accounting Officer for the proper stewardship of the public money and resources placed in his charge.

A handwritten signature in dark ink, appearing to be 'G.H.' with a flourish.

(G.H.)

31 March 1981

THE RESPONSIBILITIES OF AN ACCOUNTING OFFICER

A Permanent Secretary (or permanent head of a minor department who may be of lower rank) is appointed by his departmental Minister with the approval of the Prime Minister. Among his other responsibilities, he is responsible to his Minister for the propriety and regularity of his department's expenditure, and for prudent and economical administration. All his functions are governed by the two fundamental principles, that it is the Minister in charge of a department who is responsible to Parliament for all aspects of its policies, organisation and management, and that officials derive their authority from the Minister in charge of their department and are accountable to him for their actions.*

2. In most cases the Permanent Secretary is the Accounting Officer for Votes and accounts administered by his department. In certain departments Accounting Officer responsibility for certain Votes or other accounts is sometimes assigned to very senior officials other than the head of the department, usually of the rank of Second Permanent Secretary. The position of these other departmental Accounting Officers, in so far as it differs from that of permanent heads, is described in paragraphs 19-20 below. The duties of Accounting Officers for non-departmental bodies are described in paragraphs 21-25.

3. Appointment as Accounting Officer is made by the Treasury in compliance with Section 22 of the Exchequer and Audit Departments Act 1866. It lays on the appointee the personal duty of signing the accounts specified in his letter of appointment and, by virtue of that duty, the further duty of being the principal witness on behalf of the department before the Committee of Public Accounts (PAC), to deal with questions arising from those accounts. From these duties flow certain responsibilities which are in any event part of the responsibilities of a Permanent Secretary, but which are traditionally associated with, and emphasised by, his role as Accounting Officer. It is these responsibilities which are the subject of this memorandum.

* This paragraph describes the common case of a Government department with a departmental Minister and a permanent head. In some cases the machinery of appointment is different, and specific powers may be vested in, for example, the Commissioners of Inland Revenue, and Customs and Excise, or in certain named office-holders, so that to this extent they may have authority not derived from Ministers. Nevertheless Ministers remain answerable for them to Parliament. The principles set out in the rest of this paper are therefore relevant to the Accounting Officers for these departments too.

4. The standard practice of appointing the permanent head of a department as the Accounting Officer for that department's Votes and accounts reflects the view that finance is an inseparable element in most policy questions, and financial responsibility an inseparable part of efficient organisation and management. The permanent head is the only official in a position to discharge responsibility as a whole for the money entrusted to the department, for its resources of manpower, and for the control of assets in its keeping such as land, buildings or other property.

5. The responsibilities of an Accounting Officer can be summarised as follows:

- (a) He must sign the Appropriation and other Accounts assigned to him. Although the underlying accounting work will have to be carried out by members of the department on his behalf, the Accounting Officer's signature implies personal responsibility for the correctness of the account and, in the case of a trading account, that in his opinion it is properly drawn up so as to exhibit a true and fair view of the transactions and state of affairs of the services to which it relates. In the case of other accounts, known as "White Paper" accounts, prescribed by specified legislation, for example in regard to advances to nationalised industries, the legislative context generally determines the nature and extent of the Accounting Officer's responsibilities.
- (b) He must ensure that correct financial procedures are followed, including specifically those mentioned in paragraphs 7 and 8 below; and more broadly that the accounts for which he is responsible are maintained in a form suited to the requirements of management as well as in the form prescribed for Vote accounting purposes.
- (c) He must ensure that the public funds for which he is responsible as Accounting Officer are properly safeguarded, with independent and effective checks, made without reference to personal considerations, of cash balances in the hands of any official. Similar care, including checks as appropriate, must be taken of stores or any public property.

- (d) He must ensure that, in the consideration of policy proposals relating to the expenditure or income for which he is Accounting Officer, all relevant financial considerations are taken into account, and where necessary brought to the attention of Ministers with appropriate emphasis and in an appropriate form. These considerations include the need for economy and the avoidance of extravagance or waste.
- (e) Similarly he must ensure that in the implementation of expenditure programmes as authorised by Ministers proper regard is given to economy and the avoidance of waste.

6. Proper management of expenditure includes the preparation of the material on which decisions are taken; the efficiency with which administrative operations are carried out; the cost-consciousness of staff at all levels; the provision of special skills and services (scientific, statistical, accountancy, O & M etc) for handling particular problems, and the selection and training of staff. Good management requires effective delegation. A person appointed to be an Accounting Officer cannot perform himself, or even closely supervise, all the various procedures needed to carry out his responsibilities. He must make sure that his department is organised and staffed on sound lines, particularly in the finance and establishment branches so as to provide for proper delegation of duties. He should pay particular attention to the adequacy and effectiveness of arrangements for internal audit. The officer in charge of this function should normally be responsible to the Principal Finance Officer, with direct access to the Accounting Officer where necessary.

Regularity and Propriety of Expenditure

7. An Accounting Officer has a particular responsibility for ensuring compliance with Parliamentary requirements in the control and management of expenditure. A fundamental requirement is that the funds for which he is responsible should be applied only to the extent and for the purposes authorised by Parliament. In the case of voted expenditure he must ensure that any payments made are within the ambit and amount of the Vote, and that Parliamentary approval has been sought and given. In cases not covered by the original estimate, eg in connection with a service not contemplated when the original estimate was presented, or where a temporary advance from the Contingencies Fund has been sanctioned by the Treasury, he must

ensure that Parliamentary approval is sought and given at the earliest opportunity by way of a Supplementary Estimate, or if necessary Excess Vote. In cases involving losses or special payments, he must ensure that Parliament's attention is drawn to the matter by suitable notation of the Appropriation Account.

8. The Accounting Officer is responsible for ensuring that specific Treasury or Civil Service Department sanction for the expenditure has been obtained in all cases where it is required. It is required for any expenditure not covered by any standing authorities delegated by the Treasury or the Civil Service Department to the Department. It is required before expenditure is incurred on any subhead of a Vote in excess of the amount specified for that subhead in the Estimates, even though savings may be available elsewhere and the expenditure itself falls within the delegated authority of the department. Expenditure may never be incurred in excess of the total net sum authorised by Parliament to be spent on any one Vote, save where a temporary advance from the Contingencies Fund has been sanctioned by the Treasury, in which case as mentioned in paragraph 7 Parliamentary approval for its repayment must be sought at the earliest opportunity. The Accounting Officer is also responsible for ensuring that adequate machinery exists for the collection and bringing to account in due form of all receipts of any kind connected with the Votes and accounts for which he is responsible.

Relations with the Minister

9. The Accounting Officer has particular responsibility to see that appropriate advice is tendered to Ministers on all matters of financial propriety and regularity and more broadly as to all considerations of prudent and economical administration. He will need to determine how and in what terms such advice should be tendered, and whether in a particular case to make specific reference to his own duty as Accounting Officer to justify to the PAC his department's expenditure.

10. If the Minister in charge of the department is contemplating a course of action involving a payment which the Accounting Officer considers would infringe the requirements of propriety or regularity, the Accounting Officer should set out in writing his objection to the proposed expenditure and the reasons for his objection. If the Minister decides nonetheless to proceed, the Accounting Officer should seek a written instruction to make the payment. Having received such an instruction, the Accounting Officer must comply with it, but should then inform the Treasury (who will in turn inform the Civil Service Department where appropriate) of what has occurred, and should also communicate the papers to the Comptroller and Auditor General. Provided that this procedure has been followed, the PAC can be expected to recognise that the Accounting Officer bears no personal responsibility for the expenditure.

11. If a course of action is in contemplation which raises an issue not of formal propriety or regularity but more widely of prudent and economical administration, it is the duty of the Accounting Officer to draw the relevant factors to the attention of his Minister and to advise him in whatever way he deems appropriate. He may think it right to refer to the possibility of criticism by the PAC. If his advice is overruled, he should ensure that both his advice and the overruling of it are apparent clearly from the papers.

Appearance before the PAC

12. An Accounting Officer appears before the PAC to answer their questions concerning the expenditure from the Votes and other accounts for which he is Accounting Officer and related activities. He may be supported by other officials, who may, and commonly do, join in giving the evidence.

13. The Financial Secretary to the Treasury is formally a member of the Committee but rarely attends. Treasury officials regularly attend Committee hearings and are usually asked to comment on the evidence. They then speak as representatives of the Executive and subject to collective Ministerial authority, but are expected to comment from the standpoint of the department which has the formal responsibility for presenting Estimates to Parliament and for prescribing the form of accounts. This goes with the Treasury's central responsibility for the operation of public expenditure control. Parliament has traditionally regarded the Treasury as an ally in controlling expenditure.

14. The Accounting Officer will be expected to furnish the PAC with explanations of any indications of irregularity, waste or extravagance or inefficient administration, or weakness in financial procedure, to which their attention has been drawn by the Comptroller and Auditor General or about which they may wish to question the Accounting Officer.

15. In practice, the Accounting Officer will have delegated authority widely, but he cannot on that account disclaim his responsibility. Nor, by convention, does the incumbent Accounting Officer decline to answer questions where the events took place before he assumed his appointment; the Committee may be expected not to press his personal responsibility in such circumstances.

16. The Committee have emphasised the importance they attach to accuracy of evidence, and the responsibility of witnesses to ensure this. The Accounting Officer should ensure that he is adequately and accurately briefed on matters on which he gives evidence. He may ask the Committee for leave to supply information not within his immediate knowledge by means of a later note. Should it be discovered subsequently that the evidence provided to the Committee has contained errors, these should be made known to the Committee at the earliest possible moment.

17. In general, the rules and conventions governing appearances of officials before Parliamentary Committees apply to the PAC, including the general convention that civil servants do not disclose the advice given to Ministers. Nevertheless, in a case where the procedure described in paragraph 10 was used concerning a matter of propriety or regularity of expenditure, the Accounting Officer's advice and its overruling by the Minister, would be disclosed

to the PAC. In a case where advice of an Accounting Officer has been overruled in a matter not of propriety or regularity but of prudent and economical administration it will be appropriate for an Accounting Officer, questioned about the matter at the PAC, to lay stress on the fact that it was a decision by his Minister. He should seek to avoid disclosing advice given to his Minister, but should be ready to explain the reasons for the Minister's decision and may be called on to satisfy the Committee that all relevant financial considerations were brought to the Minister's attention before the decision was taken. It will then be for the PAC to pursue the matter further with the Minister if they so wish.

Absence of Accounting Officer

18. The PAC may be expected to postpone a hearing if the relevant Accounting Officer is temporarily indisposed. Where the Accounting Officer is unable by reason of incapacity or absence to sign the Appropriation Account in time to render it to the Comptroller and Auditor General, the department may render unsigned copies pending his return. If the Accounting Officer is unable to sign the Account in time for printing the department should ask the Treasury to appoint an interim Accounting Officer.

Additional Accounting Officers

19. Where one or more senior officials, other than the permanent head of the department, are appointed as Accounting Officers for certain Votes or accounts, there should be a clear understanding of their relationship not only with their Minister but also with the permanent head. The permanent head remains in general charge of the department, and in particular, of its organisation, management and staffing and department-wide procedures in financial and other matters. He must ensure that these promote the efficient and economical conduct of all its affairs, and safeguard financial propriety and regularity throughout the department. It is within that framework that any additional Accounting Officers are responsible for the Votes and accounts assigned to them. In matters affecting their responsibilities as Accounting Officer, their judgement

should only be overridden by or with the specific agreement of their Minister. In such cases the Minister may also seek the views of the permanent head.

20. The position of an additional Accounting Officer when he appears before the PAC is thus different from that of a permanent head who carries full responsibility under his Minister for the organisation and management of his department as a whole. An additional Accounting Officer is however able, on the basis of his discharge of his own responsibilities, to answer most questions which may be raised by the PAC concerning expenditure and activities in his field. If PAC questioning is directed to matters determined by the permanent head and the additional Accounting Officer finds himself in difficulty in responding, the Committee could be expected to accede to a suggestion that they seek evidence from the permanent head as well as from the Accounting Officer for the expenditure under discussion.

Accounting Officer Appointments in Non-Departmental Bodies

21. The Treasury also appoints Accounting Officers for some non departmental public bodies (eg the Manpower Services Commission, most museums and galleries, the Scottish and Welsh Development Agencies and the Research Councils). Appointments of this kind are made by analogy with appointments of Accounting Officers in departments. The normal practice is to appoint the senior full-time officer of the body. Those so appointed have broadly the same duties as Departmental Accounting Officers as described above and exercise them on behalf of the office holder or holders in charge of the body. With the exception of bodies (such as museums and galleries) with their own Vote, the responsibilities of these Accounting Officers are confined to the grant in aid account of the body which is financed from the Vote of its sponsoring department.

22. Whether or not a grant-aided body has its own Accounting Officer, the responsibility of the Accounting Officer in the sponsor department is to ensure that the conditions attached to the grant-in-aid conform with the terms of the Vote; to monitor compliance with these conditions by the body; and to satisfy himself that the financial and other controls applied by the department are appropriate and sufficient to safeguard public funds. Among other things he will need to satisfy himself about the quality of its management. The Accounting Officer of the body in receipt of the grant-in-aid has a special responsibility to see that the rules and conditions laid down by the Department issuing the grant-in-aid are observed.

23. An Accounting Officer in a grant-aided body will normally appear before the PAC alongside the Departmental Accounting Officer responsible for the payment of the grant-in-aid.

24. The absence of an Accounting Officer appointment in a non-departmental body does not lessen the nature and scope of its accountability to Ministers and through them to Parliament, or the right of the PAC to take evidence direct from the body if it wishes. The approved signatory of the accounts, normally the Chairman or Chief Executive, will, as in the case of a Departmental Accounting Officer, automatically assume a primary responsibility to answer for that body in any examination by the PAC and may be summoned to appear before the Committee for that purpose.

Mr PATTISON

B/F Party

Something is in its way from Tsg

MAR 1/4

INTERNAL AUDIT

1. I refer to Mr Whitmore's letter of 20 March to Mr Wiggins saying inter alia that the Prime Minister would like to be informed of the main elements in the programme of reform referred to by the Chancellor in his minute of 11 March, preferably before officials appeared before the PAC in April.
2. I understand that central department officials give evidence on Monday 6 April. I think it important that the PM should have an opportunity to comment and I suggest that if nothing has been heard by Thursday morning 2 April the Treasury should be prodded firmly.
3. You might like to have for your file a copy of the Bancroft/Wass letter of 20 March as issued to Permanent Secretaries and of the record of discussion by a few of them under Sir Douglas Wass's chairmanship on 24 March in SY.

CP

C PRIESTLEY
31 March 1981

Encs: As indicated



H M Treasury
Parliament Street London SW1P 3AG

Switchboard 01-233 3000
Direct Dialling 01-233 3620

Sir Douglas Wass GCB
Permanent Secretary

Sir Derek Rayner
Cabinet Office
Whitehall
LONDON
SW1

20 March 1981

Mr. Patten

*Please add to pp.
and return to me.*

S

25.iii.81

Mr Priestley

See Flag on file.

ME

25/iii/81

Dear Derek,

INTERNAL AUDIT

Thank you for your letter of 17 March.

I enclose a copy of the letter to Permanent Secretaries which Ian Bancroft and I have just sent out. It was amended to reflect a number of the comments which you, Ken Sharp and Clive Priestley made on the previous draft. In particular, referring to your own letter, it makes clear in paragraph 9 and elsewhere that the Treasury is in the lead, although there are matters on which the CSD will in the normal course be consulted.

Good

We have not made amendments to reflect the comments in paragraph 6 of your letter to me, since we shall have to work up the more precise documents we agree will be needed in consultation with the departments concerned. Geoffrey Littler proposes to hold an early meeting of Principal Finance Officers, and to develop with them and with the AFA Division a programme of work and priorities and arrangements for keeping track of progress.

Good

On the remaining points you make, we did not feel that we should go so far as to give instructions to our Permanent Secretary colleagues to set up Committees and select fast-stream principals. Those will not in all cases be the sensible answers, and I think we must leave some freedom to Permanent Secretaries to choose their own best methods of management.

*See PR
suggested
"addressing"
from. sub.
to set up
Audit
Committees
and say
that the centre "would expect"
dept. to place of fast stream principals
in newly developing internal audit areas.*

I am copying this letter to Ian Bancroft and Ken Sharp.

Yours etc.

Douglas Wass
DOUGLAS WASS

HM TREASURY
Parliament Street
LONDON
SW1

CIVIL SERVICE DEPARTMENT
Whitehall
LONDON
SW1

20 March 1981

Dear Brian,

INTERNAL AUDIT

We are writing jointly to you, after consultation with the Head of the Government Accountancy Service, about the general problem of the quality of internal audit service-wide, in the light of three recent indications of the need for fresh attention and action in this field.

2. Of particular importance is the Memorandum submitted by the C & AG to the Public Accounts Committee, analysing a recent survey by the Exchequer and Audit Department of internal audit in departments. It is subject to Parliamentary privilege until the PAC publishes it, but we enclose a copy, with Douglas Henley's agreement, on a confidential basis. The Memorandum is highly critical. Its message is that the general standard of internal audit units is too low and is particularly inadequate in relation to the audit of computer-based systems. These faults are attributed to insufficient involvement at senior levels in departments, a lack of professional skills and management within the audit units, personnel policies which result in staff being engaged in internal audit for too short a period, and inadequate direction from the centre.

3. The two other pieces of evidence are the results of surveys commissioned by the CSD last year on aspects of computer audit. Copies of these are also enclosed. They also report serious deficiencies.

4. These criticisms do not apply with equal force to all departments. We have already seen some comments from those who feel that they are not wholly fair. There will be opportunity later, when the report is published, to deal with its contents in more detail. But we believe that the need is demonstrated to bring the performance of internal audit up to an acceptable standard.

5. This is not just a matter of defence against criticism. Effective internal audit is an essential service for departmental management. The investigations of the Exchequer and Audit Department are no substitute for an efficient internal audit. They fulfil a different purpose; the C & AG reports to Parliament, whereas internal audit serves departmental management.

6. The range and purpose of internal audit are set out in paragraphs C 21-24 of Government Accounting. This makes clear the

Sir Brian Hayes KCB
Ministry of Agriculture, Fisheries and Food
Whitehall Place
SW1

importance of an effective system to the department, particularly to the Permanent Secretary and his senior management. It is the business of internal audit to report not only on propriety, security, completeness and accuracy of departmental activities and transactions, but also on the reliability and efficacy of financial control systems. In short, internal audit is a potent weapon to help us control our businesses, look after our assets, and secure value for money. The Head of Internal Audit should have direct access to the Principal Finance Officer, and where necessary to the Head of the Department; and get real and visible backing from them.

7. The Treasury, with the help of the CSD, has an important part to play in bringing about improvements in internal audit. The imminent transfer from the CSD to the Treasury of the Accountancy Finance Audit Division will bring together under Treasury leadership the responsibility for setting standards and procedures in Government financial control, including internal audit, and the professional capability of developing and monitoring the standards and procedures, and helping departments to make cost effective use of their own internal audit resources. Work has already begun on producing fuller audit standards and guidelines, an audit manual, and a wide range of specimen documentation. A new computer audit manual will be produced.

8. Help from the centre must extend beyond issuing written guidance. The Treasury and the CSD are reviewing the range of assistance they can provide, including help on recruitment and training.

9. Much must depend on action by individual departments themselves. Specifically we ask you, and the Permanent Secretaries of all major departments:-

- (i) To take a personal interest in reviewing and improving your internal audit arrangements and in ensuring that their importance is understood by, and recognised in relations with, Principal Finance Officers and Line Managers. You may wish to consider establishing an Audit Committee, chaired at senior level. Some departments have found this useful.
- (ii) To ensure that your Head of Internal Audit is suitably experienced, of appropriate grade, and preferably professionally qualified. We ask you to review the statement of objectives of internal audit in your department, and the job description of the Head of Internal Audit, and to submit them to the Treasury for approval by 30 September 1981. Where the description or grading of the job is to be altered you should also let us have your proposal for ensuring that the post is appropriately filled at the earliest possible date. All new appointments to the post should be cleared with the Treasury, and this will become the standard practice in future.

[Only]

- only*
- (iii) To agree with the Treasury on a provisional basis, at latest by 30 June 1982, the composition of your internal audit section. The development of these sections will have to be progressive, and it is unlikely to be completed until an appropriately qualified Head of Audit has been in post for some months and has brought his judgement to bear.
- (iv) Where the department has substantial computer operations, to agree with the Treasury by the end of this year a course of action to bring audit to an acceptable standard within three years.

You may want to consult the Treasury and the CSD on these actions, well ahead of the dates given, and we would welcome your doing so. On items (ii) and (iii) the point of contact will be Geoffrey Littler in the Treasury. On more technical audit questions and on computer audit, your people should get in touch with Edwin Walker, in AFA Division, Treasury. Where new posts above delegated levels or other matters affecting the CSD are involved, that department should be consulted in the normal way.

*ended at
part A.*

10. We recognise that the necessary improvement in the standards of internal audit in all departments will be a very large exercise. However the C & AG concludes that the need is not necessarily for larger numbers overall, but for a greater proportion of more professional, highly graded staff. We cannot do everything at once, but it is important to set and keep up momentum.

11. There will be much to be done in developing and placing adequately qualified people to work in internal audit. We think you should ask yourself whether your personnel management arrangements will ensure that adequately qualified people are available to be posted to internal audit, receive any further training that is necessary, and are retained in the internal audit section for sufficient periods (normally not less than four years) to meet the needs of the work. The current proposals for a functional specialism are relevant, as they provide some central involvement in the management of staff trained and experienced in accounting-type work, and our hope is that it will provide a substantial impetus to the input of professional accountancy skills. We believe that the importance of internal audit justifies allocating to it a due share of really able staff, both accountants and others. Periods of duty in internal audit should swell the cadre of people from whom senior financial staff can in the future be drawn.

ew

12. The key posts are those of the Head of Internal Audit and the senior staff who help him to plan and supervise the work. It must be our aim to produce and train officers who can occupy these posts with full competence within the Civil Service. This however will take time. In a number of cases it may be necessary initially to use outside consultants, particularly on computer audit, though we have to recognise that there is a nationwide shortage of people with the combination of computer and audit skills. When we know the size of the demand (see paragraph 9(ii))

above), we shall consider with you what needs to be done in order to inform the unions, find appropriate candidates and settle terms and conditions.

13. Training will be a particularly important part of our efforts, and we will welcome assessments from departments of their training needs, as soon as these can be made, so that we can provide the most effective assistance. The Treasury and the CSD, in consultation with departments, will specify minimum training standards. From this specification, and the forecast of needs which departments provide, we shall be able to build up a picture of the resources needed for development and training; and as departments develop their plans further, they should keep in close touch with the College and the centre so that training resources can be developed to meet departments' needs. The Civil Service College is already planning improvements in training, including seminars for senior audit managers and on the audit of more advanced computer systems and departments will be kept informed of all further developments in the training plans of the CSD and Treasury.

14. This letter is being copied to the Permanent Secretaries of major departments on the attached list. We felt that it was right to start with these departments, but a similar letter will be issued shortly to other, smaller, departments, in a slightly different form to recognise their particular problem.

Your own

Douglas Wass

DOUGLAS WASS

Ian Bancroft

IAN BANCROFT

3. INTERNAL AUDIT

The Committee had before them a letter of 20 March 1981 from the Permanent Secretaries of the Civil Service Department (CSD) and of the Treasury to the Permanent Secretary, Ministry of Agriculture, Fisheries and Food, and copies of a forthcoming memorandum by the Comptroller and Auditor General (C and AG) on Internal Audit in Central Government and of reports prepared by the CSD on Computer Audit Review and on Computer Audit Training in Government Departments.

SIR IAN BANCROFT said that the C and AG's report would be published shortly. The criticisms in it of Departmental internal audit arrangements were a matter of grave concern, and the Public Accounts Committee could be expected to follow them up vigorously. Although the situation varied between Departments, it was clear that major changes would be required, especially in relation to computer audit, to ensure that arrangements were brought up to a sufficiently high standard for the future. The CSD's own reviews of computer audit had pointed to the lack of relevant expertise in Departments and to the urgent need for training of existing staff and for the recruitment of appropriate specialists. For the future it would be important for Departments to assign, from within their present manpower ceilings, more able and better trained staff to internal audit. While it was extremely important to remedy the defects identified by the C and AG and by the CSD it would be a mistake to think that this could be done quickly by crash solutions rather than an evolutionary approach. It was now becoming easier to recruit outside accountants, and steps were being taken to improve the training offered by the Civil Service College; but it would probably be some years before the important defects identified in the present arrangements had been rectified.

In discussion the following were the main points made -

- a. Although the report by the C and AG had identified important defects in the present arrangements, which would need to be remedied, it did not give sufficient weight to the mechanisms within Departments, other than internal audit, for ensuring that public money was properly applied.

CONFIDENTIAL

No mention was made of responsibilities of line management, and there was no discussion of whether it might be better to develop management audits as well as to improving the existing arrangements for internal audits.

b. The C and AG's report, and the letter of 20 March from Sir Ian Bancroft and Sir Douglas Wass, were insufficiently clear about the precise functions and objectives of internal audit. There was an unacceptable inference in the C and AG's report that most of the routine audit work should be undertaken by Departmental internal audit sections with the Exchequer and Audit Department responsible for the rest. While the C and AG rightly pointed to matters which needed examination and improvements, his report included many generalisations which should not be allowed to pass unchallenged.

c. To achieve the necessary improvements in the present arrangements would require a sustained and carefully-planned programme of action. A major problem was the lack of skilled auditors in the Civil Service and the fact that not all of the existing trained staff were sufficiently able to become Departmental Head of Audit. The first priority was, therefore, for each Department to assess its requirements, then to see what resources were available throughout the Civil Service, and then, perhaps, to redistribute those resources. It would also be important to recruit auditors from outside the Civil Service at an appropriately senior level. This could be difficult since the levels of pay offered to auditors in the Civil Service had in the past been a barrier to the recruitment of able people, but in the present economic climate it should be possible to recruit suitable people from outside at about Principal level. Departments might also consider drawing up for the medium term an audit development plan in consultation with Central Departments. To avoid unnecessary duplication of effort some co-ordination by Central Departments would probably be necessary, especially in the case of those smaller Departments which at present had no qualified accountants on their staff and therefore had no base on which to build for the future. In allocating existing resources, priority would need to be given to particularly sensitive areas, such as Computer audit, and steps should be taken to ensure that auditors were involved in the design of computer programmes.

CONFIDENTIAL

SIR DOUGLAS WASS, summing up the discussion, said that a great deal of effort would be required before the present internal audit arrangements were satisfactory, and it was therefore important that Departments should embark on this task as soon as possible. The detailed arrangements discussed in the letter of 20 March to Permanent Secretaries would be the subject of further consultation with Departments. The Treasury and the CSD were due to give evidence early in April to the Public Accounts Committee. This would provide a public opportunity to describe the steps proposed to remedy the defects identified by C and AG and perhaps to refer to some of the defects ~~of that~~ identified in discussion; and before giving evidence the Treasury and the CSD would discuss this further with PFOs. ||

The Committee -

Took note, with approval, of the Chairman's summing up of their discussion.

Cabinet Office

26 March 1981

CONFIDENTIAL

JMA you Mack

[Blind copy:
- Mr Pattison]



CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01- 233 8224

25 March 1981

Sir Douglas Wass GCB

Sir Douglas,

INTERNAL AUDIT

Many thanks (in Derek Rayner's absence in Canada) for your letter and enclosure of 20 March. He will see it (together with the letters sent to the Chancellor on behalf of the Prime Minister on internal audit and Accounting Officers) on his return at the end of next week.

I am copying this to Ian Bancroft and Ken Sharp.

Yours ever,
Clive Priestley
C PRIESTLEY



u40
bc Sir D Rayner

JH

for Macle

10 DOWNING STREET

From the Private Secretary

23 March 1981

The Prime Minister has seen the Chancellor's minute of 16 March, with which he enclosed a copy of the revised version of the Memorandum for Accounting Officers. She has noted that this relates to other work which the Chancellor and Sir Derek Rayner have in hand.

The Prime Minister welcomes the clarification of the relationship between Ministers and the officials who, as Accounting Officers, represent him before the Public Accounts Committee. She has no objection to dropping the traditional doctrine of "personal liability" if it is no longer applicable. She also thinks the treatment of differences of view between Ministers and officials on matters of "prudent and economical administration" is handled reasonably in paragraphs 11 and 17 of the new version.

Whilst the Prime Minister has not gone through the new Memorandum in fine detail, she is content that it should be brought into use and conveyed to the PAC. She would like it to be circulated to Ministers at a suitable opportunity. As far as senior officials acting as Accounting Officers are concerned, the Prime Minister thinks that the dropping of personal liability should be accompanied by a firm reminder that they should obey the spirit as well as the letter of the Memorandum. The impending report by the C&AG on the state of internal audit, referred to in the Chancellor's minute of 11 March, serves to underline this.

I am sending a copy of this letter to Edward Chaplin (Lord President's Office).

M. A. PATTISON

A.J. Wiggins, Esq.,
HM Treasury.

A

Mr PATTISON

ACCOUNTING OFFICERS MEMORANDUM

1. You invited comments on the Chancellor's minute of 16 March.

Context

2. The new memorandum is relevant not only to the central/spending departments relationship and Sir Derek Rayner's work on defining the responsibilities of Ministers and Permanent Secretaries (note (A), para. 5) but also to

a. the wider and more vigorous role proposed for the Comptroller and Auditor General and a "National Audit Office"; and

b. the recent papers on Internal Audit (my minute to you of 12 March).

Background

3. The role of Accounting Officer is additional to that of Permanent Head. It reflects the willingness of Parliament to see an official instead of and on behalf of his Minister in respect of audit matters.

4. In Victorian times, it was not simply convenient for Ministers, but right within the then political and social conventions, to look to an official rather than his Minister to concern himself with the nuts and bolts of regularity and propriety. The PAC in fact retain the right to summon a Minister himself, but has not done so (I believe) for 60 years. It has however got more and more interested in the second part of the Accounting Officer's task, that of prudent and economical administration. Even so, the PAC will undoubtedly give the Service a bad time on internal audit if it suspects that it is falling down on basic regularity and propriety audit.

Sir Derek Rayner's attitude

5. Sir DR had a substantial correspondence with the Treasury last year and is now satisfied with the words in which the memorandum is expressed and with the clarification it promises. He does not like the use of the word "appoint" to describe the designation by the Treasury of an official as an Accounting Officer (compare this with the correct use of "appoint" in line 2 of the revised memorandum), but this is required under the E&AD Act 1866 and the Trading Funds Act 1973.

6. The main point is whether senior officials take their management responsibilities, including those of Accounting Officer, seriously enough. His own experience as an Accounting Officer confirms that a tremendous job of briefing is required

before PAC hearings and that junior officials put a lot into the necessary task of "protecting the Accounting Officer", not least because the PAC has been far readier to punish vice than reward virtue. However, too much of this effort is defensive and the imminent adverse report on Internal Audit shows that, even in that crucially important area of "protection", Accounting Officers generally - not universally - find it easier to obey the letter rather than the spirit of their responsibility for the items mentioned in para. 6 of the revised memorandum.

Some myths dispersed

7. There have been three important bits of magic about Accounting Officers:

a. They can in theory be made to stump up themselves for mislaid or mis-spent cash. This is now dropped (note (A), para. 8).

b. Their responsibility to Parliament is extra to their responsibility to their departmental Minister and somehow transcends it. This too is dropped (note (A), para. 9 ~~which should surely read (line 3), "these are no different from" and para. 10).~~

c. They must "shop" the Minister to the PAC if he fiddles the petty cash or is adventurous in a way inimical to prudent and economical administration. There is a passing reference to this in note (A), para. 2, but you should know that

i. no change is proposed in respect of regularity or propriety, see revised memorandum para. 10. The Accounting Officer is entitled to seek a written instruction and communicate the papers to the Treasury and the C&AG; but

ii. in respect of prudent and economical administration there is a new formulation at the end of para. 11 (which may be compared with that in para. 7(i) of the old version). Under this the threat of a complaint by the Accounting Officer to the C&AG is finally dropped in favour of simply making what has happened clearly apparent from the papers.

Prime Minister's interest

8. Apart from the point mentioned in para. 7c above, I think that a possible point of detail of interest to the Prime Minister is the reference to the appointment of a Permanent Head in the first sentence of the revised memorandum. I believe the formula used there is correct, namely "is appointed by his departmental Minister with the approval of the Prime Minister",

but you may like to check on this.

9. For the rest, the Prime Minister can, I suggest, take the detail as given and confine any point of substance to the importance of deeds rather than words.

10. I attach a possible private secretary reply, whose use depends somewhat on the reply sent or to be sent to the Chancellor's minute of 11 March on internal audit.

Sp

C PRIESTLEY
20 March 1981

Enc: Draft letter to Mr Wiggins

DRAFT OF 20 MARCH 1981

J A Wiggins Esq
HM Treasury

ACCOUNTING OFFICERS MEMORANDUM

1. The Prime Minister is grateful for the Chancellor of the Exchequer's minute of 16 March and for a sight of the revised memorandum. She has noted that it relates to other work which the Chancellor and Sir Derek Rayner have in hand.
2. The Prime Minister has not of course gone through the old and new memoranda in fine detail, but has asked me to make the following points.
3. Mrs Thatcher welcomes the clarification of the relationship between a Minister and the officials who, as Accounting Officers, represent him before the Public Accounts Committee. She has no objection to dropping the traditional doctrine of "personal liability" if it is no longer applicable; she thinks that the treatment of differences of view between Ministers and officials on matters of "prudent and economical administration" is handled reasonably (paras. 11 and 17 of the new memorandum). ~~(She takes it, incidentally, that line 3 of note (A) should read "no different from".)~~
4. The Prime Minister is content for the new memorandum to be brought into use and conveyed to the Public Accounts Committee. She would like it to be circulated to Ministers at a suitable opportunity. As far as senior officials acting as Accounting Officers are concerned, the Prime Minister thinks that the dropping of personal liability should be accompanied by a firm reminder that they should obey the spirit as well as the letter of the memorandum (witness the impending report by the Comptroller and Auditor General on the state of internal audit (the Chancellor's minute of 11 March refers)).
5. I am copying this to Edward Chaplin (Lord President's Office).

[Private Secretary]



cc CSD

Paymer

J.L. 1005/1/11/11/11

H2

10 DOWNING STREET

From the Principal Private Secretary

20 March 1981

The Prime Minister was grateful for the Chancellor's minute of 11 March giving her advance warning of the Comptroller and Auditor General's report criticising the Government's arrangements for internal audit. The matter was of course discussed briefly in Cabinet last week.

The Prime Minister feels that Ministers have the right to expect their Permanent Secretaries to ensure that the arrangements for caring for taxpayers' money are beyond reproach. She was shocked to learn that the Treasury and CSD accept as valid the Comptroller and Auditor General's criticisms that internal audit lacks professionalism and top management support, with the result that systematic abuse would probably go undetected.

The Prime Minister is glad to hear that Sir Douglas Wass and Sir Ian Bancroft have an initiative in hand. She would like to be informed of the main elements in the programme of reform to which the Chancellor refers, preferably before officials appear before the PAC next month. She hopes that full consideration will be given to the use of a firm of professional accountants with the appropriate expertise in this specialised area. Plainly, the Government will be severely criticised if its programme of reform is not seen to be adequate.

The Prime Minister is also concerned lest the terms of the joint letter to Permanent Secretaries, as outlined in paragraph 5 of the Chancellor's minute, should be too tentative. She does not want any suggestion that action by Permanent Secretaries to tighten up their audit arrangements is optional.

I am sending copies of this letter to Jim Buckley (Civil Service Department) and Sir Derek Rayner.

CW

A.J. Wiggins, Esq.,
H.M. Treasury.

RESTRICTED

H2

at Mr Osguid

MLL Mr Whitmore to see

19th

cc ✓ Mr Pattison
Mr Colman (CSD)
Mr J Taylor (HM Tsy)
Mr Littler

Go A Mech

AUDIT MACHINERY

1. Mr Joel Barnett, Chairman of the PAC, had lunch with Sir Derek Rayner yesterday.
2. The points discussed included the succession to the post of C&AG (dealt with ad rem, not ad hominem) and the impending report to the PAC on internal audit.
3. On the latter, Mr Barnett said, among other things, that IA in the Civil Service was lamentably out of date; it was barely credible that the Service felt so little shame about this; he intended to get explanations from the departments concerned, including the centre; and that he intended to keep calling departments back to make sure that they were making satisfactory progress.

CP

C PRIESTLEY
18 March 1981



CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-233 8224

Mr. Barber 13/iii
Mr. Allen
Mr. Thomas
Mr. Callaghan

17 March 1981

*To see the 3 letters
of today's date and PA,
please.*

Sir Douglas Wass GCB

[Signature]
INTERNAL AUDIT

9
17.iii.81

1. I have seen Geoffrey Littler's letter of 16 March to Richard Wilding (CSD), with a draft submission to you and Ian Bancroft, suggesting that you should jointly write to your Permanent Secretary colleagues. Earlier, of course, I saw the Chancellor of the Exchequer's minute to the Prime Minister, alerting her to the possibility of adverse publicity in this area and saying that the joint initiative had my support.
2. As I am going abroad for two weeks shortly, I thought I should write to you directly with what are likely to be the last comments on this subject before you and Ian issue your letter.
3. As I have already told Geoffrey Littler, I think the new draft a vast improvement on earlier ones but it would be wrong for me to leave you under the misapprehension that I am wholly content with what is being proposed to you, despite its many real merits. I have also seen Ken Sharp's letter to Geoffrey Littler of 11 March and should let you know that I very much agree with his view that in order to give the initiative the momentum it deserves, and to keep it, something like a "task force", under a designated leader, is needed. I myself would put more emphasis on the "designated leader" than on the "task force".
4. In the draft letter which you are to consider, therefore, I should very much prefer you to name one of your officials in the Treasury as the lead person for this exercise, responsible to you for devising and implementing together with departments a plan for the reform of internal audit. At the moment, the draft speaks of two Deputy Secretaries, one in the Treasury and one in CSD, having a hand in these matters while the head of AFA will be available to give technical advice.

5. I have no doubt at all that the Treasury lead needs to be emphasised in order to give clarity and emphasis to the plan. I understand that the CSD has an involvement in such matters as recruitment, pay and training but I think that the right course is for them to advise the Treasury on such matters rather than act in tandem. Specifically, I think it is for the Treasury to approve appointments to headships and the composition of internal audit units. Otherwise I fear that the leadership given to departments is bound to be less clear than it should be and departments themselves somewhat confused about who is responsible for what.

6. On a rather different point, I think that departments would be greatly helped if your letter were more specific than it is at the moment on what the Treasury is going to do when. Paragraph 7 of the present draft speaks of work having begun on "producing fuller audit standards and guidelines, an audit manual, and wide range of specimen documentation. A new computer audit manual will be produced". Similarly, paragraph 13 speaks of the two central departments specifying "minimum training standards". My point is that there is plainly a touch of the chicken and the egg about all this. I would have thought that Permanent Secretaries would find it easier to respond to your requests if they were able to do so with guidance in their hands. It need not be fully worked up, of course but at the moment the draft does not have - to my mind, at least - the appearance of a firm plan to which departments are expected to conform. Perhaps the obvious example is in paragraph 9(ii) where you ask Permanent Secretaries to review the objectives of their internal audit units and the job description of their heads of IA without indicating when a "model" or some other paradigm is going to be available for comparison.

7. Finally, I think that many of the admirable things the draft says might be more effective if expressed more strongly. Two examples are your references to audit committees (paragraph 9(i)) and allocating to internal audit "a due share of really able staff" (paragraph 11).

8. In the former case, I would think it entirely reasonable of you and Ian to advise colleagues to establish an audit committee (saying how such bodies work) rather than saying that they might "wish to consider" this. In the latter case, I recall very well the emphasis with which you spoke over dinner on 2 December about the need to get good people into management-type jobs. Why not in this case say that you would expect departments to place such people as fast-stream Principals in such developing areas of audit as the quality of resource control and evaluation systems and computer audit?

9. I am copying this to Ian Bancroft, Ken Sharp, Geoffrey Littler and Richard Wilding.


Derek Rayner

17 March 1981

MR WHITMORE

INTERNAL AUDIT

1. The Chancellor's warning minute to the Prime Minister of 11 March about the C&AG's report was copied to David Wolfson, John Hoskyns and Bernard Ingham.
2. But the advice to the Prime Minister from Sir Derek Rayner's office of 12 March was not copied to us. This is one of a number of cases where we get a glimpse of an issue and then it disappears from view. Is it really so difficult for Private Office to be systematic about copying a string of papers on the same subject to us? I know that Private Secretaries are often very pressed for time, but other Private Offices manage to be consistent about circulation lists by delegating responsibility for checking them to Duty Clerks or their equivalents. Could we discuss whether this could be done here?
3. Turning to the substance of these papers, John Hoskyns also thought that the action outlined by the Chancellor in paragraph 5 of his minute seemed inadequate. He thought a firm of accountants with the right expertise (like Deloittes, Coopers etc) was needed. I suggest this point could be covered by inserting the following after the second sentence of paragraph 3 of the draft Private Secretary letter supplied by Mr Priestley:

X "She hopes that full consideration will be given to the use of a firm of professional accountants with the appropriate expertise in this ~~very~~ specialised area." X
4. I have suggested a couple of ways in which the letter could be toned down slightly (on a copy attached) *and shortened!*



ANDREW DUGUID

Minutes

Wiggins Esq
HM Treasury

*criticising the Government's
arrangements for welfare
audit*

INTERNAL AUDIT

1. The Prime Minister ^{was} ~~is~~ grateful for the Chancellor's minute of 11 March ~~and for~~ giving her advance warning of the Comptroller and Auditor General's ~~adverse~~ report ^{The matter was of some discussion briefly in Cabinet last week.}

2. The Prime Minister feels ~~very strongly~~ that Ministers have the right to expect their Permanent Secretaries to ~~ensure~~ ^{ensure} guarantee them that the arrangements for caring for ~~the~~ ^{the} ~~taxpayers'~~ ^{taxpayers'} resources ~~placed in their hands on behalf of the taxpayer~~ ^{money} are beyond reproach. She ^{was} ~~is~~ shocked to ^{learn} ~~hear~~ that the Treasury and CSD accept as valid the ^{Craig's} criticisms that internal audit lacks professionalism and top management support, with the result that systematic abuse would probably go undetected. ~~The Prime Minister finds it hard to regard this as anything other than a serious neglect of duty by senior officials over a period of years which is difficult to explain or excuse.~~

3. The Prime Minister is glad to hear that ^{Sir Douglas Wilson and Sir John Bannister have} an initiative ~~is~~ in hand. She would like to be informed of the main elements in the programme of reform ^{to} to which the Chancellor refers, preferably ⁱⁿ ~~in~~ ^{advance} of officials' ~~appearing~~ ^{before} before the PAC next month. ^{Plan} The Government will be severely criticised ^{if} if its programme ^{is} is not seen to be adequate.

insert as per minute

4. ~~Finally,~~ ^{step is also covered last} the Prime Minister ~~thinks that~~ the terms of the joint letter to Permanent Secretaries, as ^{outlined} suggested in

para^{graph} 5 of the Chancellor's minute, ^{shall} ~~appear~~ ^{may be too} ~~in the circum-~~ ^{tentative.}
stances ^{too} ~~unsuitably~~ mild. ~~She wishes Permanent Secretaries~~
~~to be left under no illusion about their duties as stewards~~
on behalf of Ministers and ^{She does not want any} ~~there to be no suggestion~~ ^{imposition} ^{suggestion} that
action by ^{Permanent Secretaries} ~~them~~ to tighten up their audit arrangements is
optional.

5. I am ^{sent copies of} ~~copying~~ ^{W.H.} this ^{John Roseley} to Edward Chaplin (CSD) and
~~Clive Priestley (Sir Derek Rayner's Office)~~ ^{for} ~~Clive Priestley~~.

[Private Secretary]



cc: Sir Derek Rayner's office
19/3

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

PRIME MINISTER

Yes please
not

Prime Minister

The main points are brought out in comments from Derek Rayner's office at A.

Would you like us to comment on your behalf as in draft at B, or would you prefer just to give a general blessing?

ACCOUNTING OFFICERS MEMORANDUM

I think you should know that I propose to authorise the Treasury to take into use a revised version of the Memorandum sent to Accounting Officers when they are appointed.

MR

..... 2. The attached note (A) explains the purpose of this document, and discusses points in the revision to which attention should be drawn. The full text of the new version is annexed (B), together with the old version (C).

3. I am satisfied that the new version is a useful improvement on the old. It fits in with the work being promoted by Sir Derek Rayner to define management responsibilities more clearly and specifically. The clarification of the relationship between the Accounting Officer and his Minister, and the affirmation of the supremacy of Ministerial authority, support the emphasis we are giving to Ministerial responsibility for management.

4. The note (A) discusses the comments of the PAC. I do not consider that these call for any delay or modification of the Memorandum. The Committee clearly expect it to be taken into use. That is what I propose. I shall see that the Committee are informed by some convenient means.

5. I am sending a copy of this minute to the Lord President.

(G.H.)

16 March 1981

REVISION OF THE ACCOUNTING OFFICERS MEMORANDUM

Under the Exchequer and Audit Departments Act 1866 the Treasury appoints for each Parliamentary vote an Accounting Officer, who has the duty of signing the accounts and appearing before the Public Accounts Committee as the principle witness at hearings on those accounts. In a Government department the Accounting Officer is normally the Permanent Secretary. On appointment, Accounting Officers are sent a memorandum setting out the duties involved.

2. This memorandum has been redrafted from time to time. The version currently in use dates mainly from the early 1950s. The most recent significant revision was in 1975, after an episode which attracted some publicity when the Accounting Officer of the Department of Industry protested against certain decisions taken by the then Secretary of State, Mr Benn.

3. A further revision is timely. The version now proposed has been worked up by the Treasury and the CSD, and reflects consultation with a number of Accounting Officers.

Sir Derek Rayner was associated with the work.

4. The new version is more precise and more accurate than the old on many points. It deals more specifically with various special cases, such as the additional Accounting Officers appointed in certain major departments, and with certain non-departmental bodies.

5. It usefully foreshadows, and is consistent with, other current work on the relationship between the Treasury and CSD on the one hand and spending departments on the other, and the work being developed in association with Sir Derek Rayner on defining more specifically the responsibilities of Ministers and Permanent Secretaries and other officials.

6. The Public Accounts Committee were consulted during their recent hearings on the role of the Comptroller and Auditor General (see below).

Significant changes

7. Attention should be drawn to two main changes of some substance in the new version.

8. First, it omits reference to the traditional doctrine that an Accounting Officer may be personally liable to refund expenditure deemed by the PAC as improper. Legal advice is that there is no basis for this doctrine either in law or in House of Commons procedure. In modern conditions it is not realistic : the sums of money which in practice engage the attention of the PAC are far too large. The PAC Chairman himself suggested in an earlier hearing that it might sensibly be dropped, and the PAC have made no reference to the omission in their comments.

9. Second, the new text makes clear that, while the Accounting Officer has certain specific responsibilities towards Parliament, these are ^{different} from and consistent with his main responsibilities towards his own Minister. The supremacy of Ministerial authority is stated unequivocally.

? NO
(we are checking)
M/R

10. The old text implies, somewhat confusingly, that an Accounting Officer may be responsible simultaneously, and possibly conflictingly, both to his own Minister and to Parliament. This reflects some widely-held beliefs, but both their constitutional logic and their historical pedigree are shaky. It is better to set the responsibilities of the Accounting Officer for economy and efficiency specifically within the framework of Ministerial responsibility and accountability. In practice it will not change the function of the Accounting Officer in relation to the PAC.

11. The PAC were interested in this point. This is reflected in their comments annexed. However, while they express some doubt, the positive recommendation at the end of the passage proposes a definition of the Accounting Officer's responsibilities to Parliament precisely in line with the revised memorandum. In any event, as the PAC recognise, this memorandum is an internal Government document, and they do not suggest any further amendment of it. Rather, the PAC Report assumes that the new version is to be taken into use. It is recommended that this should now be done.

11 March 1981

THE RESPONSIBILITIES OF AN ACCOUNTING OFFICER

A Permanent Secretary (or permanent head of a minor department who may be of lower rank) is appointed by his departmental Minister with the approval of the Prime Minister. Among his other responsibilities, he is responsible to his Minister for the propriety and regularity of his department's expenditure, and for prudent and economical administration. All his functions are governed by the two fundamental principles, that it is the Minister in charge of a department who is responsible to Parliament for all aspects of its policies, organisation and management, and that officials derive their authority from the Minister in charge of their department and are accountable to him for their actions.*

2. In most cases the Permanent Secretary is the Accounting Officer for Votes and accounts administered by his department. In certain departments Accounting Officer responsibility for certain Votes or other accounts is sometimes assigned to very senior officials other than the head of the department, usually of the rank of Second Permanent Secretary. The position of these other departmental Accounting Officers, in so far as it differs from that of permanent heads, is described in paragraphs 19-20 below. The duties of Accounting Officers for non-departmental bodies are described in paragraphs 21-25.

3. Appointment as Accounting Officer is made by the Treasury in compliance with Section 22 of the Exchequer and Audit Departments Act 1866. It lays on the appointee the personal duty of signing the accounts specified in his letter of appointment and, by virtue of that duty, the further duty of being the principal witness on behalf of the department before the Committee of Public Accounts (PAC), to deal with questions arising from those accounts. From these duties flow certain responsibilities which are in any event part of the responsibilities of a Permanent Secretary, but which are traditionally associated with, and emphasised by, his role as Accounting Officer. It is these responsibilities which are the subject of this memorandum.

* This paragraph describes the common case of a Government department with a departmental Minister and a permanent head. In some cases the machinery of appointment is different, and specific powers may be vested in, for example, the Commissioners of Inland Revenue, and Customs and Excise, or in certain named office-holders, so that, to this extent they may have authority not derived from Ministers. Nevertheless Ministers remain answerable for them to Parliament. The principles set out in the rest of this paper are therefore relevant to the Accounting Officers for these departments too.

4. The standard practice of appointing the permanent head of a department as the Accounting Officer for that department's Votes and accounts reflects the view that finance is an inseparable element in most policy questions, and financial responsibility an inseparable part of efficient organisation and management. The permanent head is the only official in a position to discharge responsibility as a whole for the money entrusted to the department, for its resources of manpower, and for the control of assets in its keeping such as land, buildings or other property.

5. The responsibilities of an Accounting Officer can be summarised as follows:

- (a) He must sign the Appropriation and other Accounts assigned to him. Although the underlying accounting work will have to be carried out by members of the department on his behalf, the Accounting Officer's signature implies personal responsibility for the correctness of the account and, in the case of a trading account, that in his opinion it is properly drawn up so as to exhibit a true and fair view of the transactions and state of affairs of the services to which it relates. In the case of other accounts, known as "White Paper" accounts, prescribed by specified legislation, for example in regard to advances to nationalised industries, the legislative context generally determines the nature and extent of the Accounting Officer's responsibilities.
- (b) He must ensure that correct financial procedures are followed, including specifically those mentioned in paragraphs 7 and 8 below; and more broadly that the accounts for which he is responsible are maintained in a form suited to the requirements of management as well as in the form prescribed for Vote accounting purposes.
- (c) He must ensure that the public funds for which he is responsible as Accounting Officer are properly safeguarded, with independent and effective checks, made without reference to personal considerations, of cash balances in the hands of any official. Similar care, including checks as appropriate, must be taken of stores or any public property.

- (d) He must ensure that, in the consideration of policy proposals relating to the expenditure or income for which he is Accounting Officer, all relevant financial considerations are taken into account, and where necessary brought to the attention of Ministers with appropriate emphasis and in an appropriate form. These considerations include the need for economy and the avoidance of extravagance or waste.
- (e) Similarly he must ensure that in the implementation of expenditure programmes as authorised by Ministers proper regard is given to economy and the avoidance of waste.

6. Proper management of expenditure includes the preparation of the material on which decisions are taken; the efficiency with which administrative operations are carried out; the cost-consciousness of staff at all levels; the provision of special skills and services (scientific, statistical, accountancy, O & M etc) for handling particular problems, and the selection and training of staff. Good management requires effective delegation. A person appointed to be an Accounting Officer cannot perform himself, or even closely supervise, all the various procedures needed to carry out his responsibilities. He must make sure that his department is organised and staffed on sound lines, particularly in the finance and establishment branches so as to provide for proper delegation of duties. He should pay particular attention to the adequacy and effectiveness of arrangements for internal audit. The officer in charge of this function should normally be responsible to the Principal Finance Officer, with direct access to the Accounting Officer where necessary.

Regularity and Propriety of Expenditure

7. An Accounting Officer has a particular responsibility for ensuring compliance with Parliamentary requirements in the control and management of expenditure. A fundamental requirement is that the funds for which he is responsible should be applied only to the extent and for the purposes authorised by Parliament. In the case of voted expenditure he must ensure that any payments made are within the ambit and amount of the Vote, and that Parliamentary approval has been sought and given. In cases not covered by the original estimate, eg in connection with a service not contemplated when the original estimate was presented, or where a temporary advance from the Contingencies Fund has been sanctioned by the Treasury, he must

ensure that Parliamentary approval is sought and given at the earliest opportunity by way of a Supplementary Estimate, or if necessary Excess Vote. In cases involving losses or special payments, he must ensure that Parliament's attention is drawn to the matter by suitable notation of the Appropriation Account.

8. The Accounting Officer is responsible for ensuring that specific Treasury or Civil Service Department sanction for the expenditure has been obtained in all cases where it is required. It is required for any expenditure not covered by any standing authorities delegated by the Treasury or the Civil Service Department to the Department. It is required before expenditure is incurred on any subhead of a Vote in excess of the amount specified for that subhead in the Estimates, even though savings may be available elsewhere and the expenditure itself falls within the delegated authority of the department. Expenditure may never be incurred in excess of the total net sum authorised by Parliament to be spent on any one Vote, save where a temporary advance from the Contingencies Fund has been sanctioned by the Treasury, in which case as mentioned in paragraph 7 Parliamentary approval for its repayment must be sought at the earliest opportunity. The Accounting Officer is also responsible for ensuring that adequate machinery exists for the collection and bringing to account in due form of all receipts of any kind connected with the Votes and accounts for which he is responsible.

Relations with the Minister

9. The Accounting Officer has particular responsibility to see that appropriate advice is tendered to Ministers on all matters of financial propriety and regularity and more broadly as to all considerations of prudent and economical administration. He will need to determine how and in what terms such advice should be tendered, and whether in a particular case to make specific reference to his own duty as Accounting Officer to justify to the PAC his department's expenditure.

10. If the Minister in charge of the department is contemplating a course of action involving a payment which the Accounting Officer considers would infringe the requirements of propriety or regularity, the Accounting Officer should set out in writing his objection to the proposed expenditure and the reasons for his objection. If the Minister decides nonetheless to proceed, the Accounting Officer should seek a written instruction to make the payment. Having received such an instruction, the Accounting Officer must comply with it, but should then inform the Treasury (who will in turn inform the Civil Service Department where appropriate) of what has occurred, and should also communicate the papers to the Comptroller and Auditor General. Provided that this procedure has been followed, the PAC can be expected to recognise that the Accounting Officer bears no personal responsibility for the expenditure.

11. If a course of action is in contemplation which raises an issue not of formal propriety or regularity but more widely of prudent and economical administration, it is the duty of the Accounting Officer to draw the relevant factors to the attention of his Minister and to advise him in whatever way he deems appropriate. He may think it right to refer to the possibility of criticism by the PAC. If his advice is overruled, he should ensure that both his advice and the overruling of it are apparent clearly from the papers.

Appearance before the PAC

12. An Accounting Officer appears before the PAC to answer their questions concerning the expenditure from the Votes and other accounts for which he is Accounting Officer and related activities. He may be supported by other officials, who may, and commonly do, join in giving the evidence.

13. The Financial Secretary to the Treasury is formally a member of the Committee but rarely attends. Treasury officials regularly attend Committee hearings and are usually asked to comment on the evidence. They then speak as representatives of the Executive and subject to collective Ministerial authority, but are expected to comment from the standpoint of the department which has the formal responsibility for presenting Estimates to Parliament and for prescribing the form of accounts. This goes with the Treasury's central responsibility for the operation of public expenditure control. Parliament has traditionally regarded the Treasury as an ally in controlling expenditure.

14. The Accounting Officer will be expected to furnish the PAC with explanations of any indications of irregularity, waste or extravagance or inefficient administration, or weakness in financial procedure, to which their attention has been drawn by the Comptroller and Auditor General or about which they may wish to question the Accounting Officer.

15. In practice, the Accounting Officer will have delegated authority widely, but he cannot on that account disclaim his responsibility. Nor, by convention, does the incumbent Accounting Officer decline to answer questions where the events took place before he assumed his appointment; the Committee may be expected not to press his personal responsibility in such circumstances.

16. The Committee have emphasised the importance they attach to accuracy of evidence, and the responsibility of witnesses to ensure this. The Accounting Officer should ensure that he is adequately and accurately briefed on matters on which he gives evidence. He may ask the Committee for leave to supply information not within his immediate knowledge by means of a later note. Should it be discovered subsequently that the evidence provided to the Committee has contained errors, these should be made known to the Committee at the earliest possible moment.

17. In general, the rules and conventions governing appearances of officials before Parliamentary Committees apply to the PAC, including the general convention that civil servants do not disclose the advice given to Ministers. Nevertheless, in a case where the procedure described in paragraph 10 was used concerning a matter of propriety or regularity of expenditure, the Accounting Officer's advice and its overruling by the Minister, would be disclosed

to the PAC. In a case where advice of an Accounting Officer has been overruled in a matter not of propriety or regularity but of prudent and economical administration it will be appropriate for an Accounting Officer, questioned about the matter at the PAC, to lay stress on the fact that it was a decision by his Minister. He should seek to avoid disclosing advice given to his Minister, but should be ready to explain the reasons for the Minister's decision and may be called on to satisfy the Committee that all relevant financial considerations were brought to the Minister's attention before the decision was taken. It will then be for the PAC to pursue the matter further with the Minister if they so wish.

Absence of Accounting Officer

18. The PAC may be expected to postpone a hearing if the relevant Accounting Officer is temporarily indisposed. Where the Accounting Officer is unable by reason of incapacity or absence to sign the Appropriation Account in time to render it to the Comptroller and Auditor General, the department may render unsigned copies pending his return. If the Accounting Officer is unable to sign the Account in time for printing the department should ask the Treasury to appoint an interim Accounting Officer.

Additional Accounting Officers

19. Where one or more senior officials, other than the permanent head of the department, are appointed as Accounting Officers for certain Votes or accounts, there should be a clear understanding of their relationship not only with their Minister but also with the permanent head. The permanent head remains in general charge of the department, and in particular, of its organisation, management and staffing and department-wide procedures in financial and other matters. He must ensure that these promote the efficient and economical conduct of all its affairs, and safeguard financial propriety and regularity throughout the department. It is within that framework that any additional Accounting Officers are responsible for the Votes and accounts assigned to them. In matters affecting their responsibilities as Accounting Officer, their judgement

should only be overridden by or with the specific agreement of their Minister. In such cases the Minister may also seek the views of the permanent head.

20. The position of an additional Accounting Officer when he appears before the PAC is thus different from that of a permanent head who carries full responsibility under his Minister for the organisation and management of his department as a whole. An additional Accounting Officer is however able, on the basis of his discharge of his own responsibilities, to answer most questions which may be raised by the PAC concerning expenditure and activities in his field. If PAC questioning is directed to matters determined by the permanent head and the additional Accounting Officer finds himself in difficulty in responding, the Committee could be expected to accede to a suggestion that they seek evidence from the permanent head as well as from the Accounting Officer for the expenditure under discussion.

Accounting Officer Appointments in Non-Departmental Bodies

21. The Treasury also appoints Accounting Officers for some non departmental public bodies (eg the Manpower Services Commission, most museums and galleries, the Scottish and Welsh Development Agencies and the Research Councils). Appointments of this kind are made by analogy with appointments of Accounting Officers in departments. The normal practice is to appoint the senior full-time officer of the body. Those so appointed have broadly the same duties as Departmental Accounting Officers as described above and exercise them on behalf of the office holder or holders in charge of the body. With the exception of bodies (such as museums and galleries) with their own Vote, the responsibilities of these Accounting Officers are confined to the grant in aid account of the body which is financed from the Vote of its sponsoring department.

22. Whether or not a grant-aided body has its own Accounting Officer, the responsibility of the Accounting Officer in the sponsor department is to ensure that the conditions attached to the grant-in-aid conform with the terms of the Vote; to monitor compliance with these conditions by the body; and to satisfy himself that the financial and other controls applied by the department are appropriate and sufficient to safeguard public funds. Among other things he will need to satisfy himself about the quality of its management. The Accounting Officer of the body in receipt of the grant-in-aid has a special responsibility to see that the rules and conditions laid down by the Department issuing the grant-in-aid are observed.

23. An Accounting Officer in a grant-aided body will normally appear before the PAC alongside the Departmental Accounting Officer responsible for the payment of the grant-in-aid.

24. The absence of an Accounting Officer appointment in a non-departmental body does not lessen the nature and scope of its accountability to Ministers and through them to Parliament, or the right of the PAC to take evidence direct from the body if it wishes. The approved signatory of the accounts, normally the Chairman or Chief Executive, will, as in the case of a Departmental Accounting Officer, automatically assume a primary responsibility to answer for that body in any examination by the PAC and may be summoned to appear before the Committee for that purpose.

THE RESPONSIBILITIES OF AN ACCOUNTING OFFICER

Note by the Treasury

Accounting Officers are appointed by the Treasury in compliance with section 22 of the Exchequer and Audit Departments Act, 1866. An extract from the Act is attached.

2. It was from the outset inherent in the concept of an Accounting Officer that he should be responsible, at least in financial matters, for the work and organisation of his Department.

3. In the 1920's it came to be accepted that finance is an inseparable element in all policy questions, that financial responsibility has wider implications for efficient management, and consequently that financial and administrative responsibility should be concentrated in one person in each Department. Hence the Permanent Head of the Department came to be appointed as Accounting Officer, as the only official in a position to discharge both responsibilities. More recently some very large Departments have been created, each with a number of Votes. In these and a few other special cases Accounting Officer responsibility for some of the Department's Votes has been assigned to very senior officials other than the Head of the Department.

RESPONSIBILITY FOR EFFICIENT AND ECONOMICAL ADMINISTRATION

4. The Accounting Officer's responsibilities, in their widest sense, spring from the basic conception underlying British Government financial procedure and organisation, namely that due regard can never be paid to financial considerations if finance and administration are divorced so that finance is kept separate from other factors which enter into policy decisions.

(i) Connection between finance, policy and administration

The Accounting Officer must make sure, as a prerequisite of efficient and economical management, that financial considerations are taken into account at all stages by his Department in formulating policy proposals, and in their execution. He must be prepared to answer for the efficient and economical conduct of his Department as a whole. The Plowden Report*, using a formulation still equally relevant, emphasised the importance of management, which it defined as covering the preparation of the material on which decisions are taken; the technical efficiency with which large administrative operations are carried out; the cost-consciousness of staff at all levels; the provision of special skills and services (scientific, statistical,

* "Control of Public Expenditure", Cmnd 1432, paragraphs 44 to 47.

accountancy, O & M, etc.) for handling particular problems; and the training and selection of staff. It is on these that effective control of expenditure and value for money depend.

(ii) Avoidance of waste and extravagance

As part of this general conception, the Comptroller and Auditor General is expected by the Public Accounts Committee to bring to the notice of Parliament any cases of apparent waste or extravagant administration (as well as any weakness in financial procedure). The Committee expect the Accounting Officer to satisfy them that the policy approved by Parliament has been carried out with due regard to economy, and to furnish them with explanations of any indications to the contrary to which their attention has been drawn.

(iii) Organisation and staffing of Department

The Accounting Officer cannot carry out this responsibility for efficient management unless he is supported by a sound organisation which provides for proper delegation of duties. It is therefore one of his chief duties to make sure that the Department is organised and staffed on sound lines. In particular, he should pay special attention to the organisation and staffing of both finance and establishment branches, and should encourage close liaison between them; for these branches have a particular responsibility on his behalf for seeing that full value is obtained for the expenditure of the public funds with which the Department is entrusted.

CONDUCT OF FORMAL FINANCIAL BUSINESS

5. (i) Safeguarding of public property

It is the Accounting Officer's duty to ensure that the public funds entrusted to his care are properly safeguarded and that there are independent and effective checks, made without reference to personal considerations, of cash balances in the hands of any official. Similar care must be taken of stores or any other public property.

(ii) Regularity and propriety of expenditure

It is equally part of his duty to ensure that the funds entrusted to him are applied only to the purposes intended by Parliament. He must satisfy himself, for instance, that any payments made by his Department are both within the ambit of the Vote and also covered by specific statutory authority where necessary; and that Parliamentary approval has been sought, normally by way of a Supplementary Estimate, in all cases in which it is appropriate to do so, eg in connection with a service not contemplated when the original Estimate was taken. That this has been done is implicit in the signature of the Account.

Furthermore, the Accounting Officer is responsible for ensuring that specific Treasury sanction for the expenditure has been obtained in all cases which are not covered by any standing authorities delegated by the Treasury to the Department. Expenditure may not be incurred in excess of the total sum authorised by Parliament to be spent on any one Vote; nor may the Accounting Officer, without the prior sanction of the Treasury, incur expenditure on any Subhead of a Vote in excess of the amount specified in the Estimates, even though savings may be available elsewhere, and though the expenditure would itself fall within the delegated authority of the Department. The Accounting Officer is answerable to the Public Accounts Committee for the formal regularity and propriety, in the senses described above, of all the expenditure out of the Votes and Accounts for which he is responsible. Similarly he is expected to ensure that adequate machinery exists for the due collection and bringing to account of all receipts of any kind connected with these Votes and Accounts.

(iii) Consultation with the Treasury

If any questions are raised concerning the propriety of a particular payment, the Committee may seek the view of the Treasury; and they will normally wish to know whether the Treasury have been consulted. The Accounting Officer should, therefore, ensure that before his Department enters into any transaction the regularity of which may be called in question, the advice of the Treasury is sought. Treasury officials are present, when departmental Accounting Officers are examined by the Public Accounts Committee, and answer for any advice which the Treasury have given. This Treasury advice does not, however, absolve the

Accounting Officer from his responsibility. He should therefore also make sure that any issue of sufficient importance seriously to call in question that responsibility is brought to his personal attention even though the advice of the Treasury may already have been obtained. Relations with the Treasury are discussed more fully in paragraph 6 of this note.

(iv) Accounts other than Appropriation Accounts

This note, in general, refers to responsibility for Appropriation Accounts. Many Accounting Officers are responsible also for other Accounts. The same principles apply to these accounts. They include stock and store accounts maintained under section 4 of the Exchequer and Audit Departments Act, 1921; and accounts of trading and commercial services which the Treasury direct to be maintained under section 5 of that Act. It is implicit in the signing of a trading account that in the Accounting Officer's opinion it is properly drawn up so as to exhibit a true and fair view of the transactions and state of affairs of the services to which it relates.

Apart from the accounts required to be prepared under the provisions of the Exchequer and Audit Departments Acts, there are accounts, known as "White Paper" Accounts, prescribed by specific legislation such as that relating, for example, to advances to the Nationalised Industries. For these accounts the extent of the Accounting Officer's responsibilities will be largely determined by the nature of the legislation; and may vary from a minimum of ensuring that the sums authorised by Parliament to be paid are duly handed over and any repayments properly brought to account, to an extensive responsibility for the affairs of the organisation itself.

(v) Personal Accountability

Dereliction of the Accounting Officer's duty, set out in this paragraph, for the proper conduct of financial business, renders him liable, under the doctrine of personal accountability, to refund any expenditure which the Public Accounts Committee recommend should be disallowed. There is, however, a recognised procedure, set out in paragraph 7(ii) of this note, to protect an Accounting Officer should he be overruled by his Minister in a matter which may lay him open to a financial penalty.

6. The relationship between Departments and the Treasury was defined in the Plowden Report*:-

"The relationship should be one of joint working together in a common enterprise; it should be considered not in terms of more or less "independence" of Departments from "control" by the Treasury, but rather in terms of getting the right balance and differentiation of function.

The primary responsibility of a Department is to conduct its policy effectively within the limits laid down by the Government. The Department is itself responsible for the efficiency with which it does its work; the Permanent Secretary, as Accounting Officer, is responsible for the financial management

The Treasury is the Department with the central responsibility for economic and financial policy, the custodian of the Exchequer, and the authority for Civil Service and establishment matters.

It bears the responsibility:-

- (a) for allocating the amount of money and economic resources to be made available for each purpose to each Department;
- (b) for advising the Departments on economic and financial matters, and for assisting them to maintain proper practice in the expenditure of public money;
- (c) for the overall efficiency of the public service, and thus for seeing that the Departments are staffed, particularly at the top levels, with the best available officers ^{drawn} ~~down~~ from the Service as a whole;
- (d) for the development of management services throughout the public service; for taking the initiative in the introduction of new management techniques; and for keeping an oversight over the management practice of all the Departments;
- (e) for the settlement of pay and conditions of service, and grading of staff throughout the Service."

These principles remain fully valid today. At the time when the Plowden Report was prepared the Civil Service Department had not been set up. The subjects listed under (c), (d) and (e) above are now the responsibility of that Department. The effective discharge of the responsibilities of the Treasury and of the Civil Service Department calls for the fullest co-operation of the Accounting Officers of Departments. Their appointment by the Treasury is a mark of the responsibility which they, no less than the Treasury, have as trustees for the taxpayer.

RELATIONS WITH THE MINISTER

7. (i) Matters affecting efficient and economical administration

Senior officials must advise their Minister freely, candidly and in confidence about all aspects of the policy area for which they are responsible, including financial aspects. Where an official is also designated an Accounting Officer, he has a particular responsibility to Parliament in connection with the requirements of efficiency, financial prudence and economical resource use in the conduct of his Department, and he will from time to time need to advise his Minister from this standpoint. There is a wide range of occasions on which advice may be called for, orally or in writing; and the degree of emphasis which is necessary will vary from case to case.

It is for the Accounting Officer himself to decide how and in what terms to give his advice, and whether to make any specific reference to his position as Accounting Officer and the guidance he has received on appointment. He should, however, be ready to state clearly and explicitly, in writing, to his Minister his disagreement with any aspects of a proposal which as Accounting Officer he considers he would have difficulty in defending as a matter of prudent and economical administration before the Public Accounts Committee; and to ask for a specific instruction from his Minister on these issues if his advice is not accepted. Having done so, he must, if the Minister adheres to his decision, accept it; in which case he should support any subsequent defence of the action taken by reference as necessary to the policy ruling given by his Minister.

(ii) Matters affecting the Accounting Officer's personal accountability for the conduct of financial business

Alternatively, the matter which is the subject of the Accounting

Officer's representations may be one which involves his personal liability on a question of formal regularity or propriety, referred to in paragraph 5. In that case he should set out in writing his objection to the proposed expenditure, and the reasons for his objection, and should make the payment only upon a written instruction from his Minister overruling the objection. After making such a payment, the Accounting Officer should inform the Treasury of the circumstances and should communicate the papers to the Comptroller and Auditor General. Provided that this procedure has been followed, the Public Accounts Committee will no doubt acquit him of any personal responsibility for the expenditure.

Extract from the Exchequer and Audit Departments Act, 1866, Section 22

"On or before the days specified in the respective columns of ... Schedule A annexed to this Act, accounts of the appropriation of the several supply grants comprised in the Appropriation Act of each year shall be prepared by the several departments, and be transmitted for examination to the Comptroller and Auditor General and to the Treasury, and when certified and reported upon they shall be laid before the House of Commons; and such accounts shall be called the "Appropriation Accounts" of the moneys expended for the services to which they may respectively relate; and the Treasury shall determine by what departments such accounts shall be prepared and rendered to the Comptroller and Auditor General and the Comptroller and Auditor General shall certify and report upon such accounts..; and the reports thereon shall be signed by the Comptroller and Auditor General: Provided always, and it is the intention of this Act that the Treasury shall direct that the department charged with the expenditure of any vote under the authority of the Treasury shall prepare the appropriation account thereof: Provided also, that the term "department", when used in this Act in connection with the duty of preparing the said appropriation accounts, shall be construed as including any public officer or officers to whom that duty may be assigned by the Treasury."

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2.

Prime Minister.

Mr PATTISON

I think the letter should go. It is excellent.

You may be interested to see this, though I think yesterday's Cabinet discussion has made it unnecessary to send out a letter from here. AM 13/11

INTERNAL AUDIT

1. This minute offers some background information to help the Prime Minister in responding to the Chancellor of the Exchequer's minute of yesterday and suggests a draft private secretary reply.

Background

2. It is true that the Bancroft/Wass initiative "has Sir Derek Rayner's full support", but it remains for him to see and comment on a final draft of the joint letter to Permanent Secretaries. The present draft by no means has his wholehearted endorsement.

3. For the last three months Sir DR has been pushing, first CSD and now Treasury and CSD, to produce a plan for the reform of internal audit, rather than (as was CSD's first instinct) a too gentle, all too conscious of the problems plea to departments to do better.

4. The main things which struck Sir DR in this matter included these:

a. It is extraordinary that - despite all the emphasis the Service lays on accountability to and the Accounting Officer's special relationship with Parliament - the audit arrangements should be as bad as they have been described in the papers to which the Chancellor refers.

b. As only about 1 in 50 of the Government's internal auditors are professionally qualified (some units having no professionals at all), financial management in the Service is doubly unprofessional - its amateurs in finance branches are advised by amateur auditors.

c. The defectiveness of internal audit is attributable in part to confusion and indecisiveness at the centre. An early CSD draft observed:

"A contributory factor [in the failure to produce adequate standards of internal audit] has been the fact that the central expertise has been developed in the CSD, while the policy for internal audit standards rests with the Treasury. Partly for this reason, and partly because there has not so far been developed a clear doctrine about the extent to which the central departments should be responsible for satisfying themselves about the adequacy of departmental management systems (including audit), the centre has developed its concern with audit as an advisory part of its management services and not as a subject on which it should make standards mandatory and monitor their achievement."

d. The Service as a whole has so far failed to grasp the fact that high quality audit (of the kind provided to M&S by Deloitte, Haskins and Sell) goes very much further than the rather low level "propriety and regularity" audit on which it has concentrated, partly because professionalism is still looked at askance.

5. Sir DR regards the deficiencies of internal audit as an example not merely of the under-development of financial management in the Service but also of the neglect which can result from the "privacy" of Service management to which he referred in his minute to the Prime Minister of 30 January on management review.

campaign,

6. He therefore believes that a vigorous/under determined Treasury leadership, is needed to up-rate the quality of internal audit and of financial management generally. The Chief Secretary, who lunched with Sir DR on Monday, takes the same view in respect of financial management.



7. Reforming internal audit cannot be done quickly or easily. There are problems of attitudes, recruitment, training and - especially in relation to the new science of computer audit - technique. But there should be no shadow of doubt about either the need or the determination and imagination which will be needed to satisfy it.

Reply to the Chancellor

8. I attach a private secretary letter for consideration. It calls a spade a spade without overdoing it (I trust) and emphasises the importance of effective action.

SP

C PRIESTLEY
12 March 1981

Enc: Draft letter to Mr Wiggins

J A Wiggins Esq
HM Treasury


INTERNAL AUDIT

1. The Prime Minister is grateful for the Chancellor's minute of 11 March and for giving her advance warning of the Comptroller and Auditor General's adverse report.

2. The Prime Minister feels very strongly that Ministers have the right to expect their Permanent Secretaries to guarantee them that the arrangements for caring for the resources placed in their hands on behalf of the taxpayer are beyond reproach. She is shocked to hear that the Treasury and CSD accept as valid the criticisms that internal audit lacks professionalism and top management support, with the result that systematic abuse would probably go undetected. The Prime Minister finds it hard to regard this as anything other than a serious neglect of duty by senior officials over a period of years which is difficult to explain or excuse.

3. The Prime Minister is glad to hear that an initiative is in hand. She would like to be informed of the main elements in the programme of reform to which the Chancellor refers, preferably in advance of officials' appearing before the PAC next month. The Government will be severely criticised of its programme is not seen to be adequate.

4. Finally, the Prime Minister thinks that the terms of the joint letter to Permanent Secretaries, as suggested in



para. 5 of the Chancellor's minute, appear - in the circumstances - unsuitably mild. She wishes Permanent Secretaries to be left under no illusion about their duties as stewards on behalf of Ministers and there to be no suggestion that action by them to tighten up their audit arrangements is optional.

5. I am copying this to Edward Chaplin (CSD) and Clive Priestley (Sir Derek Rayner's Office).

[Private Secretary]

Cabinet / Cabinet Committee Document

The following document, which was enclosed on this file, has been removed and destroyed. Such documents are the responsibility of the Cabinet Office. When released they are available in the appropriate **CAB (CABINET OFFICE) CLASSES**.

Reference: CC(81) 11th Conclusions, Minute 1

Date: 12 March 1981

Signed A Wayland Date 19 April 2011

PREM Records Team

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Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

Prime Minister.
This is lamentable. And of course it links with the weaknesses we have seen recently in the Government's accountability capability and in relation to standards of focus in trouble.

HM
11/11

PRIME MINISTER

INTERNAL AUDIT

I am writing to give you advance warning of the publication, probably within the next week or two, of a highly critical report which the Comptroller and Auditor General has prepared for the PAC on the state of internal audit in Government. Treasury and CSD officials, and probably officials from some other Department, will be appearing before the PAC to answer questions about the report early in April.

2. The C & AG's diagnosis is that internal audit in Government has suffered from lack of professionalism, and lack of top management support. He believes that we are especially at risk in the area of computer audit. The Chief Inspector of Local Government External Audit not long ago made similar criticisms of internal audit in local government.

3. The C & AG does not identify specific cases of fraud or other types of leakage. This was not the purpose of his report. What he does suggest is that if there were systematic abuses we would be unlikely to know about them.

4. The report is disturbing. We and the CSD are well aware of the worrying problems and risks in this area. We accept the validity of the main criticisms - indeed the

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severest ones are based on the results of studies commissioned by CSD which confirmed the risks being run on computer systems. We must expect adverse publicity. The situation illustrates the need for the central departments to adopt a more positive role in relation to standards of financial management and control in Government departments.

5. Sir Douglas Wass has told me that he and Sir Ian Bancroft intend to send a joint letter to Permanent Secretaries to impress on them the urgency of remedial action, and suggesting a long-term programme of reform with emphasis on training and career management. It will emphasise the service that internal audit can provide for efficient management, and ask Permanent Secretaries to take a close personal interest in their department's internal audit arrangements, to review the objectives and staffing of the sections concerned, and to look particularly at the quality of the person in charge. I welcome this initiative, which, I believe, will set in motion a substantial and necessary improvement. It also has Sir Derek Rayner's full support.

6. I am sending a copy of this minute to the Lord President and to Sir Derek Rayner.

A handwritten signature in black ink, appearing to be 'G.H.' with a stylized flourish.

(G.H.)

" March 1981

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Gov. March



cc: Chief Secretary
Financial Secretary
Sir Douglas Wass
Sir Anthony Rawlinson
Mr. Bailey
Mr. Littler
Mr. Burnger
Mr. Kemp
Mr. Kitcatt
Mr. Unwin
Mr. Perry
Mr. Ridley
Mr. C. Whitmore - No.10

MR. CAREY

AW
bin

THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

The Chancellor discussed his minute to the Prime Minister of 24 February briefly with her on 3 March. I understand from Mr. Whitmore that the Prime Minister raised no objections to the arrangements suggested for interdepartmental study of the PAC's recommendations. The way is therefore open for the Treasury to organise the work, on the lines indicated in the Chancellor's minute.

JW

(A.J. WIGGINS)

6 March 1981

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ROLE OF THE COMPTROLLER AND AUDITOR GENERAL - PAC REPORT

Background

The report was published on Wednesday 4 March. It follows the Government's Green Paper of March 1980. At the moment, the C & AG's audit covers mainly Government departments, plus a number of statutory boards, but does not include the nationalised industries. The PAC argues the principle that the C & AG should be able to report on all bodies in receipt of public money, and recommends that while the normal financial audit of the nationalised industries, NEB, BNOC should continue, the C & AG should have access to the books in order to report to Parliament. He should also have access to the books of all companies and bodies in receipt of voted grants and loans. He should carry out the external audit of the NHS, and the staff which audit local authorities should come under him. His own department and the other staff would be reformed into a National Audit Office, borne on the House of Commons. Vote, and the C & AG will be appointed by the Crown on the recommendation of the House. The Green Paper argued that the C & AG should examine only where Ministers are accountable and thus he should not have access to the nationalised industries, etc. On local authorities, the Green Paper pointed to their local accountability.

Line to Take

The Government is most grateful to the Chairman of the PAC, and his Committee, for a most stimulating report. It has only just been published, and I cannot comment now on its wide ranging recommendations. The Government will give the report its fullest consideration, and make known its views in due course.

Supplementaries

Q1 Difference between PAC report and Green Paper

Answer: Yes there are important differences between the two.

It was a Green Paper. The PAC report raises important

and fundamental issues and we will look at the arguments very carefully.

Q2 When and how will the Government reply

Answer: There will be no unnecessary delay, but the report raises extensive and important questions. [If pressed - I would very much hope before the Summer Recess.] It would be normal for the Government to reply in a White Paper.

Q3 Legislation?

Answer: This will of course depend on the changes to be made. But if there is to be legislation, I would hope that it could be in the next Session.

Q4 Successor to Sir Douglas Henley (the present C & AG)

Answer: I am sure the PAC and the House will join in acknowledging the excellent service which Sir Douglas Henley has given. No decision has yet been made on his successor.

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Prime Minister 2.

Advance warning of PAC views on the role of Comptroller and Auditor-General. I am sure that informed discussion of these possibilities will be generally helpful.

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

Prime Minister.

PRIME MINISTER

You saw the PAC's report last week in connection with the appointment of a successor to the present C & AG. AMW 24.ii.

MJD 24/2.

THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

This minute is to give you advance notice that the Committee of Public Accounts (PAC) are expected to publish soon, probably on 4 March, their report on the enquiry which they have been conducting over recent months into the role of the Comptroller and Auditor General.

2. The starting point of their enquiry was the Government Green Paper (Cmd 7845) of last March "The Role of the Comptroller and Auditor General". Between them the Green Paper and the PAC Report amount to a major review of our public audit system, the first comprehensive review for over a hundred years.

3. Because of Nigel Lawson's formal position as a member of the Committee the Treasury have had a private sight of the Report. The PAC will be jealous of the privacy of their report at this stage, so our knowledge of it should be treated with discretion.

4. Under present legislation the C and AG is an independent office holder under the Crown and his audit reporting is mainly but not exclusively about the expenditure of central Government money. The PAC recommend some fundamental changes in these arrangements, of which the most important proposals are:

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- In addition to his present duties concerning Government Departments, the C and AG should scrutinise the accounts of the nationalised industries, of all other public corporations, and of any private body in receipt of Government grant or loan, in order to advise Parliament on the efficiency and effectiveness of the use made of public funds.

- The District Audit Service should come under the C and AG, who would report to the PAC on general issues, not specific to particular local authorities.

- The C and AG, and his staff in E and AD, should become servants of the House, supervised by a new Public Accounts Commission.

5. The PAC Report will be a unanimous one. The same proposals were advocated by the Expenditure and Procedure Committees of the last Parliament, and judging by Edward du Cann's evidence to the PAC recently the first two proposals above would certainly be supported by the Treasury and Civil Service Committee.

6. The Government's Green Paper took a more conventional line on these issues, but it was a Green Paper, and I see no reason for defensive or hostile reaction on our part to the PAC Report when it appears. The Report is bound to provoke debate, and I welcome this prospect. There are, of course, other developments going on in the area covered by the Report which we will need to take into account in deciding our reaction. For example in the case of nationalised industries we have been considering with the CPRS rather different possibilities for introducing efficiency audits and hope to be able to put proposals for colleagues shortly.

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Similarly Michael Heseltine has recently put forward rather different ideas for reforming local authority audit in the form of an Accounts Commission in England and Wales ; similar to that which already exists in Scotland. When the Budget is out of the way, I should like to give more thought to these important issues, and I think we shall need to consider our collective attitude rather carefully, taking account of the work already in hand in this area as well as public and Parliamentary reaction. There is also the point that Sir Douglas Henley's successor may soon be in post, and we might want to seek his views on all this. The PAC's recommendations about nationalised industries and local authorities were heavily influenced by suggestions from Sir Douglas Henley in evidence to them

7. Most of the PAC's proposals would require legislation. We need be in no particular hurry to make up our mind about this, but I think we must reckon on a debate in Government time before the Summer Recess. In the meantime I am asking my officials to start the preliminary work, with other interested Departments on studying the report and preparing papers on it for Ministerial consideration leading eventually to the drafting of a Government reply to the PAC Report in White Paper form. I will report back to you and Cabinet colleagues when I am in a position to make firm recommendations about this.

8. I am copying this minute to Christopher Soames and to Sir Robert Armstrong, but not, at this stage, to others. I should be grateful if colleagues would regard all information about the PAC report as being in the strictest confidence prior to publication.

A handwritten signature in black ink, appearing to be 'G.H.' with a stylized flourish.

(G.H.)

24 February 1981

Gov. Mark

cc for information

Mr GAFFIN

- ✓ Mr Pattison (CSD)
- Mr Buckley (CSD)
- Mr Green (CSD)
- Mr Colman (CSD)
- Mrs Gilmore (HM Tsy)
- Sir A Rawlinson (HM Tsy)*
- Mr Carey (HM Tsy)*

Mr HENNESSY, The Times

* with attachment

1. I understand that Mr Hennessy will probably run a piece in tomorrow's paper on Sir Derek Rayner's letter of 10 March to Sir Anthony Rawlinson (HM Treasury) on the Role of the Comptroller and Auditor General, which has just been published in evidence by the PAC. (It was copied at the time to the Prime Minister, Chancellor and CST.)
2. I attach a copy of the letter, as conveyed slightly edited, via the Treasury, to the Clerk of the Committee. This was in response to a request from her that Sir Derek Rayner should give oral evidence on the future of the E&AD, including that of the C&AG, which we resisted on the grounds that he was not an expert in that field.
3. The article may make some play with Sir Derek Rayner's view (para. 11c and d) that the C&AG should be specifically appointed and tasked by the House of Commons.

CP

C PRIESTLEY
25 November 1980



CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-~~270 4222~~ 233-8224

10 March 1980

Sir Anthony Rawlinson KCB
HM Treasury
Parliament Street
London SW1

THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

Thank you for your letter of 22 February and for the enclosed draft Green Paper, which I found a most readable and interesting document. I should like to make the following comments, some on the text as a draft, some on the issues.

General

2. The draft says nothing about the numbers or professional training of EAD staff or about the coverage of their work, eg about how much time they spend on the basic, financial and regularity audit of departmental accounts, on examining the efficiency and economy with which funds are spent and on investigating the effectiveness of programmes and projects in meeting established policy goals. That leaves me with no real grasp of the nature of the instrument the paper is addressing - who the staff are, where they are or what they do. It is therefore hard to apply oneself authoritatively to the first question raised in paragraph 5, mainly "What kinds of audit should the C & AG undertake?".
3. My second point follows on: what are the effects of traditional EAD audit and the extension "in appropriate cases into effectiveness audit" (paragraph 11)? I am feeling for the kind of results produced, both for Parliament and the public service, of conventional and newer audit in terms of the practices and behaviours of institutions on the one hand and of actual benefits in particular cases on the other. For example, are Ministers satisfied that the C & AG's audit function is producing institutional and particular results worth having? Are there practical examples one can quote in explanation of the "further extension of VFM audit" in paragraphs 11 and 16, for instance? And what view does the Treasury take, in the light of recent practice, for the correct balance of

effort as between basic, VFM and effectiveness audits (see paragraphs 18 and 20)?

4. A related point to which I attach great importance is the way in which the auditor presents himself and is perceived. In our business, I regard our auditors as allies, very much part of the team. It is a pity if the auditors in Government are regarded as unfriendly but if their skill lies only or mainly in playing a checking role they are bound to be seen so. To my mind it is a great waste of an important national asset if the EAD is always used by Parliament as a witness for the prosecution. Nor do I believe that Parliament can make sound judgements on the behaviour of the Executive if all the evidence it receives is of failure or rule-breaking. I would like to see EAD bringing examples of good management as well as bad before Parliament. This would help produce a much needed change in the climate of opinion in Westminster and in Whitehall. But obviously this depends on EAD having staff who know good management when they see it.

5. Thirdly, I am struck by the draft's references to lack of or limitation on definition, as in paragraphs 12 and 20. I have some sympathy with the traditional British virtue of avoiding being explicit in defining powers and relationships, but I should think there would be substantial merit if the EAD Acts are to be revised in indicating with reasonable precision how the C & AG and his staff are expected to spend their time, and what skills they should develop. In the case of paragraphs 20 and 21, I do not see how the C & AG can do good work on the adequacy of departmental systems without also doing some independent work on the effectiveness and value of particular policy instruments, because systems have to be tested by reference to examples of the work they are supposed to control. Nor do I see, under existing arrangements for supporting Select Committees where they can look for independent, professional assessments of policy instruments unless to the C & AG.

6. I therefore applaud the idea (paragraph 24) that the C & AG's power to audit particular bodies should be provided for "by statute wherever practicable", provided of course that this does not exclude important classes of or particular institutions from examination.

Range of the C & AG's audit

7. While I take the point that Ministers' technical responsibility for public funds transferred to companies does not extend beyond making the payment provided for by Parliament (paragraph 30), I think it would be worth stating here how the taxpayer is assured that his tax pound has been properly and effectively spent. Similarly, at the end of paragraph 31, it would be helpful to establish who decides whether the C & AG's audit and inspection should be extended to a particular "public funded body".

Local authorities

8. I sympathise with the drift of paragraph 41, but I think that it would be worth a sentence or so more to explain the conundrum in accountability terms represented by:

- the constitutional autonomy of local authorities
- the fact that they are nonetheless funded to a large extent by national taxation
- the restrictive nature of local government Ministers' accountability to Parliament for the money spent through RSG
- the absence of any local authority accountability to Ministers or Parliament for that money
- the specific nature of Parliament's legitimate interest in respect of money voted by it to pay for RSG.

Keep section "The text" ... not

9. You might like to know, by way, that [a very senior local government officer] told me the other day that RSG should be regarded as general tax money, that it was not especially relevant that it came from Parliament rather than from local property taxes and that it was a misconception to suggest that there should be an accountability for it separate from that of Members to their local electorate. I have always regarded this as a very odd idea.

Nationalised industries

10. Does paragraph 50 mean that the Government is satisfied that nationalised industries are efficient and have appropriate means of promoting their own efficiency, again recognising that some industries have large subsidies?

Status of the C & AG and his staff

11. This is a very interesting section on which I have these points:

- a. To whom, if anyone, does the C & AG report (paragraph 56)?
- b. I see the reference to "an obsolete conception of the Treasury role in the control of public spending" (paragraph 57). It would be helpful if the current conception were stated to help point out the distinction between what the Executive does for itself and what the EAD does on behalf of (presumably) Parliament.

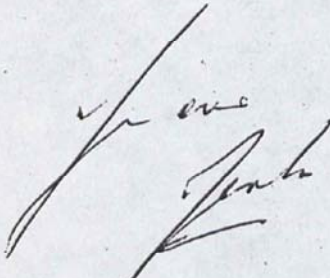
c. Who fills the post of/appoints the C & AG (paragraph 61)? My first impression is that who appoints and pays the C & AG must be assumed to have some hold over him, however tenuous, and I would not myself be all that strongly opposed to the idea of C & AG being a servant of Parliament. Are the Speaker and the Clerk of the House of Commons regarded as having insufficient independence because they are servants of the House?

d. I do not see why it would be undesirable for the C&AG to be directed by the House or a Select Committee to undertake enquiries (paragraph 62). Parliament might make mistakes - we all do - but I would think it an important strengthening of its capacity to look after the taxpayer's pound.

Annex A

12. I note in paragraph 3 the limitation on appropriation accounts with which we are all familiar. As you know, I am keen that Ministers should have an account of the value of assets in their keeping and that the Government should progressively move away from the restricted concept of an account of the flow of receipts and payments to that of an account of stock as well as flow.

13. I am copying this to the Prime Minister, the Chancellor of the Exchequer and the Chief Secretary.



DEREK RAYNER



10 DOWNING STREET

PRIME MINISTER

You have expressed some interest in the work of the Comptroller and Auditor General's Department, and you agreed that a consultation paper should be published.

You might like to glance at Sir Derek Rayner's comments below on the Green Paper.

17 March 1980

MAP

A large, stylized handwritten signature in dark ink, appearing to be 'M. P.' or similar, written over the date.



Gat Mach

H M Treasury

29

Parliament Street London SW1P 3AG

Switchboard 01-233 3000
Direct Dialling 01-233 5362

Sir, Anthony Rawlinson KCB
Second Permanent Secretary
Public Services

C A S S Gordon Esq
Clerk of the House of Commons
House of Commons
LONDON SW1A 0AA

17 March 1980

Dear Gordon

I am writing at the suggestion of the Chancellor of the Duchy of Lancaster to draw your attention to certain ideas discussed in the Government's recent Green Paper (Cmd 7845) about the role of the Comptroller and Auditor General. I enclose a copy.

Some of these ideas could have implications for the House authorities.

Part 4 refers to the possibility of control of staffing and grading of the Exchequer & Audit Department being transferred from the Civil Service Department to the House of Commons Commission. This idea was put forward in reports by the former Expenditure and Procedure Committees in the last Parliament.

As it states, the Green Paper is intended to provide the basis for discussion both with the relevant Parliamentary Committees and with other. The Government have not yet taken firm decisions on the matters raised in it. Any move in the direction of transferring control of the E & AD staffing matters to the House of Commons Commission would in any event almost certainly require legislation.

I should be happy to receive any observations you wish to make on this, and indeed on any part of the Green Paper; or to arrange a meeting if you would like that.

The Green Paper asks for comments by 31 July. Whether the Parliamentary Committees concerned will be ready to report by then remains to be seen. I would expect Ministers to want to return to the matter in the autumn.

I am sending a copy of this letter to the Clerk of the Parliaments, to the Comptroller & Auditor General; and to the Private Secretary to the Chancellor of the Duchy.

Yours sincerely
Anthony Rawlinson

ANTHONY RAWLINSON



Chancellor of the Duchy of Lancaster

cc: Mr Hyde
Mr Pattison (No 10)

Bob Mail
MAP
PRIVY COUNCIL OFFICE

WHITEHALL, LONDON SW1A 2AT

11 March 1980

Jean Alistair

GREEN PAPER ON THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

The Chancellor of the Duchy has seen with interest the draft Green Paper on the role of the Comptroller and Auditor General. He does not want to make any comments at this stage on the merits of the proposals discussed in Part IV of the Paper dealing with the status of the Comptroller and Auditor General and his staff. These proposals would, however, if implemented, have major implications for the House authorities, and the Chancellor of the Duchy hopes that it will be possible to give the Clerk of the House, as a matter of courtesy, some forewarning of the publication of the Green Paper containing these proposals.

Yours sincerely

Petra Laidlaw

MISS PETRA LAIDLAW
Private Secretary

A C Pirie Esq
Private Secretary to the Chief Secretary
HM Treasury
Whitehall



BF 14/3
Gort. Mad
MA

CABINET OFFICE

70 Whitehall, London SW1A 2AS Telephone 01-~~XXXX XXXX~~ 233-8224

10 March 1980

Sir Anthony Rawlinson KCB
HM Treasury
Parliament Street
London SW1

THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

Thank you for your letter of 22 February and for the enclosed draft Green Paper, which I found a most readable and interesting document. I should like to make the following comments, some on the text as a draft, some on the issues.

General

2. The draft says nothing about the numbers or professional training of EAD staff or about the coverage of their work, eg about how much time they spend on the basic, financial and regularity audit of departmental accounts, on examining the efficiency and economy with which funds are spent and on investigating the effectiveness of programmes and projects in meeting established policy goals. That leaves me with no real grasp of the nature of the instrument the paper is addressing - who the staff are, where they are or what they do. It is therefore hard to apply oneself authoritatively to the first question raised in paragraph 5, mainly "What kinds of audit should the C & AG undertake?".

3. My second point follows on: what are the effects of traditional EAD audit and the extension "in appropriate cases into effectiveness audit" (paragraph 11)? I am feeling for the kind of results produced, both for Parliament and the public service, of conventional and newer audit in terms of the practices and behaviours of institutions on the one hand and of actual benefits in particular cases on the other. For example, are Ministers satisfied that the C & AG's audit function is producing institutional and particular results worth having? Are there practical examples one can quote in explanation of the "further extension of VFM audit" in paragraphs 11 and 16, for instance? And what view does the Treasury take, in the light of recent practice, for the correct balance of

effort as between basic, VFM and effectiveness audits (see paragraphs 18 and 20)?

4. A related point to which I attach great importance is the way in which the auditor presents himself and is perceived. In our business, I regard our auditors as allies, very much part of the team. It is a pity if the auditors in Government are regarded as unfriendly but if their skill lies only or mainly in playing a checking role they are bound to be seen so. To my mind it is a great waste of an important national asset if the EAD is always used by Parliament as a witness for the prosecution. Nor do I believe that Parliament can make sound judgements on the behaviour of the Executive if all the evidence it receives is of failure or rule-breaking. I would like to see EAD bringing examples of good management as well as bad before Parliament. This would help produce a much needed change in the climate of opinion in Westminster and in Whitehall. But obviously this depends on EAD having staff who know good management when they see it.

5. Thirdly, I am struck by the draft's references to lack of or limitation on definition, as in paragraphs 12 and 20. I have some sympathy with the traditional British virtue of avoiding being explicit in defining powers and relationships, but I should think there would be substantial merit if the EAD Acts are to be revised in indicating with reasonable precision how the C & AG and his staff are expected to spend their time, and what skills they should develop. In the case of paragraphs 20 and 21, I do not see how the C & AG can do good work on the adequacy of departmental systems without also doing some independent work on the effectiveness and value of particular policy instruments, because systems have to be tested by reference to examples of the work they are supposed to control. Nor do I see, under existing arrangements for supporting Select Committees where they can look for independent, professional assessments of policy instruments unless to the C & AG.

6. I therefore applaud the idea (paragraph 24) that the C & AG's power to audit particular bodies should be provided for "by statute wherever practicable", provided of course that this does not exclude important classes of or particular institutions from examination.

Range of the C & AG's audit

7. While I take the point that Ministers' technical responsibility for public funds transferred to companies does not extend beyond making the payment provided for by Parliament (paragraph 30), I think it would be worth stating here how the taxpayer is assured that his tax pound has been properly and effectively spent. Similarly, at the end of paragraph 31, it would be helpful to establish who decides whether the C & AG's audit and inspection should be extended to a particular "public funded body".

Local authorities

8. I am aware of Mr Heseltine's interest in establishing an "Accounts Commission for Local Government" and of its relevance to what is said in paragraph 41 about strengthening DAS arrangements. But I find the contrast between paragraph 37 and the last sentence of paragraph 41 a bit too stark for comfort. I sympathise with the drift of paragraph 41, but I think that it would be worth a sentence or so more to explain the conundrum in accountability terms represented by:

- the constitutional autonomy of local authorities
- / the fact that they are nonetheless funded to a large extent by national taxation
- the restrictive nature of local government Ministers' accountability to Parliament for the money spent through RSG
- / the absence of any local authority accountability to Ministers or Parliament for that money
- the specific nature of Parliament's "legitimate interest" in respect of money voted by it to pay for RSG.

9. The text might also speculate briefly on what Parliament might do "while respecting the autonomy of individual local authorities". (You might like to know, by way, that the Director General of the GLC told us over lunch in the Members' splendid dining room at County Hall the other day that RSG should be regarded as general tax money, that it was not especially relevant that it came from Parliament rather than from local property taxes and that it was a misconception to suggest that there should be an accountability for it separate from that of Members to their local electorate. I have always regarded this as a very odd idea.)

Nationalised industries

10. Does paragraph 50 mean that the Government is satisfied that nationalised industries are efficient and have appropriate means of promoting their own efficiency, again recognising that some industries have large subsidies?

Status of the C & AG and his staff

11. This is a very interesting section on which I have these points:
- a. To whom, if anyone, does the C & AG report (paragraph 56)?
 - b. I see the reference to "an obsolete conception of the Treasury role in the control of public spending" (paragraph 57). It would be helpful if the current conception were stated to help point out the distinction between what the Executive does for itself and what the EAD does on behalf of (presumably) Parliament.

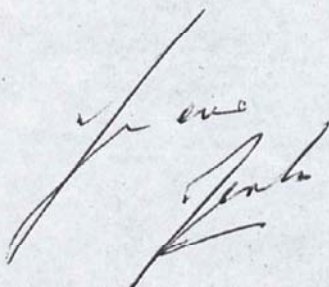
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d. I do not see why it would be undesirable for the C&AG to be directed by the House or a Select Committee to undertake enquiries (paragraph 62). Parliament might make mistakes - we all do - but I would think it an important strengthening of its capacity to look after the taxpayer's pound.

Annex A

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13. I am copying this to the Prime Minister, the Chancellor of the Exchequer and the Chief Secretary.

A handwritten signature in dark ink, appearing to read 'Derek Rayner', written in a cursive style.

DEREK RAYNER



Secretary of State for Industry

V MAP

Govt Mach

DEPARTMENT OF INDUSTRY
ASHDOWN HOUSE
123 VICTORIA STREET
LONDON SW1E 6RB

TELEPHONE DIRECT LINE 01-212 3301
SWITCHBOARD 01-212 7676

3. March 1978

The Rt Hon John Biffen MP
Chief Secretary to the Treasury
HM Treasury
Parliament Street
London SW1

John Biffen

Thank you for sending me a copy of your minute of 21 February seeking the Prime Minister's agreement to publishing the proposed Green Paper on the role of the C & AG.

I confirm that my views on the handling of the question of providing for C & AG access to the books of the National Enterprise Board are as described in paragraph 8 of your minute. I should be content for the text you enclosed to be published as a Green Paper, subject to a minor change in the wording of paragraph 52 which I understand has been agreed between our officials.

I am sending copies of this letter to the Prime Minister and the other recipients of your minute.

Eric Lewis

Govt Macd
MAS

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MINISTRY OF DEFENCE WHITEHALL LONDON SW1A 2HB

MO 21/8/5

3rd March 1980

Dear John,

GREEN PAPER ON C&AG's ROLE

Thank you for your minute of 21st February 1980 circulating the draft Green Paper. I am in agreement with your view that the paper be kept "deliberately green". The problems that could arise if the Controller and Auditor General were given too wide a statutory or discretionary remit, in particular on matters of policy, seem to me to call for a very cautious approach.

I am copying this letter to the recipients of yours.

Jasper

Francis

Francis Pym

The Rt Hon John Biffen MP

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DEPARTMENT OF THE ENVIRONMENT

2 MARSHAM STREET

LONDON SW1P 3EB

01-212 3434

MINISTER FOR LOCAL GOVERNMENT AND ENVIRONMENTAL SERVICES

28 February 1980

Dear John,

GREEN PAPER ON THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

In Michael Heseltine's absence from the office, I am responding to your minute of 21 February to the Prime Minister covering the draft Green Paper.

My interest relates primarily to the references to local authorities in paragraphs 37-41. I am content with paragraphs 37-40 and with the first 3 sentences of paragraph 41 which will provide a useful jumping-off point for whatever initiatives we decide to take on local authority audit and efficiency matters following the recent exchanges between colleagues. I am less happy however with the final sentence of paragraph 41 which appears to imply the possibility of developing a closer Parliamentary involvement in local authority affairs which I do not think would be appropriate. I would greatly prefer to see this sentence omitted.

I am copying this letter to the recipients of your minute to the Prime Minister.

Tom King

TOM KING

Rt Hon John Biffen MP

cc Cabinet
M/Trans
CO

HS

27 February 1980

The Prime Minister has seen the Chief Secretary's minute of 21 February, in which he seeks her approval to publish as a Green Paper a study of the role of the Comptroller and Auditor General.

The Prime Minister is content that the Chief Secretary should go ahead as he proposes.

I am sending copies of this letter to the Private Secretaries to other recipients of Mr. Biffen's minute.

M.A. PATTISON

A.C. Pirie, Esq.,
H.M. Treasury.

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PRIME MINISTER

1.



Mr Biffen seeks permission to publish this Green Paper on the role of the C & AG.

Agree now: or would you prefer to have this back at the week-end for a closer look?

MAD 26/2.

PRIME MINISTER

Mue

MT

GREEN PAPER ON THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL (C & AG)

This minute seeks your approval to publish as a Green Paper the attached study of the Role of the C & AG.

Background

2. In response to various recommendations from the Public Accounts Committee and the Expenditure and Procedure Committee, the previous Administration initiated a review of the E & AD Acts. In June 1979 we announced our intention to press forward with the review. The Green Paper is the result of the first phase. It has been prepared by a Steering Group of officials under the chairmanship of Sir Anthony Rawlinson, comprising representatives of the Treasury and CSD, selected Permanent Secretaries of the main spending departments, the Treasury Solicitor, the head of the Government Accountancy Service, and Sir Douglas Henley, the present C & AG.

Timing

3. I should like to arrange for early publication. There are signs of renewed Parliamentary and other interest in the subject, and Parliamentary answers have indicated that the Government are considering publication shortly. The next stage is discussion with the PAC and the Treasury and CSD Committee, and a public invitation to comment. The PAC have provisionally booked 17 March for a hearing on the subject; it could be allowed to slip but I should like to meet their date if possible. That would mean publication early in March.

Content and likely impact

4. The Green Paper discusses three main questions:-

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- a. What kinds of audit should the C & AG undertake?
- b. How far should his responsibilities extend?
- c. What should be his status in relation to Parliament and the Executive?

Some preliminary conclusions are listed at paragraph 64. But they are preliminary. The paper is deliberately green. Its main purpose is to focus wider discussion. Early publication will help to push that forward, and need not preclude further thoughts of our own later, for example which may be prompted by the further work of Sir Derek Rayner.

5. The Green Paper adopts a cautious and thoughtful approach to reform of the public audit system. I believe that is right, and that serious commentators will agree. There will doubtless be criticisms, eg from certain former members of the Expenditure and Procedure Committee such as Michael English and John Garrett, that the Green Paper does not advocate more radical changes. It is not clear however that their views on the subject have any wide support in the House. By publishing the Green Paper the Government will not be committed either way but can claim credit for enabling the debate to proceed.

Points of interest

6. The Green Paper deals in rather more detail with some accountability issues touched on in Sir Leo Pliatzky's Report on Non-Departmental public bodies (Cmnd 7797). The two documents are basically consistent. The Pliatzky Report talks in terms of the C & AG's audit role. The rather fuller analysis in the Green Paper distinguishes between audit and inspection. There is no inconsistency in substance.

7. The section on local authorities has been drafted so as to allow for a subsequent initiative on audit should this be decided upon. This would cover both Michael Heseltine's proposal for an Accounts Commission and your own intention that Sir Derek Rayner should consider local authority efficiency.

8. The section on the National Enterprise Board comes to no firm conclusion on the question of providing for C & AG access to the Board's books. The previous PAC pressed for this and we understand

that the present Committee takes a similar line. In Opposition we supported the PAC. In due course we may settle the matter in their favour. However, in my judgment and, I understand, in that of Keith Joseph, now is not the time, nor is a Green Paper the right context, in which to take and announce this decision. There are some signs that the new Board may like their predecessors be hostile to the C & AG having access. The chances of an amicable solution are likely to be no worse, and possibly better, if we do not try to resolve the question now.

Procedure

9. It may be necessary to make one or two minor changes in this text, eg to meet any last minute comments by the C & AG. Subject to that, I should be glad to have your agreement to early publication, with the aim of enabling the PAC to hold their first hearing as they wish on 17 March.

10. I am copying this minute and the draft Green Paper to other members of the Cabinet and to the Minister of Transport; and to Sir Robert Armstrong.

W. J. B.

JOHN BIFFEN

21 February 1980

DRAFT GREEN PAPER (Version of 20.2.80)

THE ROLE OF THE COMPTROLLER AND AUDITOR GENERAL

I INTRODUCTION

1. This Green Paper represents the first stage of the Government's review of the Exchequer and Audit Departments Acts. The Government announced on 25 June 1979¹ that they would press forward with this review which had been begun by the previous Administration.

2. The Exchequer and Audit Departments Acts 1866 to 1957 (E & AD Acts), together with provisions in other Acts about the audit of various bodies, provide the statutory basis for the work of the Comptroller and Auditor General (C & AG) and his Department, the Exchequer and Audit Department (E & AD). The main provisions of these Acts relevant to audit remain generally valid, but it is difficult nowadays to relate them and their underlying assumptions directly to the way in which Government manages and accounts for public spending or to the work of a modern national audit office. If it were decided that no fundamental changes were necessary, the need for new legislation would not be pressing, but some of the provisions are outdated and there would be merit in revising the Acts to express their operative provisions in language better related to modern conditions.

3. The E & AD Acts also deal with other aspects of the management of the Government's finances apart from audit. If the audit provisions in the Acts are being revised, it would be convenient to take the opportunity to revise such other provisions as are now out of date and to consolidate other related legislation.

4. The main reason for the current review however is the belief that the time is ripe to look systematically at our public audit arrangements, which have evolved largely piecemeal over the years. The need for such a review was one of the themes of observations and recommendations put forward in the previous Parliament by the Select Committees on Expenditure, Procedure and Public Accounts concerning the C & AG's role and functions².

¹ O.R. Vol 969 Col 37

² Eleventh Report from the Expenditure Committee, Session 1976-77 (HC 535), paras 153-158 and 160; First Report from the Select Committee on Procedure, Session 1977-78 (HC 588), paras 8.7-8.21 and 6.44; Second Special Report from the Committee of Public Accounts, Session 1978-79 (HC 330)

5. The main questions discussed in this Green Paper are:

- (a) What kinds of audit should the C & AG undertake?
- (b) How far should his responsibilities extend?
- (c) What should be his status in relation to Parliament and the Executive?

6. The Government intend to discuss the Green Paper with the relevant Parliamentary Committees. They would also be glad to receive comments from interested institutions, organisations and individuals. Any such comments should be addressed to the Second Permanent Secretary (Public Services), HM Treasury, Parliament Street, London SW1P 3AG, not later than.....

7. The Government wish to acknowledge the assistance provided by the present C & AG, Sir Douglas Henley KCB, and his Department, in the production of this Green Paper. He will no doubt take part in the planned discussions with the Parliamentary Committees and others.

II THE NATURE OF THE C & AG'S AUDIT

8. As the Government's external auditor the C & AG is a key figure in our system of public audit. His role needs to be viewed in the context of the general framework of Parliamentary accountability, which is based on the principle that Parliament grants supply to the Crown and holds the Ministers of Her Majesty's Administration accountable for the use made of it.

9. The ultimate accountability of Ministers to Parliament on the floor of the House is supplemented by the work of the Public Accounts Committee (PAC). From the earliest days the PAC has based its examination of Government spending and of Departmental administration on the reports of the C & AG. Under the terms of the E & AD Act 1921 the C & AG carries out his audit on behalf of the House of Commons as a whole, and not for the PAC, but in practice he works in close association with that Committee. The Government consider that this effective working relationship between the C & AG and the PAC should be preserved.

10. As currently pursued the C & AG's work covers a spectrum of activities of which the main elements can be summarised as follows:-

Financial and Regularity Audit

- a. a financial audit to ensure that systems of accounting and financial control are efficient and operating properly and that financial transactions have been correctly authorised and accounted for.
- b. a regularity audit which verifies that expenditure has been incurred on approved services and in accordance with statutory and other regulations and authorities governing them.

Value for Money Audit

- c. an examination of economy and efficiency, to bring to light examples of wasteful, extravagant or unrewarding expenditure, failure to maximise receipts or financial arrangements detrimental to the Exchequer, and weaknesses leading to them.

Effectiveness Audit

- d. an examination to assess whether programmes or projects undertaken to meet established policy goals or objectives have met those aims.

In his work the C & AG takes into account the arrangements for internal audit made by Government Departments and other bodies with whose affairs he is concerned.

11. It was with the support and encouragement of the PAC that, before the end of the last century, the C & AG began to extend his examination of the financial activities of Government beyond financial and regularity audit into the economy and efficiency of the management of public funds, ie into questions of value for money (VFM). More recent is the further extension of VFM audit in appropriate cases into effectiveness audit.

12. The distinction between financial and regularity audit on the one hand and VFM and effectiveness audit on the other is not precise. It does however mark the divide between statutory and non-statutory aspects of the C & AG's audit. Financial and regularity audit are covered, in the case of Appropriation Accounts of Government Departments, by the requirement in the E & AD Acts that the C & AG should certify and report on such accounts. Neither the 1866 nor the 1921 E & AD Acts specifically provide for him to examine broader questions of efficiency and economy or of effectiveness, but since they do not provide any detailed guidance on the scope of the audit, it has been possible for changes to take place without the need for amending legislation.

Financial and Regularity Audit

13. The Government believe that an efficient and thorough financial and regularity audit of Government Departments must remain the foundation of the C & AG's work as a whole. That the accounts of Government Departments should be audited externally is an essential public safeguard. This is the primary function of the C & AG. The Government see merit in the PAC investigating, on the basis of audit reports by the C & AG, deficiencies in accounting systems or financial controls. This is a valuable discipline bringing benefits wider and deeper than the immediate results of individual investigations.

14. In modern conditions the most cost-effective means of carrying out the audit task is likely to be a systems-based approach, ie an approach based on evaluation of key internal control systems, supported by substantive tests of selected items of information in the accounts and records. Such techniques are widely used in modern auditing and the recent E & AD management review (the report of the Steering Committee was printed as a appendix to the PAC's Second Special Report, Session 1978-79) referred to the benefits to be derived from greater use by the C & AG of systems-based methods. A financial and regularity audit of Departments which emphasises examination of systems may be expected to contribute to improving Departmental management by helping to identify weaknesses in financial control which can then be corrected.

15. There should still be a formal statutory requirement on the C & AG to provide an annual report or certificate covering the audit of all accounts for which he is responsible. In the course of the present review however the C & AG has represented that there may be a case in relation to Departmental Appropriation Accounts for reconsidering the definition of his formal audit responsibilities, and the nature of the corresponding certificate or report in the light of modern conditions and Parliamentary requirements. A note by the C & AG on this aspect of his work is at Annex A. The Government would be glad to have comments from the relevant Parliamentary Committees and from the accountancy profession on the issues raised.

Value for Money Audit

16. Under the broad designation of value for money audit, economy and efficiency examinations have for many years been a feature of the C & AG's work, as they have more recently of the work of public auditors in many other countries. This emphasis is reflected in his annual reports to Parliament, which have covered the efficiency of the management of all major Government services - eg defence, health, education, social security, agricultural and industrial support, etc - as well as that of many smaller ones. The work of the PAC has also largely concentrated on such questions in recent years.

17. Examinations of this type need not in practice be closely related to the financial audit of annual accounts. They are not concerned solely with aspects of financial management but also with a scrutiny of project management, contract procedures, the use of manpower, and so on. In the private sector it is the exception rather than the rule for statutory audit examinations to deal with questions of efficiency. The purpose of public audit, on the other hand, is to monitor the efficiency as well as the integrity of government in the management and spending of public money.

18. The Government believe that any new statutory framework for the C & AG's operations should provide for his continuing examination of value for money in the expenditure of public funds and for him to report to Parliament as appropriate on the results of his examinations in this field.

Effectiveness Audit

19. Such a provision could also in principle cover the development of the C & AG's effectiveness audit where this is a natural and sensible development of his other work. For example, it may be useful for the C & AG to explore how far a particular policy instrument is achieving the results which were intended and whether these results can be justified in relation to the manpower or other costs involved.

20. It is an open question how far the statutory provisions should define the scope of this type of activity by the C & AG. It might be possible to express any statutory provisions in broad terms, so as to leave the C & AG with some degree of discretion as to the development of his work in this area. In the exercise of that discretion or by virtue of the statute, the C & AG's work in this field might concentrate primarily on whether Departments have themselves established satisfactory procedures for measuring and reporting the effectiveness of their policies and for taking remedial action where necessary. In any event, the development of the C & AG's work should take into account how far in particular cases the C & AG's examination is likely to lead to worthwhile results.

21. The C & AG should not get involved in debate about the merits of particular policy objectives, as distinct from the efficiency or cost-effectiveness of measures designed to pursue them. Such an extension of his activities would take the C & AG a long way from his traditional role of conducting an audit-based examination of ways in which money has been spent, and could take him into fields primarily the concern of Select Committees other than the PAC. It would put at risk the traditionally non-partisan character of examination by the PAC of matters raised in the C & AG's reports. Such a move could compromise the independence of the C & AG and pose a threat to the smooth working of the arrangements for his access to Departmental files.

III THE RANGE OF THE C & AG's AUDIT

22. The C & AG is at present responsible as designated auditor for the annual examination and certification of some 450 accounts involving net annual expenditure in excess of £50,000 million. In addition to the Appropriation Accounts, store accounts and trading funds and accounts of all Government Departments, these include the accounts of a wide range of statutory boards and authorities as well as of certain international bodies and UN agencies (whose audit is conducted on a fee basis). The C & AG examines and reports to Parliament on Inland Revenue, Customs and Excise and other revenue accounts. Without being designated auditor he has been granted access to inspect the books of more than 500 bodies of widely varying types which depend to a greater or lesser extent on finance from public funds. This enables him to report to Parliament in such cases where it might not be appropriate or necessary for him to be appointed auditor³. The C & AG's responsibilities do not however extend, within the public sector, to local authorities and nationalised industries, or, within the private sector, to numerous companies and other businesses and organisations in receipt of voted moneys.

23. Questions have been raised, particularly by Select Committee reports over the past two years, about the appropriate extent of the C & AG's remit. Both the Expenditure Committee and the Procedure Committee of the last Parliament recommended that the C & AG should be empowered to examine the accounts of all bodies in receipt of public funds or, more specifically, voted moneys. The Procedure Committee added the proviso that the C & AG should be empowered to authorise "alternative audit procedures in respect of individual bodies to whose accounts he has rights of access".

24. The Government share the Select Committee's concern that the provision of public funds should always be accompanied by careful consideration of the arrangements for audit and accountability. This was a theme in the recent Report to the Prime Minister on Non-Departmental Public Bodies⁴. The Government do not believe that it should be for the C & AG himself to determine what accounts he should audit in detail, as the Procedure Committee proposed. It should be laid down by statute wherever practicable, as for example where the body is itself established by statute.

³Details of bodies of which the C & AG is the appointed auditor or over whose books and records he has rights of inspection are given at Annex B.

⁴Cmnd 7797.

25. The broad principle underlying existing practice is that where a major source of an organisation's income is voted money the C & AG should be appointed its formal auditor or be granted a right of access to inspect its books and records. In the Government's view this general principle provides a useful starting-point for the decisions which Parliament and the Government are from time to time required to take about the audit and accountability of non-departmental bodies. The Government also accept the suggestion made in Cmnd 7797 that no distinction should be made in this connection between bodies directly financed from public funds and bodies which while not of a commercial character or subject to the pressures of competition are able to use their Government-backed status to raise money, eg by levy or loan.

26. Another sound principle in this context is that if the C & AG is to be required to examine the affairs of a body this ought to reflect a degree of Ministerial responsibility to Parliament for that body extending beyond a responsibility simply for the payment of money from voted funds. Otherwise Parliament would have no reliable means of securing any action to implement any conclusions or recommendations formulated by the PAC.

27. This principle has two other implications. First, it implies that in relation to bodies for which Ministers are not directly responsible an important objective of the C & AG's examination must be to review the effectiveness of the arrangements under which Ministers monitor and control the payment of public funds to them and not to restrict itself to the financial transactions of the bodies in isolation. Even where bodies remain outside the C & AG's audit or inspection remit, the way in which Departments exercise controls over them can still be a worthwhile field for his examination and report. The C & AG's audit of Departments already covers such matters.

28. Secondly, by emphasising the responsibility of Ministers it suggests that where it is decided that the C & AG should examine the affairs of bodies of this sort it will often be possible to satisfy the requirements of Parliamentary accountability in future by giving the C & AG the right and duty of inspection rather than formal audit responsibility. Where the C & AG is at present the auditor, consideration could be given to making other arrangements for the exercise of the formal audit responsibility, so long as he retains inspection rights. If other arrangements for audit can be made which are satisfactory and economical, there is a case for doing so in order to avoid overloading the resources of the E & AD.

29. It has been proved by experience to be of valuable assistance to the PAC if without being appointed the auditor the C & AG is given rights of inspection. To use this technique more widely need not imply any relaxation in the customary rigour of the Committee's or the

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C & AG's scrutiny. Representatives of bodies under examination could still be summoned to attend meetings of the PAC. Their evidence would however not be limited to the way in which the body had itself conducted its financial activities but would also shed light on the sponsoring Department's own scrutiny of the body's expenditure and systems of financial control. It might also on occasion help to show whether any change is needed in the exercise of Ministerial responsibility for the relevant functions.

30. In most cases the principle of Ministerial responsibility will point to the same conclusion as the approach described in paragraph 25 above. It is implicit to a large extent in cases where the C & AG is already the designated auditor or has inspection rights. For example, the C & AG is the designated auditor of the Research Councils, each of which is responsible in its field for promoting activity on behalf of - if at arms' length from - its sponsoring Department. On the other hand, it would be no more appropriate than cost-effective to require the C & AG to examine the accounts of companies qualifying under general schemes of Government support, eg under the Industry Acts. In such cases Ministers' responsibility for public funds does not extend beyond making the payment as provided for by Parliament. Similarly, the C & AG cannot generally exercise, or effectively be given by the Government, rights of access to the books of countries in receipt of UK aid or of international organisations to which the UK contributes. (The C & AG is the appointed auditor of certain UN Special Agencies, but that has come about as a result of an invitation from the bodies themselves. In these audits the C & AG's responsibility is to the Governing Bodies concerned, to whom he reports.)

31. While it is possible to point to some criteria of general relevance to the range of the C & AG's responsibilities, a definition of these should permit sensible flexibility, to take account of the wide variety of financial transactions involving payment and receipt of public money. They include, for example, social security benefits, payments - sometimes contractual - for purchases of goods and services, professional fees, award schemes, general or particular schemes of industrial support, overseas aid. There are also differences, as was noted in Part II, in the sorts of audit examination undertaken by the C & AG and corresponding differences in the reports which he makes to Parliament. There is a great variety in the status, organisation and functions of bodies which receive public funds. The taxpayer has a stronger and more direct interest in the activities of an agency which is engaged in administering Government policy and is fully Government funded than in, say, a voluntary body receiving some financial support from the Government among other sources. Decisions whether to provide for C & AG audit or inspection of publicly funded bodies will always need to have regard to the circumstances of each case, bringing in such considerations as the need to preserve commercial freedom of action, local democratic accountability, and the circumstances and objectives of each institution.

32. There may be cases where decisions have been taken in the past to involve or exclude the C & AG without reference to the general considerations discussed in the preceding paragraphs. These could if necessary be looked at again, although the Government doubt whether any major changes are required. In some cases alternative and workable arrangements already exist to ensure that Parliament can scrutinise the bodies in question, and these arrangements have recently been reinforced by the setting up of the new Departmental Committees. Some further justification, going beyond a desire for uniformity, would be needed to warrant the involvement of the C & AG. Conversely, where, eg for the universities, arrangements already exist, and are justified on practical grounds, for the C & AG to audit or inspect the accounts of bodies for whose activities Ministers are not responsible, they should not be terminated on this account.

33. In the light of the preceding analysis, the remaining paragraphs of this section consider the audit arrangements for the National Health Service, local authorities, the nationalised industries, the British National Oil Corporation (BNOC) and the National Enterprise Board (NEB). These are all important examples of publicly financed bodies within the public sector, and some of them have been the focus of Select Committee recommendations about possible changes in the C & AG's remit.

National Health Service

34. One important area of public expenditure under the control of non-departmental bodies in which the C & AG is rightly involved is the National Health Service. Under present arrangements the Health Departments allocate funds to their top tier Health Authorities individually, who in turn sub-allocate down the line. Each authority is responsible for its internal audit and for applying its funds in the light of Departmental guidance in the way it considers most suitable to its local needs. Its accounts are independently audited by specialist Departmental staff who are appointed by the Secretaries of State as the "statutory auditors" under the NHS Acts.

35. The NHS Acts also require - reflecting the overall responsibility of the Secretaries of State for the Service - that the C & AG should examine, certify and report on the annual summarised accounts of this expenditure and permit him to examine the accounts and records of the health authorities and the reports of the auditors on them. In addition, the C & AG examines and certifies the Departmental appropriation accounts to which all current and capital expenditure is finally charged. He has complete freedom to pursue his enquiries at all NHS locations; but having regard to the work of the statutory auditors and of the internal audit of the health authorities, he mainly examines the effectiveness of procedures for financial control and for efficiency in the use of resources.

36. These arrangements involve some possibility of overlap of audit activity between the statutory audit and the E & AD. But the audit organisation reporting directly to them is an essential support to the Permanent Heads of the Health Departments in fulfilling their responsibilities as accounting officers for all expenditure borne on NHS Votes for a highly decentralised service. In carrying out his functions the C & AG has responsibilities similar to those of a primary auditor of group accounts; he is entitled to take account of the work and the reports of the statutory auditors in deciding what further work he needs to undertake in order to satisfy himself that, with the inclusion of figures which he himself has not audited, he can give his opinion that the accounts are correct. Provided that the provisions of the NHS Acts in regard to accounts and audit continue to be interpreted in this way, there will be no need to change the arrangements.

Local Authorities

37. Local authorities are autonomous bodies answerable to their own electors and not to Parliament or to Ministers. Central government grants overall now provide more than 50% of local authority funds. The bulk of this is rate support grant which is provided primarily to supplement local sources of income and there is no Ministerial responsibility for how it is spent.

38. In England and Wales present legislation gives local authorities the choice between commercial and District audit and most have opted for the latter. District Auditors, in their professional capacity, are independent of the Government and their duties are imposed on them by Parliament but discharged by reporting to local authorities. Different arrangements apply in Scotland where the audit of local authorities is supervised by the Commission for Local Authority Accounts in Scotland, which is responsible for appointing auditors either from its own staff or, in most cases, from private practice.

39. One disadvantage with the arrangements in England and Wales is that it is difficult to focus on issues of efficiency affecting the whole range of local authorities. The Layfield Committee⁵ recognised that the primary responsibility for ensuring value for money rested within local government but drew attention to the need for comparative studies of this type, and the previous Administration in March 1979 set up the Advisory Committee on Local Government Audit with a specific responsibility for considering general audit and value for money enquiries.

⁵Report of the Committee of Enquiry under Frank Layfield QC on Local Government Finance Cmnd 6453.

40. Independently of those developments the C & AG suggested, in his observations on the Eleventh Report of the former Expenditure Committee, Session 1976-77, that an amalgamation of the District Audit with the Exchequer and Audit Department under the C & AG would have certain advantages. This proposal was welcomed by the 1977-78 Procedure Committee, and the previous PAC saw some merit in it but thought some further evidence from those concerned would be desirable before they could reach a firm conclusion. Among its operational advantages a combined public audit service should promote the pooling and development of techniques and training, enhance the authority of the service as a whole and provide more varied career prospects. Pooling experience and combining in the development of value for money auditing would be particularly valuable. At the same time it would enable Parliament more easily to pursue its interest in the economy of services administered by local authorities.

41. The difficulty with this sort of proposal, with the implication of a closer relationship between local authorities and Parliament, is how to reconcile it with the existing constitutional arrangements and to avoid confusing the division of responsibilities. The Government accept the importance of maintaining and further developing an effective local authority audit and of promoting efficiency across the whole range of local authorities. In the light of experience of the Advisory Committee's first twelve months of operations they plan to consider what scope, if any, there is for strengthening existing arrangements in order to increase the impact of the work of District Audit among local authorities. They would also be ready to consider with the relevant Parliamentary Committees any suggestions which, while respecting the autonomy of individual local authorities, might enable Parliament, eg through its new Departmental Committees, to pursue matters of legitimate interest to itself relating to services administered by local government.

Nationalised Industries

42. The nationalised industries constitute a major sector of the national economy, and some of them are monopolies. The efficiency with which they conduct their operations is of great importance, as is their ability to demonstrate - not least to the consumer - the value of the services they provide.

43. The nationalised industries' statutes provide for their accounts to be audited by commercial auditors appointed by the Secretary of State. The scope of their audit, like the audit of a private company, is designed to ensure that the accounts provide "a true and fair view" and is not concerned with questions of efficiency.

44. To fill this gap the Government have recently proposed in the Competition Bill currently before Parliament that the Monopolies and Mergers Commission (MMC) be given a role in

examining and reporting on the efficiency of bodies such as the nationalised industries. The Commission's reports will help Ministers and Parliament to identify aspects of the industries' operations where improvements are needed and to press for specific action to achieve these improvements.

45. In the context of this Review the question arises whether this arrangement should be supplemented by a provision for the C & AG to have access to the books and records of the industries in order to make reports of his own on these and other matters. Such a development would be in accordance with practice in some other countries where, as was noted in evidence submitted to the Procedure Committee⁶, the national audit machinery has been developed to incorporate audit functions in relation to their nationalised industries. The French Cour des Comptes, for example, in addition to its responsibility for the financial audit has a wider responsibility covering the performance of public enterprises.

46. In the United Kingdom the statutory duties for which nationalised industries are accountable to Ministers and through them to Parliament are of a limited and general nature. Successive Governments have affirmed that within a broad framework laid down by government, which includes the establishment of medium term financial targets, the industries should act commercially and their day-to-day running should be a matter for their management, not for government.

47. Parliament's interest in the nationalised industries' accounts has been exercised not through the PAC but through the Select Committee on Nationalised Industries (SCNI), which held periodic hearings with Chairmen on a range of matters concerning the industries. This has now been superseded by the new system of committees set up to scrutinise the activities of the major Departments and their associated public bodies; the relevant committees may establish a joint sub-committee specifically to consider the affairs of the nationalised industries.

48. Ministers have a responsibility to keep under scrutiny the general performance of the industries, and in particular developments which require or could in future generate a claim on voted moneys. In the course of his normal examination of Departments the C & AG may be expected to look at the arrangements made for this purpose.

49. It would however be a major new departure for the C & AG to engage directly in an examination of the industries' efficiency. Unlike the MMC, which will mount its studies as and when the Secretary of State for Trade requests it to do so, the C & AG would have permanent access to the books and accounts of the industries. Although the C & AG has acquired

⁶by Dr E L Normanton (First Report of the Procedure Committee, Session 1977-78 Volume III p 137).

considerable experience over the years of efficiency audit in the public services, he has not hitherto been involved in a major sector of the market economy. An extension of his role to cover the nationalised industries would be seen by them as a serious threat to their own commercial freedom of action, and would probably necessitate greater involvement by Government Departments in their day to day affairs.

50. In the Government's view the proper division of responsibilities between Ministers and the industries, which is vital to their efficient operation, is appropriately underpinned by existing arrangements for the industries' audit and accountability, to which the work of the MMC will contribute. The Government are not persuaded that it would contribute to the efficiency of the industries for the C & AG to be involved as well.

British National Oil Corporation and National Enterprise Board

51. The PAC recommended in the previous Parliament that the C & AG be granted rights of access to the books and records of BNOC. The Government are at present considering the future structure of the Corporation's activities. A final view about the appropriateness of providing for C & AG access should be reserved until conclusions are reached, but the Government at present incline to the view that the C & AG should not be granted access. Relevant to this view is the decision announced by the Secretary of State for Energy on 26 July 1979 that BNOC should no longer have privileged access to (interest free) Government funds from the National Oil Account, and the intention, announced by the Secretary of State on 14 September 1979, to consider schemes for the introduction of private capital into BNOC's North Sea operations.

52. The PAC also recommended that the C & AG should be given access to the books of the NEB. There are arguments both for and against this. In some respects the NEB resembles the generality of nationalised industries. The changes recently announced in the NEB's role will result in the reduction of its activities, but in essence these will remain the same. In carrying out its investment programme on behalf of the Government it will still be important that the NEB should employ its commercial judgement and not feel itself subject to any process of second-guessing of its decisions.

53. On the other hand, the NEB is not an 'industry': it is not a supplier of goods or services to the public, and in practice operates mainly through a range of companies which are in a commercial and competitive environment and subject to the Companies Acts rather than to specific nationalisation statutes. Because of these differences and the extent of the NEB's dependence on financing from public funds, the Board was outside the terms of reference of

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the former Select Committee on Nationalised Industries; Parliamentary oversight of its operations was undertaken by the PAC.

54. The PAC suggested that access by the C & AG is essential to enable the Committee to carry out this responsibility effectively, and pointed to the fact that the Scottish and Welsh Development Agencies, which have investment functions similar to those of the NEB, are subject to examination by the C & AG by virtue of his appointment as their auditor. This appointment was made largely in consequence of the Agencies' assumption of industrial estate and environmental improvement activities which were certain to make substantial and continuing demands on public funds and for which audit by the C & AG was appropriate. His audit however covers all the Agencies' activities.

55. The Government will consider the question in the light of comments on this Green Paper.

IV STATUS OF THE C & AG AND HIS STAFF

56. The C & AG is an office holder under the Crown, subject to removal only on an address from the two Houses of Parliament. Like members of the judiciary, he is not subject to control either by Parliament or by the Executive in the exercise of his functions. His main duties under the E & AD Acts are undertaken "on behalf of the House of Commons". He is not however a servant of the House, although he has frequently been referred to in those terms.

57. The suggestion was made in 1977 by the Expenditure Committee, and subsequently by the Procedure Committee, that certain powers of direction available to the Treasury under the E & AD Acts are inconsistent with the claim that the C & AG is fully independent of the Executive. The suggestion related principally to the power under Section 3 of the 1921 Act to direct the C & AG to undertake the audit of particular accounts. This power is hardly ever exercised nowadays, and then only in relation to relatively unimportant accounts. It is never exercised in a way which has any material effect on the C & AG's independence. Like some other powers in the Acts it is a relic of an obsolete conception of the Treasury's role in the control of public spending. Such provisions are now inappropriate and should be recast or removed in any new legislation.

58. The Expenditure Committee and the Procedure Committee also drew attention to the provisions of the E & AD Acts which give the Civil Service Department control over E & AD staff numbers and gradings. The Committees considered this an unacceptable degree of Executive influence over the C & AG's work. They recommended that the staff of E & AD should become or be regarded as servants of the House, with the Department's costs borne on

the Vote of the House, and that the House of Commons Commission should assume responsibility for their numbers and grading.

59. The Government have no wish to maintain CSD control for its own sake, but they believe that there should be some external oversight of the C & AG's budget and the staffing costs of the E & AD. Present arrangements take advantage of the wide relevant expertise of the CSD, and if the responsibility were exercised unreasonably, the C & AG, being independent, could report the matter to Parliament. The Government would be ready to consider some form of control by the House of Commons Commission as an alternative. Any changes would need to be discussed with the Staff Side of E & AD, particularly if they would result in the staff ceasing to be members of the Home Civil Service and could reduce opportunities for exchanges with other Departments.

60. As for the C & AG himself, the Government consider that independence in the exercise of his responsibilities, and in deciding on the disposition of his staff resources and on audit priorities, is of fundamental importance to a national auditor. The nature and balance of his work under the statutes should not be subject to direction from any quarter. The PAC of Session 1978-79 also considered that the C & AG's independence was essential to the function of his office as the Government auditor, and that there should be no external constraint on his right to determine the direction and application of his audit resources.

61. The Government believe that the C & AG's independence will best be safeguarded if he remains an office holder under the Crown and is not and does not become regarded as a servant of the House. However, as was proposed by the previous Administration,⁷ there should be consultations with the Chairman of the PAC when the post of C & AG is to be filled in the future.

62. The Expenditure and Procedure Committees suggested that the C & AG should undertake enquiries if requested to do so by the House of Commons or any of its Select Committees. Any such power to direct the C & AG would entail an undesirable limitation of his independence, even if the request did not prescribe the manner in which the enquiry should be conducted. It would also imply an extension of his functions beyond that of the audit-based enquiries which are appropriately considered by the PAC.

⁷ Cmnd 7117 paras 100-102.

63. Special occasions may arise, as they have in the past, when one or two staff have been loaned from E & AD to assist other Select Committees. The C & AG has already made it clear that while serving in that capacity the loaned staff do not act as auditors, are not responsible to him and do not have rights of access to Departmental books and papers. In general, however, the Government agree with the PAC that the importance of the tasks facing the C & AG, and inevitable staff constraints, would not permit E & AD to become the main provider of staff support for Parliamentary Committees in their examination of Government business.

V CONCLUSIONS

64. The Government would welcome any views that the Parliamentary Committees and other interested bodies and individuals may wish to express on the issues discussed in this paper. The Government's provisional views can be summarised as follows:-

- a. The role of the C & AG should be
 - i. to provide a basic financial and regularity audit of Departmental accounts (paras 13-15);
 - ii. to undertake an examination of the economy and efficiency with which public funds are spent (paras 16-18), and
 - iii. in appropriate cases, to investigate the effectiveness of programmes and projects in meeting established policy goals (paras 19-21).
- b. The effective working relationship between the C & AG and the PAC should be preserved (para 9).
- c. In the case of non-departmental bodies an important objective of the C & AG's examination should be to review the effectiveness of the arrangements under which Ministers monitor and control the payment of public funds to such bodies (para 27).
- d. Decisions whether to provide for C & AG audit or inspection of such bodies need to be taken case by case (para 31). The C & AG should not cover the nationalised industries (paras 42-50).
- e. Certain powers of direction available to the Treasury in the E & AD Acts are obsolete and could be removed in any new legislation (para 57).

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- f. The Government are prepared to consider alternative arrangements for controlling the budget of the C & AG but the implications for the staff of E & AD would need to be considered (para 59).
- g. The independence of the C & AG of both the Executive and Parliament should be reaffirmed and there should be no change in his status as an office holder under the Crown (para 61).

65. In the light of comments received on these and other issues the Government will consider whether and in what form to bring forward proposals for new legislation. There is a case for a new Act to replace the existing legislation in order to provide an up-to-date and concise statement of the arrangements for public audit in this country. At the same time, as already indicated, the existing Acts remain for the most part technically valid and pose no insuperable problems of interpretation that require their early replacement. The Government believe that it would be right to replace the existing legislation only when there is a consensus on which a new and durable statutory statement of the role of the C & AG might be constructed.

THE C & AG'S CERTIFICATION AUDIT OF APPROPRIATION ACCOUNTS

Note by Sir Douglas Henley KCB, Comptroller and Auditor General

This note discusses the objectives of the C & AG's formal certification responsibility in respect of Departmental appropriation accounts and suggests how this part of E & AD's work should be discharged in modern conditions.

2. Under the E & AD Act 1866 all Government Departments are required to prepare annual "appropriation accounts" and the C & AG is required to examine, certify and report on them. The amending E & AD Act passed in 1921 requires him to satisfy himself that the money expended has been applied to the purpose or purposes for which the grants made by Parliament were intended to provide and that the expenditure conforms to the authority which governs it. The C & AG audits on behalf of the House of Commons but the 1921 Act, which repealed the requirements of the 1866 Act for him to carry out a detailed examination of all vouchers, left the nature and extent of his examination largely to his professional judgement, subject to the House being informed of any important changes therein. The 1921 Act also provided for the preparation and audit of trading, manufacturing, etc accounts.

3. Appropriation accounts are receipts and payments accounts which set out the sums which Parliament has appropriated for specified services in a financial year and what has been actually paid and received under those specified headings. They do not embody, as do commercial accounts, the concept of profit or loss and net worth, nor do they involve accounting on an accrual basis or the valuation of assets and liabilities. The C & AG's audit of appropriation accounts cannot therefore address itself to "a true and fair view" of profits or losses earned or of a Department's financial position; while central to the success of commercial operations these concepts are irrelevant to most Departmental activities. Their formal audit serves quite different objectives.

4. That part of the C & AG's audit which supports his certificate to appropriation accounts consists of a financial audit covering the general reliability of the accounts and a regularity audit to meet the specific requirements of the 1921 Act. These are designed to provide assurance that:

- (a) The figures in the appropriation accounts are accurate and that any Parliamentary or Treasury rules governing their form and content, including notes of losses, special payments, etc, have been followed.
- (b) Moneys voted by Parliament have been expended only for

the purposes set out in the Departmental Estimates and authorised by Parliament through Appropriation Acts; and that more has not been spent than the funds voted.

- (c) Departments have adhered to the statutory or other rules governing the administration of the services for which they are responsible, including such major programmes as social security benefits, and agricultural and industrial assistance schemes.

Broadly, (a) represents the financial audit and (b) and (c) constitute regularity audit.

5. In carrying out this work E & AD use some audit techniques which in principle are applicable both to commercial and to appropriation accounts: notably the systems based approach which focuses on the financial and accounting controls designed to guard against accounting errors and irregular use of public money, losses of cash or stores and, in the extreme case, fraud. Attention has been, and will continue to be, devoted to improving these techniques, and to applying them to the increasingly important areas of computerised processing of, and accounting for, financial and stores transactions.

6. It should however be noted that the discharge of the C & AG's certification responsibilities is directed solely to the formal accuracy and regularity of Departmental expenditures and receipts in relation to Parliamentary authorisations and other rules; and to give Parliament itself some independent assurance in these respects was a main objective of the founding Act of 1866. For the purpose of certifying the accounts it is not necessary for the C & AG to examine other aspects of Departments' financial management, relating for example to the adequacy of their budgeting and project controls, the management information they produce, and whether they obtain value for money in using the funds and resources at their disposal. Good administration in such financial management is central to efficient and effective public expenditure. It is therefore important that the C & AG's audit should concentrate on these areas as well. The conceptual distinction between the audit examination required solely to enable the C & AG to certify the formal accounts and that directed to these other aspects of financial control or efficiency is important because it underlines the need for a proper distribution of E & AD's resources. But in practice the same examination may sometime serve more than one objective and there is no intention, or need, to change this.

7. Financial accuracy of appropriation accounts and formal regularity of expenditure remain important objectives. But Parliament, through the PAC, have increasingly concentrated their attention on the more substantive aspects of public audit. They may agree that the C & AG should employ the most cost-effective methods and devote no greater resources purely to certification audit work than he considers necessary in the exercise of his professional judgement.

8. Some of the considerations which are relevant to the exercise of his judgement are:

- (a) All Departments follow a common Vote accounting guide issued by the Treasury which has remained relatively unchanged over many years. Departments' operations under this guide have been continuously subject to E & AD audit.
- (b) Whilst there is a large number of Departmental sub-systems supporting the central accounting systems, these tend to be standardised and to follow central rules and guidance from the Treasury or Civil Service Department. In this area E & AD already adopt a cyclic approach to the audit.
- (c) Departments maintain extensive accounts staffs and internal audit organisations of their own, which seek to provide their Permanent Secretaries/Accounting Officers with an assurance that financial control systems are adequate and operating effectively.
- (d) Accounting Officers take personal responsibility, for which they must answer to the PAC, for the correctness and regularity of their Departments' accounts.

9. As stated above the E & AD Acts require the C & AG to certify the appropriation accounts. By long standing practice followed since 1866 and specifically endorsed by the PAC in 1922 he has generally certified each account individually, some 170 in all, as "in my opinion, correct". This is a more stringent form of words than is applied to any commercial style account, public or private; to the audit of local authorities; or to the audit of public accounts in most advanced countries. Though the PAC have accepted that the word "correct" should not be taken literally, a form of report or certificate for Appropriation and similar accounts may now be desirable which would be more appropriate to the degree of formal assurance which Parliament might reasonably expect the C & AG to provide in modern conditions, and which would reflect the consequential nature of this part

of his Department's audit examination.

10. In practical terms this analysis suggests that E & AD should continue to apply a professional audit examination of high standard to Departments' discharge of their formal Vote accounting responsibilities. The direction and extent of that examination in each Department should be the C & AG's responsibility, taking into account both the materiality and sensitiveness of particular accounts and the general factors in paragraph 8 above. A report by the C & AG, rather than a certificate, on the results of this part of the audit might be appropriate. Whether legislation should specify the wording of that report, or whether the form should be left for consideration by the Public Accounts Committee will need to be considered. But legislation should in any case provide in suitable terms for these responsibilities.

ACCOUNTS AUDITED OR INSPECTED BY THE C & AG

This Annex groups the accounts audited or inspected by the C & AG into four Parts as shown below.

PART I Accounts relating to the expenditure of public funds, grouped as follows:-

	Corresponding Supply Estimates Classes
Defence	I
Overseas	II
Agriculture, Fisheries, Food and Forestry	III
Trade, Industry, Energy and Employment	IV and V
Roads and Transport	VI
Housing and other Environmental Services	VII and VIII
Law, Order and Protective Services	IX
Education and Libraries, Science and Arts	X
Health, Personal Social Services and Social Security	XI and XII
Other Public and Common Services	XIII and XIV
Northern Ireland	XV
Rate Support Grant and Financial Services	XVII

Within each group the accounts are listed under five headings:

- (i) Appropriation Accounts The C & AG audits all Appropriation Accounts with the exception of that for the Exchequer and Audit Department, which is audited by the Auditor of the Civil List (the Treasury).
- (ii) Trading Accounts and Trading Funds The C & AG audits all Departmental Trading Accounts and Trading Funds.
- (iii) National Loans Fund Accounts Accounts prepared by Departments relating to issues from the National Loans Fund and audited by the C & AG.
- (iv) Other Accounts audited by the C & AG.¹ These are not necessarily laid before Parliament but relate to the receipt or payment of public funds.²
- (v) Inspection Rights In addition, the C & AG has acquired non-statutory rights of access to the books and records of a wide variety of organisations of which he is not the auditor. These rights are not necessarily exercised every year but relate to
 - a. Grant-aided organisations, where access rights have been negotiated because the Exchequer makes a significant contribution²
 - b. Bodies in receipt of voted funds in a form other than Grant-in-Aid, to whose books the C & AG has automatic rights of access by virtue of his audit of the relevant Appropriation Account.²

All the responsibilities under (i)-(iii) and some of those under (iv) are laid on the C & AG by statute.

/PART II

1. Accounts which are audited by the C & AG following a Treasury direction under Section 3 of the E & AD Act 1921 or on the basis of an agreement between the C & AG, the relevant Department and the body concerned are marked with an * or a † respectively.

2. Bodies which in accordance with Cmnd 7797 it is proposed should be disbanded or where public funding is to be discontinued are marked with a ϕ.

- PART II Revenue, Banking and Superannuation Accounts audited by
the C & AG¹
- PART III Accounts which do not relate to the current (1979-80) payment
or receipt of public funds, where the C & AG audits usually on
a fee basis¹
- PART IV International organisations audited by the C & AG on a fee basis

1. See footnote on previous page

PART I Accounts relating to the expenditure of public funds

DEFENCE

- (i) Class I Votes 1-5
- (ii) HM Dockyards and other establishments
; Royal Ordnance Factories
- (iii) Nil
- (iv) Naval and Marine Museums (Grant in Aid)
National Army Museum (Grant in Aid)
Royal Air Force Museum (Grant in Aid)
- (v) a. Nil
b. Nil¹

1. In addition the C & AG has rights of access to the books of International Military Services Ltd for which token provision is made at Class I Vote 2 Subhead N5 for any contingent liability arising from its defence activities, for which the Secretary of State for Defence assumed responsibility on 1 April 1977.

OVERSEAS

- (i) Class II Votes 1-11
- (ii) Nil
- (iii) Nil
- (iv) †British Council
‡Bureau of Hygiene and Tropical Disease
‡Commonwealth Agricultural Bureaux
‡Commonwealth Foundation
‡Commonwealth Fund for Technical Cooperation
*Commonwealth Institutes (London and Edinburgh)
‡Commonwealth Secretariat
‡Commonwealth Science Council
‡Commonwealth Youth Programme
Foreign Compensation Commission
†Overseas Service Pension Scheme Fund
†Overseas Superannuation Scheme
Widows and Childrens/Orphans Pension Funds:
Botswana, Ghana, Kenya, Lesotho, Seychelles, Sierra Leone, Swaziland
- (v) a. British Atlantic Committee
British Youth Council
British Yugoslav Society
- Franco-British Council (British Section) Ltd
GB-China Centre
GB-East Europe Centre
GB-USSR Association
∩ Institute of Development Studies
Inter-University Council for Higher Education Overseas
Marshall Aid Commemoration Commission
United Nations Association
Bodies grant-aided under Class II Vote 10 Subhead D10 and certain
of those grant-aided under Vote 10 Subhead D11.
- b. Association of Commonwealth Universities
Catholic Institute for International Relations
International Voluntary Service Intermediate Technology Industrial
Voluntary Service Overseas Services
World University Service

AGRICULTURE, FISHERIES, FOOD AND FORESTRY

- (i) Class III Votes 1-10
- (ii) Ministry of Agriculture, Fisheries and Foods: Lands Managed
Department of Agriculture and Fisheries, Scotland: Lands Managed and Farmed
Welsh Office Agriculture Department: Lands Managed
- (iii) National Loans Fund Issues to the Covent Garden Market Authority
- (iv) Agricultural Marketing Fund
Central Council for Agricultural and Horticultural Cooperation
Forestry Fund
Herring Industry Fund and Board
IBAP Buying Accounts
White Fish Authority
- (v) a. Agricultural Training Board
National Institute of Agricultural Botany
- b. Agricultural Credit Corporation Ltd
British Wool Marketing Board
Cereals Committee Ltd
Crofters Commission
Eggs Authority
Home Grown Cereals Authority
Land Settlement Association Ltd
Meat and Livestock Commission
Milk Marketing Boards
National Proficiency Tests Council
Potato Marketing Board
Red Deer Commission
Scottish Agricultural Organisation Society
Scottish Agricultural Colleges and Research Institutes¹

¹In addition the C & AG has access to the books and records of the Covent Garden Market Authority (in respect of finance from the National Loans Fund - see (iii) above) and the National Seeds Development Organisation Ltd, whose net receipts are surrendered to the Consolidated Fund

TRADE, INDUSTRY, ENERGY AND EMPLOYMENT

- (i) Class IV Votes 1-25 and Class V Votes 1-2
- (ii) Export Credits Guarantee Department:
Credits Insurance Scheme
Overseas Investment Insurance Scheme
Special Guarantees Scheme
Offshore Petroleum Installation Facilities
- (iii) National Loans Fund Issues to
British Airports Authority
British Airways Board
Civil Aviation Authority
British Aerospace
British Shipbuilders
British Steel Corporation
Development Board for Rural Wales
National Enterprise Board
Post Office
Scottish Development Agency
Shipbuilding Industry Board
Welsh Development Agency
British Gas Corporation
British Nuclear Fuels Ltd
Electricity Council
National Coal Board
North of Scotland Hydro-Electric Board
South of Scotland Electricity Board
The Radiochemical Centre Ltd
- (iv) British Tourist Authority
Civil Aviation Authority
English Tourist Board
Marine and Aviation Insurance (War Risks) Account¹
Price Commission
Scottish Tourist Board
Simplification of International Trade Procedures Board
Wales Tourist Board
Anglo-German Foundation for the Study of Industrial Society
Cooperative Development Agency
Design Council
Development Board for Rural Wales
Highland and Islands Development Board
National Research Development Corporation (Statements of Account)
Scottish Development Agency
Welsh Development Agency
United Kingdom Atomic Energy Authority
Advisory, Conciliation and Arbitration Service
Health and Safety Commission² /Executive
Manpower Services Commission

1. The Secretary of State is empowered to insure and reinsure ships, aircraft and cargo against war risks. Any receipts or payments are paid into or out of the Consolidated Fund.

2. In addition, the C & AG audits the accounts prepared by the Department of Industry under the Local Employment Act 1972 showing the financial results of providing premises through the English Industrial Estates Corporation. For the purpose the C & AG enjoys rights of access to the books of the Corporation.

TRADE, INDUSTRY, ENERGY AND EMPLOYMENT (continued)

- (v) a. British Agricultural Export Council
British Overseas Trade Group for Israel
British Standards Institution
Committee for Middle East Trade
East European Trade Council
Latin American Trade Advisory Group
Merchant Navy Welfare Board
National Association of Citizens Advice Bureaux
National Consumer Council
National Federation of Consumer Groups
National Metrology Coordinating Unit
Royal Society for the Prevention of Accidents
Sino-British Trade Council
Clothing Industry Productivity Resources Agency
Development Corporation of Wales
Devon and Cornwall Development Bureau
Institute of Patentees and Inventors
North of England Development Council
North-West Industrial Development Association
Welsh Development Agency Holdings Ltd
Yorkshire and Humberside Development Association
Royal Society
UKAEA Retirement Fellowships Scheme
- b. Monopolies and Mergers Commission
Nationalised Industry Consumer Councils
Overseas Projects Fund
Ship Mortgage Finance Co
Community Industry Scheme Bodies
Industrial Training Boards¹
Miscellaneous Training Bodies¹
National Dock Labour Board
Remploy Ltd
Youth Opportunities¹ and Job Creation Scheme Bodies
National Coal Board (access to records relating to Vote payments to redundant mine workers)
- Metrication Board
UK Trade Agency for Developing Countries
Genetic Manipulation Advisory Group²

-
1. The C & AG enjoys rights of access to these bodies by virtue of his audit of the Manpower Services Commission (see (iv) above)
 2. The C & AG has rights of access to this body by virtue of his audit of the Health and Safety Commission/Executive

ROADS AND TRANSPORT

- (i) Class VI Votes 1-7
- (ii) Nil
- (iii) National Loans Fund Issues to
 - British Railways Board
 - British Transport Docks Board
 - British Waterways Board
 - Harbour Authorities
 - National Bus Company
 - National Freight Corporation
 - Scottish Transport Group
- (iv) Erskine Bridge and Severn Bridge Toll Accounts¹
- (v) a. Nil
 - b. Loganair Ltd
 - Orkney Islands Shipping Co Ltd
 - Road Safety Education Development Unit

1. Net receipts are surrendered to the Consolidated Fund

HOUSING AND OTHER ENVIRONMENTAL SERVICES

- (i) Class VII Votes 1-4 and Class VIII Votes 1-8
 - (ii) Nil
 - (iii) National Loans Fund Issues to
 - Building Societies
 - Housing Associations
 - Housing Corporation
 - Land Authority for Wales
 - New Towns Development Corporations and Commission
 - Scottish Special Housing Association
 - Water Authorities
 - (iv) Countryside Commission for Scotland
 - Development Fund
 - Ironstone Restoration Fund
 - Land Authority for Wales
 - Nature Conservancy Council
 - Scottish Commission for Local Authority Accounts
 - Sports Council
 - Sports Council for Wales
 - (v) a. Agreement Board
 - Centre for Environmental Studies
 - Council for Small Industries in Rural Areas
 - National Building Agency
 - b. Building and Friendly Societies (in connection with Option Mortgage Scheme)
 - Countryside Commission
 - Housing Associations
 - Housing Corporation
 - Scottish Special Housing Association
- Location of Offices Bureau

LAW, ORDER AND PROTECTIVE SERVICES

- (i) Class IX Votes 1-15
- (ii) Nil
- (iii) Nil
- (iv) Commission for Racial Equality
Criminal Injuries Compensation Board
Equal Opportunities Commission
Legal Aid Funds (Statements of Account)
Metropolitan Police Fund
Police Complaints Board
- (v) a. Catholic Marriage Advisory Council
Family Welfare Association
Institute of Marital Studies
Jewish Marriage Education Council
National Association for the Care and Resettlement of Offenders
National Council of Social Service
National Marriage Guidance Council Women's Royal Voluntary
United Kingdom Immigrants Advisory Service Service
- b. Gaming Board

EDUCATION AND LIBRARIES, SCIENCE AND ARTS

- (i) Class X Votes 1-30
- (ii) Nil
- (iii) Nil
- (iv) Agricultural Research Council
+Arts Council
: British Library
+Crafts Advisory Committee
Medical Research Council
+National Library of Wales
+National Museum of Wales
Natural Environment Research Council (including British Antarctic Territory)
Science Research Council
+Scottish Arts Council
+Scottish Sports Council
Social Science Research Council
+Welsh Arts Council
- Trustee Museums and Galleries Purchase
Grant in Aid Accounts
- (v) a. British Academy
British Film Institute
British Institute of Recorded Sound
Cranfield Institute of Technology
Gaelic Books Grant
Open University
Royal College of Art
Royal Geographical Society
Royal Scottish Geographical Society
Royal Society
Royal Society (Edinburgh)
Schools Council
Sir John Soane's Museum
South Bank Theatre Board
Universities in England, Wales and Scotland
- b. Central Bureau for Educational Visits and Exchanges
Council for Educational Technology
Council for Museums and Galleries etc, Scotland
Council of Museums in Wales
Direct Grant Further and Adult Education Establishments in England,
Wales and Scotland
Direct Grant Secondary Schools in England, Wales and Scotland
Direct Grant Special Schools in England, Wales and Scotland
League for the Exchange of Commonwealth Teachers
Museum Documentation Association
National Film School
University Grants Committee
Voluntary Teacher Training Colleges in England and Wales
Scottish Council for Educational Technology
Scottish Council for Research in Education
- Advisory Council
for Adult and
Continuing
Education
Teacher Training Colleges in Scotland

HEALTH, PERSONAL SOCIAL SERVICES AND SOCIAL SECURITY

- (i) Classes XI Votes 1-5 and XII Votes 1-4
- (ii) Nil
- (iii) Nil
- (iv) Central Council for Education and Training in Social Work
Council for Education and Training of Health Visitors
Health Services Board
National Biological Standards Board
National Health Service Summarised Accounts
National Health Service (Scotland) Accounts
National Radiological Protection Board
Public Health Laboratory Service Board
- (v) a. Joseph Rowntree Memorial Trust
Intermediate Treatment Trust
Midwife Teachers Training College
- b. Association of Community Health Councils
Association of Scottish Local Health Councils
Central Blood Laboratories
Central Midwives Boards (England and Wales, and Scotland)
Common Services Agency (Scotland)
Council for Postgraduate Medical Education and Training
Dental Estimates Board
Development Team for the Mentally Handicapped
Family Fund
General Nursing Council
General Nursing Council for Scotland
Health Authorities, Boards, Councils and Special Trustees
Health Education Council
Joint Board of Clinical Nursing Studies
List D Schools (Scotland)
Malaria Reference Laboratory
Medical Practices Committee
Mental Welfare Commission for Scotland
Occupational Pensions Board
Panel of Assessors for District Nurse Training
Personal Social Services Council
Prescription Pricing Authority
School for Dental Auxiliaries Ltd
Scottish Council for Postgraduate Medical Education and Training
Welsh Health Technical Services Organisation

OTHER PUBLIC AND COMMON SERVICES

- (i) Class XIII Votes 1-31 (excluding Vote 9), Class XIII A Vote 1 and Class XIV Votes 1-10
- (ii) HMSO: Government Bookshops
Property Services Agency: Supplies Trading Fund
Royal Mint Trading Fund
- (iii) Issues from the National Loans Fund to
Local Authorities
- (iv) Consolidated Fund and National Loans Fund Accounts
Consolidated Fund and National Loans Fund Supplementary Statements
Contingencies Fund
Government Hospitality Fund (Grant in Aid)
+History of Parliament Trust Account
House of Commons Members Fund
House of Commons Refreshment Department Accounts
Irish Land Purchase Fund
Parliamentary Contributory Pension Fund
Tithe Act 1936 Account
- (v) a. British American Parliamentary Group
Chequers Trust
Civil Service Sports Council
Commonwealth Parliamentary Association
Inter-Parliamentary Union
Commonwealth War Graves Commission
- b. Royal Commissions
National Economic Development Council

NORTHERN IRELAND¹

- (i) Class XV Votes 1-5
- (ii) Nil
- (iii) National Loans Fund Issues to
Northern Ireland Consolidated Fund
- (iv) Police Authority for Northern Ireland
Police Complaints Board for Northern Ireland
- (v) a. Belfast Community Law Centre
"Extern"
Northern Ireland Association for the Care and Resettlement of Offenders
Save the Children Fund
Training Schools and Remand Homes Accommodation
- b. Nil

-
1. Accounts relating to services financed from the Northern Ireland Consolidated Fund are audited and inspected by the Comptroller and Auditor General (Northern Ireland). At present, these accounts, together with the C & AG (NI)'s reports on them are laid before Parliament.

RATE SUPPORT GRANT AND FINANCIAL SERVICES

- (i) Class XVII Votes 1-15
- (ii) Nil
- (iii) Nil
- (iv) Nil
- (v) a. Nil
b. Nil

PART II Revenue, Banking and Superannuation Accounts audited by the C & AG

- Inland Revenue Revenue Account
- Customs and Excise Revenue Account
 - (including Isle of Man Act 1958 Customs and Excise Account)
- Driver and Vehicle Licence Revenue Account
- IBA: Additional Payments by Programme Contractors Account
- National Oil Account
- Post Office Broadcast Receiving Licence Receipts Account
- DOE and SDD Betterment Levy Revenue Accounts
- Community Land Surpluses Account
- National Insurance Surcharge Revenue Accounts (DHSS and DHSS(NI))
- Funds left in Trust for the Reduction of the National Debt:
 - Elsie Mackay Fund
 - John Buchanan Fund
 - †Doris Duke Gift Fund
- *Paymaster General's Banking Account
- National Savings Bank Accounts (Investment and Ordinary Deposits)
- Trustee Savings Bank Accounts (Fund for the Banks for Savings) Account
- Maternity Pay Fund
- National Insurance Fund
- Redundancy Fund
- †National Insurance (Industrial Injuries) Colliery Workers Supplementary Scheme
- *NHS Acts Revenue and Expenditure Accounts under Superannuation Regulations
- *Teachers Superannuation (England and Wales): Actuarial Account
- *Teachers Superannuation (Scotland): Actuarial Account
- UKAEA Principal Non-industrial Superannuation Scheme and Industrial Superannuation Scheme

PART III Accounts which do not relate to the current (1979-80) payment or receipt of public funds, where the C & AG audits usually on a fee basis

- *Air Travel Reserve Fund
- †Arts Council Retirement Fund
 - Aviation Security Fund
 - Church Commissioners Accounts
- †Commonwealth Institute Superannuation Scheme Funds
- †Commonwealth Zimbabwe Scholarships Fund
- Crown Agents Realisation Account
- *Crown Agents Abstract Accounts (final accounts relating to period up to 31/12/79)
- Distribution of German Enemy Property Account
- †Flora Zambesiaca
 - Forestry Enterprise Accounts
 - Funds in Court in England and Wales
- *Funds in Court (Northern Ireland)
 - General Lighthouse Fund
 - Greenwich Hospital and Travers Foundation Accounts
- †Holyrood Amenity Trust
- *House of Lords Security Fund
 - Industrial Organisation and Development Levy Accounts
 - Insolvency Services (Accountancy and Investment) Act 1970 Account
- †Interim Commissioner for the West Indies
- *Land Purchase Trustee for Northern Ireland Account
- *Merchant Shipping Acts: Wages of Living Seamen
- *Merchant Shipping Acts: Property of Deceased Seamen
- National Land Fund¹
 - Official Custodian of Charities (Charities Act 1960) Account
- †Palestine Currency Fund
 - Police Property Fund (Northern Ireland)
 - Royal Hospital Chelsea Account
- †Royal Patriotic Fund Corporation
 - Royal Ulster Constabulary Fund
- †Society of Clerks at the Table in Commonwealth Parliaments
- †Sports Council Trust
- Sugar Beet (Research and Education) Fund
- Supreme Court of Judicature (Northern Ireland) Land Purchase Account
- Trust Funds:
 - †Agricultural Research Council Underwood Fund
 - †Agricultural Research Council Wain Fund
 - †British Council Donations for Special Purposes
 - †British Library Trust Funds
 - †British Library Endowment Funds
 - †British Museum Trust Funds
 - †British Museum (Natural History) Special Funds
 - Department of Education and Science Trust Funds
 - †Imperial War Museum Trust Funds
 - †Medical Research Council Endowment Funds
 - †National Army Museum Private Funds
 - †National Gallery Trust Funds
 - *National Galleries of Scotland Trust Funds
 - †National Library of Scotland Trust Funds
 - †National Maritime Museum Trust Funds
 - †National Museum of Antiquities of Scotland Trust Funds

-
1. Payments from the National Land Fund are made to the Commissioners of Inland Revenue in satisfaction of CTT in return for property accepted in lieu.

Trust Funds (continued):

- †National Portrait Gallery Trust Funds
- †Royal Scottish Museum Lindsay Carnegie Trust
- †Science Museum Trust Funds
- †Social Science Research Council Private Funds
- †Tate Gallery Trust Funds
- †Victoria and Albert Museum Trust Funds Pool
- †Victoria and Albert Museum John Webb Trust Fund
- *Universities and Colleges Estates (Winchester College)
- USA (MDAP) Equipment Disposal Deposit Account
- †West Africa Currency Board (Residual Assets) Fund
- *Wreck and Salvage Account

PART IV International organisations audited by the C & AG on a fee basis

Food and Agriculture Organisation
General Agreement on Tariffs and Trade
Inter-Governmental Maritime Consultative Organisation
International Agency for Research on Cancer
International Centre for Advanced Technical and Vocational Training
International Labour Organisation
International Maritime Satellite Organisation
International Oil Pollution Compensation Fund
North Atlantic Ocean Stations
North East Atlantic Fisheries Commission
Oslo Commission on the Prevention of Marine Pollution by Dumping
Pan American Health Organisation
United Nations Educational, Scientific and Cultural Organisation
Western European Union
World Health Organisation
World Meteorological Organisation

IN CONFIDENCE



File Govt Machinery SK

10 DOWNING STREET

From the Private Secretary

12 November 1979

Dear David

The Prime Minister has seen the recent correspondence on the Comptroller and Auditor General's enquiries about the financial implications of policy on council house sales, initiated in your Secretary of State's letter of 22 October. She has also seen the letters from the Lord Chancellor of 26 October, the Chancellor of the Duchy of Lancaster of 7 November and the Chancellor of the Exchequer of 8 November.

The Prime Minister agrees that the developments illustrated by this case seem undesirable. For the present, she is content that matters should be pursued through the Treasury's continuing informal contacts with the Comptroller and Auditor General, as suggested in the Chancellor of the Exchequer's letter of 8 November.

I am sending copies of this letter to the Private Secretaries to the members of the Cabinet, including the Minister of Transport, and to Martin Vile (Cabinet Office) and David Laughrin (Civil Service Department).

*Yours sincerely
Mike Pattison*

David Edmonds, Esq.,
Department of the Environment

IN CONFIDENCE



PRIME MINISTER.

A sensible response to the problem about the C & AG's use of his powers, raised in the Heseltine's letter below

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

8 November, 1979

M.P. 9/11

Dear Michael

[Handwritten signature]

THE C & AG AND COUNCIL HOUSE SALES

Thank you for your letter of 22nd October about Sir Douglas Henley's recent initiative. I have also seen Quintin Hailsham's and Norman St. John Stevas' letters of 26th October and 2nd November respectively. I share the concern which everyone has expressed.

Some of the urgency has gone out of this matter as a result of a deliberative meeting of the PAC of which my officials have had informal reports from the Clerk and from representatives of the Exchequer & Audit Department. It seems that the Chairman took the initiative to refer briefly, at the end of a long meeting about other matters, to the issue of council house sales. He implied that this was an important issue within the purview of the Committee, and that he hoped the Committee would be able to find room for it in their programme at some future date. There appears to have been no reaction from other members of the Committee. The Clerk has suggested to my officials that the Committee are unlikely to be able to deal with this matter until after January, since they already face a heavy programme.

Although members of the Committee are aware in general terms of the Comptroller and Auditor General's personal interest in this subject, they do not appear to know of the existence of the draft memorandum, and there was no mention of this at last week's meeting. Joel Barnett did however draw their attention to your written Answer in the House on 23rd October in which you promised an appraisal of the financial effects of council house sales in connection with the Bill. Clearly, therefore, the assumption in the minds of the Chairman and the members is that any hearing which they decide to hold on this issue will be based on your financial appraisal.

/In these

The Rt. Hon. Michael Heseltine, M.P.

IN CONFIDENCE



In these circumstances I suggest the right line for your Accounting Officer to take in writing to Sir Douglas Henley might be to decline to offer detailed comments on the draft memorandum on the ground that he understands it has now been overtaken, while making clear that had it been for use as originally intended he would have had difficulty with much of it. I also think it would do no harm if your Accounting Officer's letter were to mention that this use of powers of access to Departmental papers, which were intended for audit purposes, as a source of information about the process of formulating current and future policy raises some awkward questions.

While it is some comfort that the memorandum as drafted seems now unlikely to go forward to the PAC, it is less satisfactory that the Committee may yet decide to involve themselves in the political debate about the forthcoming legislation. As you point out, this kind of development could jeopardise the traditionally bipartisan character of the PAC, and the effective working arrangements which have grown up over the years between Departments and the E & AD. It would also be a departure from the audit-based tradition of the PAC's work, and take them into questions better discussed on the floor of the House, or in the Committee on the relevant legislation, or in the new departmental Committee.

I am doubtful about direct intervention with Joel Barnett at the present stage. It might only stimulate his interest. But we can well keep the idea in mind, and meanwhile seek to influence events in the right direction through the Treasury's continuing informal contacts with the C & AG.

Both because of the possibility that the Committee may go ahead with their enquiry and for other reasons I should be glad to have a sight in due course of your financial appraisal in draft.

I am sending copies of this letter to the recipients of yours.

A handwritten signature in dark ink, appearing to read 'Geoffrey Howe', written in a cursive style.

(GEOFFREY HOWE)

IN CONFIDENCE

CONFIDENTIAL

TMW

Govt Machinery

cc Priestley, Cab. Off.

MR. LAUGHRIN,
CIVIL SERVICE DEPARTMENT.

The Prime Minister has seen the paper on the Exchequer and Audit Department which you sent me under cover of your letter of 31 October.

She was grateful for this further information. She recognises that she should take this up with the Financial Secretary to the Treasury and the Comptroller and Auditor General if she wishes to look further into ways in which E&AD work can assist the Government's drive to improve efficiency and eliminate waste. For the present, however, she does not propose to take this any further.

M.A. PATTISON

5 November 1979

CONFIDENTIAL

MBD

PRIME MINISTER

Here is a paper describing the existing functions of the Exchequer and Audit Department. It also shows the slight changes of direction that are now being suggested. The important point to note is the complete independence of the Comptroller and Auditor General.

There are some small ways in which E & A D work, particularly with these changes, can assist Departmental Ministers in the management task you have given them, both on the Rayner exercises and on the Civil Service manpower exercise. In particular, the pressure for more effective internal audit within Departments is following one of Rayner's key principles, that people within a Department can best follow through questions about the performance of functions.

I suspect that there is little that Government can do to get more direct assistance in its management role from E & A D. I showed you Mr. Heseltine's letter expressing alarm at the Comptroller and Auditor General's attempt to comment in advance on the implications of policy decisions now under study on council house sales. The Lord Chancellor has now written in to support strongly Mr. Heseltine's reservations. But the internal audit work suggested in paragraph 6d of the paper is one of the tools on which Ministers can draw in carrying out their management task. When the Lord President comes back to Cabinet for endorsement of his six per cent cuts, and for directions on how manpower is to be controlled in the future, it could be helpful to draw attention to the instruments on which Ministers can call - e.g. Rayner-type studies, Heseltine-type personal control of complementing and recruiting, and internal audit of the kind now encouraged by the C & A G. If you want to pursue the E & A D role further, you should probably now talk to Sir Douglas Henley, first taking advice from the Financial Secretary to the Treasury.

A R M Laven
PP Mr Pattison.

They are waiting a little
There is so much else
to pursue at present

2 November 1979

BF 9/11 MRP



Chancellor of the Duchy of Lancaster

PRIVY COUNCIL OFFICE
WHITEHALL, LONDON SW1A 2AT

2 November 1979

COMPTROLLER AND AUDITOR GENERAL

The Secretary of State for the Environment has sent me a copy of his letter to you of 22 October about the Comptroller and Auditor General's proposed memorandum for the Public Accounts Committee on the sale of council houses.

I share Michael Heseltine's concern about Sir Douglas Henley's intervention and the exposure of advice to Ministers which could result from it. I am also concerned about the role of the PAC in this matter. I can well see that Jack Staw may have aroused their interest but it would seem to me most unfortunate if the PAC were to see it as their business to question the financial assumptions behind legislation which has not yet been introduced or which is still before the House. This would complicate and delay the preparation and passage of bills with potentially serious implications for our legislative programme; and it would confuse the functions of the PAC, of the Standing Committee on the Bill, and possibly of the new Select Committee on the department concerned. We have not yet formulated a Government view on how far it would be appropriate for the new Select Committees to interest themselves in proposals for future legislation, and at this stage I think it would be best to deal with such interest as it arises in individual committees, with guidance from the departmental Minister concerned. My own view - which I indicated briefly in the debate on 25 June (Col. 217) - is that we should not prevent them from asking about the shape of coming legislation as their dialogue with the department goes on - but their interest would be broader and the context and scope of such questioning would be different from what would be involved in an enquiry by the PAC. A third consideration is that Ministers and officials could hardly be very forthcoming in such a discussion with the PAC, and that could lead to criticism and ill-feeling that could affect relations with Select Committees generally.

Contd...



I therefore hope very much that the PAC can be discouraged from this kind of enquiry, and I wonder if you or Nigel Lawson might have a discreet word with Jock Barnett. You will not want to overplay the problem, but I should be glad to join in if you think that would help.

I am sending copies of this letter to Cabinet colleagues and the Minister of Transport, and to Sir Robert Armstrong and Sir Ian Bancroft.

James Callaghan

The Rt Hon Sir Geoffrey Howe, QC, MP
Chancellor of the Exchequer
HM Treasury
SW1

CONFIDENTIAL



CIVIL SERVICE DEPARTMENT
WHITEHALL LONDON SW1A 2AZ

Telephone 01 273 5400

*Sir Ian Bancroft G.C.B.
Head of the Home Civil Service*

M A Pattison Esq
10 Downing Street
LONDON SW1

31 October 1979

Dear Nick

DEVELOPING WORK OF THE E&AD

... As requested in your minute of 8 October, I attach a supplementary note about the developing work of the E&AD. The terms of the note have been agreed with the Treasury.

It was agreed earlier that we should not show this note to E&AD; but that if you wanted to pursue questions about its developing role in more detail you might wish to bring the C&AG into consultation on this.

I am copying this letter to Jonathon Taylor.

*Yours sincerely
Tof Churchd.*

DL
DAVID LAUGHRIN

CONFIDENTIAL

THE DEVELOPING WORK OF THE EXCHEQUER AND AUDIT DEPARTMENT (E&AD)

The E&AD assist the Comptroller and Auditor General (C&AG) in the performance of his statutory role as external auditor of the Government. In effect, they are the C&AG's Department.

2. The C&AG is an independent office holder under the Crown, and is answerable neither to the Government nor to Parliament though in practice most of his work is for Parliament's benefit. He works closely with the Public Accounts Committee. The Committee uses his reports on Departments' accounts as the basis for their examination of the way Departments have managed and spent the public funds for which they are responsible.

3. The C&AG is required by statute to examine and certify the accounts of Government departments (and certain other public bodies) after checking that money is only spent on the purposes approved by Parliament in conformity with the appropriate statutory or other authority. This check on the propriety and regularity of Departmental expenditure remains his basic audit task.

4. In addition he has for many years with the encouragement of the PAC extended his examinations to cover questions of economy and efficiency. These are known as "value for money" inquiries and are directed at uncovering wasteful or extravagant expenditure. In some recent cases his inquiries have moved towards an "effectiveness" audit. This involves an assessment of the "cost effectiveness" of particular expenditure programmes in meeting their policy objectives.

5. In view of the wide range of government expenditure, the C&AG has to be selective in deciding on areas to study in any depth. His work is "audit based", by which is meant that it is directed to an appraisal of the results of expenditure on specific projects or programmes. He has a statutory right of access to the records of Departments etc for the purposes of his audit examinations.

6. The work of E&AD was examined by a Management Review during 1978. The review team contained staff from E&AD itself and from the CSD and Treasury and two outside consultants. It reported to a Steering Committee chaired by the C&AG himself. Various recommendations were made to improve the quality of the Department's work. Their aim was:

- a. To encourage a more "professional" approach to the work of the department through better planning, monitoring and subsequent review of the audit of

departmental accounts. In particular the Department was recommended to adopt more widely the practice (followed by outside audit firms) of reviewing the adequacy of the accounting and control systems rather than spending a great deal of time checking the correctness of individual transactions.

b. To encourage a more positive approach to the auditing of departmental accounts through reporting areas of potential weakness to departments rather than waiting for errors to occur; and by examining and reporting on the adequacy of departmental financial and management information systems as well as on the formal accounting records.

c. To develop the professionalism of the Department's staff by extending and improving its training effort for new and existing staff. (All new staff must now study for and obtain a recognised accountancy qualification.)

d. To bring pressure to bear on departments to improve the quality of their own internal audit branches and then to make greater use themselves of the work done by internal audit in planning their own work.

7. The C&AG as the external auditor of the government helps Parliament with its scrutiny of the Executive. As such, he and his department must be entirely independent of government and cannot be its instrument. Securing the efficiency of its operations must be the task of government itself. However, the E&AD can act as a spur to greater efficiency of the government and the development of its work in the ways suggested by the Management Review (and in particular at '6b' above) should enable it to do that job more effectively.

8. The E&AD Acts which provide the statutory framework for the Department's work are now being reviewed by a group of officials under Treasury chairmanship reporting to the Financial Secretary. The review was launched earlier this year by the previous Administration, partly in response to a series of recommendations over the previous two years by various Select Committees (Expenditure, Procedure, PAC) all aimed at strengthening the public audit system and making it more relevant to modern Parliamentary needs. The present Government announced in June that they intended to press on with the review, and present plans envisage publication early next year of a Green Paper as a basis in the first place for public and Parliamentary discussion and thereafter for legislation. The nature and objectives of the C & AG's audit work (ie the balance between the various activities referred to in paragraphs 3 and 4 above)

will be one of the issues to be covered in the Green Paper. Others will include the range of public bodies to be audited by the Department and the constitutional status of the C&AG and his staff.

Civil Service Department
Whitehall
London SW1

October 1979

NBPM
Guth Mad
30/x

010.



HOUSE OF LORDS,
SW1A 0PW

26th October 1979

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My dear Geoffrey..

Michael Heseltine sent me a copy of his letter to you of 22nd October about the suggestion that the Comptroller and Auditor General had made that he might submit to the Public Accounts Committee a memorandum based on departmental files and dealing with officials' calculations relevant to the policy of selling Council Houses.

I share Michael Heseltine's misgivings about this development. I think, as he does, that it could form an unfortunate precedent for financial advice relevant to policy currently being formulated being made available to the Public Accounts Committee. I do, therefore, agree that it would be wise to take such steps as can be taken to stop this development.

I am sending copies of this letter to Michael Heseltine and to those to whom he sent copies of his letter to you.

Yrs :

The Right Honourable
Sir Geoffrey Howe, C.C., M.P.

PRIME MINISTER

The attached letter from Mr. Heseltine to the Chancellor argues that the Comptroller and Auditor General is exceeding his functions. Mr. Heseltine records the intention of E and AD to submit to PAC a paper on the future financial implications of policy decisions now being considered in the Department.

We shall shortly be receiving a note about the functions of E and AD following your comments to Sir Derek Rayner. The questions now raised by Mr. Heseltine can also be looked at in that context. His letter raises an important issue of principle: the particular case which has brought it up is no longer urgent, as the PAC Chairman has now decided to approach housing issues in a different way, with the result that Sir Douglas Henley's draft memorandum will not be issued.

You should, however, be aware of the point now in case Mr. Heseltine mentions it to you in the margins of Cabinet.

24 October 1979



2 MARSHAM STREET
LONDON SW1P 3EB

My ref:

Your ref:

22 October 1977

Jan Cullis

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I think I should alert you, and our colleagues, to my concern at what appears to be an attempt by the Comptroller and Auditor General, Sir Douglas Henley, to extend his role into commenting on financial aspects of forthcoming legislation, and using his access to our files for audit purposes to reveal in advance of our defending our legislative proposals in Parliament the advice we have received from officials on those proposals. This precedent if established clearly has the most far-reaching implications for all Government Departments.

The issue is that of the sale of council houses, which is of course a main element in the programme on which we were elected and is highly contentious politically - and especially the terms of sale, notably the discounts. When we came into office we made our improved discount arrangements available for existing voluntary sales in advance of the legislation we are introducing this session. My officials called my attention with supporting figures to the possibility of criticism that, on certain assumptions, while there was bound to be a short term gain to the public purse, there could be a loss in the long term; but all depended on the assumptions, which were bound to be speculative eg about future rates of inflation. On this basis we concluded we could reject any such criticism either at that time or when the issue would no doubt be debated on our forthcoming legislation.

The Comptroller and Auditor General, through Exchequer and Audit Department, has access to departmental files for purposes of audit. My officials knew that some interest had been shown by Exchequer and Audit Department in the arrangements for the sale of council houses, and that Sir Douglas Henley had mooted the possibility of putting forward a Memorandum to the Public Accounts Committee in the light of this. But when they expressed doubts about this novel proposal, which seemed rather far away from Comptroller and Auditor General's normal role of an apolitical auditor of the regularity, propriety, and value for money of transactions under existing legislation, and venturing into a field which was to be the subject of forthcoming and no doubt politically contentious legislation, they had received reassurances.

My Accounting Officer was, therefore, greatly surprised to receive, towards the end of last month, a draft Memorandum which Sir Douglas Henley had in mind to submit to the Public Accounts Committee, which, using the information on our files, set out in summary form the calculations my officials had put before me, and repeated their advice to me about the possibilities of longer term loss wider certain assumptions - assumptions I should stress that are not accepted by Ministers in the Department as being the most probable.

Your officials and mine have talked to Sir Douglas Henley to represent the concern of Accounting Officers generally that material obtained through Comptroller and Auditor General's right of access for audit purposes should be used in this way; that there were great dangers in the Comptroller and Auditor General setting himself up to give a financial view on forthcoming legislation and particularly in drawing on departmental papers for this purpose - papers that are not endorsed by Ministers and to which he had access for quite different purposes: that although Accounting Officers have a peculiar responsibility to Parliament through the Public Accounts Committee for their financial management of Departments, it is Ministers, not Accounting Officers, who have to defend proposals in legislation with financial implications, and Accounting Officers are only responsible for carrying out what Parliament has enacted. Even though, as in this case, they would expect to advise Ministers of the financial implications and possible criticisms of legislative proposals, they would not expect to be questioned by the PAC in advance of the legislation being discussed in Parliament on the tenor of their advice: nor would they expect Ministers to be confronted, during the passage of the legislation, with the advice they had received from officials, obtained as it was through access directed primarily at audit.

My Accounting Officer made it clear that if current material was used in this way, he might have to consider withdrawing access by Exchequer and Audit Department to current papers without his own prior approval; though he would do this with the greatest reluctance, because it would upset the effective understandings which has long prevailed between the PAC, Comptroller and Auditor General, and Accounting Officers. But in any event the issue of the proposed Memorandum, on so politically contentious an issue, would doubtless upset the bi-partisan nature of the PAC to the detriment of those understandings.

Our officials believe that Sir Douglas Henley was impressed by these arguments. He still thinks that Parliament ought to have before it information on the financial implications of Government proposals, but has taken note of the argument that he, with his particular responsibilities and powers, and the PAC, to which Accounting Officers are directly answerable, may not be the most appropriate channel. However, he said he needed to consult Joel Barnett, as Chairman of the PAC, before deciding whether to go ahead with his Memorandum. And this is understandable because Jack Straw MP has written to Joel Barnett as Chairman of the PAC on this issue, which the Opposition know to be a contentious one.

My Accounting Officer is proposing to write to Sir Douglas Henley saying that the Memorandum is unacceptable in principle as something prepared by C & AG on the basis of access to files for a different purpose; to re-iterate the arguments already put orally to Sir Douglas Henley; and to ask him not to proceed with it.

I am sure we should do everything we can to prevent this Memorandum going forward. Quite apart from the massive extension of the role of the C and AG that it would represent, it raises the most serious implications for relations between Ministers and officials in their own Departments. If this precedent is created it will mean that financial advice given to Ministers, whether they agree with it or not, is potentially immediately available to the PAC from the C and AG and is therefore accessible to the Opposition at the very time that Ministers are proceeding with Bills relating to that advice in the House. If Joel Barnett and Sir Douglas Henley decide themselves not to proceed, so well and good, though the prospect of further initiatives of this kind, perhaps more insinuatingly in a less politically contentious field, would still remain, and we should still be at risk because of the access to our files that this involves. But if there are signs that Joel Barnett does not reject the idea, perhaps one of us should have a talk with him? The role of the C & AG is of course under review at present and Joel Barnett will know that a Green Paper is in prospect. (Of course Sir Douglas Henley is very exercised about his own appearance of independence, as he has been under criticism for lacking it: and too overt an intervention by Ministers might have the opposite effect to what we wish).

I am sending copies of this to our Cabinet colleagues, including the Minister of Transport, and to Sir Robert Armstrong and Sir Ian Bancroft.

Yours ever
MHE

MICHAEL HESELTINE

The Rt Hon Sir Geoffrey Howe MP



EXCHEQUER AND AUDIT DEPARTMENT
AUDIT HOUSE VICTORIA EMBANKMENT
LONDON EC4Y 0DS

Comptroller and
Auditor General
Sir Douglas Henley K.C.B.
DOH 1728

8 June 1979

Nigel Lawson Esq MP
Financial Secretary to the Treasury
Treasury Chambers
Parliament Street
London SW1P 3AG

Dear Financial Secretary,

REVIEW OF THE EXCHEQUER AND AUDIT DEPARTMENTS ACTS

Sir Anthony Rawlinson has mentioned to me that you are consulting your colleagues about the review of the C&AG's role announced by the previous Government, and has shown me a copy of the proposed arranged P.Q. and Answer.

I warmly welcome your proposal that the review should continue; and I should be happy to have my view of the need for this work mentioned.

May I offer two comments on the draft answer I have seen. First, there are important and complex issues to be considered some of which are sensitive in Parliament and elsewhere, and it might be as well to avoid an immediate commitment on the timing. Second, I wonder whether it is either practicable or desirable to envisage breaking the consultative process down into a first stage of bilateral consultation with the relevant Parliamentary Committees and a second round of discussions with other interests; officials might be invited to consider in due course the precise form which consultation should take.

If you agree, you might like to consider a revised draft as follows:-

Q: To ask the Chancellor of the Exchequer whether the study of the Comptroller and Auditor General's present day role announced by the previous Government is continuing and whether he will make a statement.

A: My Rt. Hon Friend shares the views of recent Select Committees and of the Comptroller and Auditor General about the need for fundamental review of the C&AG's role and the Exchequer and Audit Departments Acts leading to proposals for new legislation. He has given instructions for work on the review announced by the previous Government on 18 January 1979 (OR. Col. 2037) to be pressed forward.

/I am

Govt
Mach

1. Mr. Lawson MS

2. Mr. P. S.

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I am copying this letter to the other Ministers whom I understand you are consulting, and to Sir John Hunt.

Yours sincerely
Douglas Henley.

DOUGLAS HENLEY

Govt Machinery



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SPH

10 DOWNING STREET

From the Private Secretary

5 June 1979

The Prime Minister has seen the Financial Secretary's letter of 30 May to the Chancellor of the Duchy of Lancaster in which he proposes that the review of the Exchequer and Audit Departments Acts should proceed. Subject to other colleagues' views, the Prime Minister agrees that this review should continue.

I am sending copies of this letter to the Private Secretaries to the Lord President, the Chief Whip, the Secretaries of State for Scotland, Wales, Industry, Defence, Environment, Energy and Social Services and to Martin Vile (Cabinet Office).

TL

Mrs P.C. Diggle,
HM Treasury.

SPH



Treasury Chambers, Parliament Street, SW1P 3AG

30 May 1979

The Rt Hon Norman St John Stevas MP
Chancellor of the Duchy of Lancaster
Cabinet Office
Whitehall
LONDON SW1

Prime Minister

Are you content
for his review to
proceed?

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REVIEW OF THE EXCHEQUER AND AUDIT DEPARTMENTS ACTS

The previous Government announced in January a study of the present day role of the Comptroller and Auditor General with a view to possible legislation to revise or perhaps replace the Exchequer and Audit Departments Acts 1866 and 1921. This was in response to a number of recommendations, notably from the Expenditure and Procedure Committees, for changes in the public audit system as part of wider proposals for improvements in the way in which Parliament seeks to scrutinize expenditure and control the Executive. W

The question now arises whether we should go forward with this review. I think we should. This letter is to seek your agreement, and that of other recipients.

The review is at an early stage. The initial work is being done by officials under Treasury chairmanship, and the Comptroller and Auditor General is associated with the work. The plan, of which the Public Accounts Committee were informed before the Election, is to consult the relevant Parliamentary Committees fairly soon, before initiating consultations with other outside interests.

I am in favour of the review continuing both because I think there is a good case for it on merits, and because those in the House who are interested will expect it. When the Procedure Committee Report was debated in February the main protagonists in the House welcomed the idea and seemed content that the Committee's recommendations about audit should be pursued in this way.

We are likely to be asked whether we intend to continue and I see some advantage in showing ourselves willing to do so.

I should like to announce our intentions soon, by means of an arranged PQ as follows:-

"Q: To ask the Chancellor of the Exchequer whether the review of the Exchequer and Audit Departments Acts announced by the previous Government is continuing and whether he will make a statement.

,A: My Rt. Hon Friend shares the views of recent Select Committees and of the Comptroller and Auditor General about the need for fundamental review of these Acts. He has given instructions for work on the review announced by the previous Government on 18 January 1979 (OR. Col. 2037) to be pressed to an early conclusion. He intends to arrange consultations as soon as possible with the relevant Parliamentary Committees on the basis of a discussion document as a first step to possible legislation later in this Parliament."

I should be glad to know if you would be content with this.

Copies go to the Lord President, the Chief Whip, the Secretary of State for Scotland and the Secretary of State for Wales, and to the Secretaries of State for Industry, Defence, Environment, Energy and the Social Services, and to Sir John Hunt.

NIGEL LAWSON