

Our reference Milis001ltr
Your reference
Date 19 December 2001

Members of the Metropolitan Police Authority
Romney House
43 Marsham Street
London
SW1P 3PY

Dear Member

Annual Audit Letter - 2000/2001 Audit

Please find enclosed my Annual Audit Letter on the Authority's 2000/2001 audit.

You may note that the reporting style in the Letter is different from that which we have previously used. The change reflects client feedback to us about the length and style of previous Letters. I hope that you find the format user friendly, but I would welcome your thoughts on it.

You should also be aware that under recently enacted regulations the Letter is a public document. In particular, Members of the public are entitled to a copy, should they so wish, on payment of a reasonable sum for photocopying.

Finally, I would like to thank Members for the courtesy and assistance offered to my team during the audit by you, your staff and the officers of the MPS.

Yours sincerely

Kash Pandya
District Auditor

Annual Audit Letter Metropolitan Police Authority

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DISTRICT AUDIT

Reference:	appendix1toitem11cont
Date:	December 2001

The purpose of this Letter

This is the first Annual Audit Letter (AAL) to the newly established Metropolitan Police Authority (MPA). It is issued in accordance with the requirements of the Audit Commission's Code of Audit Practice.

This AAL summarises for Members the more important matters arising from our audit for 2000/2001 and comments on other current issues. We have produced separate reports during the year on completion of specific aspects of our work, which have been discussed in detail with your staff. The reports are listed at the end of this Letter for Members' information.

The Audit Commission has circulated to all audited bodies a statement that summarises the key responsibilities of auditors. Our audit has been conducted in accordance with the principles set out in that statement. What we say about the results of our audit should be viewed in the context of that more formal background.

Audit objectives

Audit work is based on the significant financial and operational risks that the MPA and the Metropolitan Police Service (MPS) face and is structured around the three main elements set out below.

EXHIBIT 1

The three main elements of the audit



Our integrated audit covers

Accounts

- Opinion

Financial aspects of corporate governance

- Financial standing
- Systems of internal financial control
- Legality of financial transactions
- Standards of financial conduct and the prevention and detection of fraud and corruption

Performance management

- Best Value Performance Plan
- Performance information
- Use of resources

Our audit has addressed the requirements of the Code of Audit Practice and we have worked with the MPA and the MPS to maximise the benefits of the integrated audit approach. We have reviewed your arrangements for dealing with risks and we have undertaken more detailed work in selected areas of higher audit risk. Wherever possible we have liaised with other review agencies, both internal and external and in particular, with Her Majesty's Inspector of Constabulary (HMIC) and Internal Audit.

Overview

The MPA, together with the MPS, is responsible for policing in the Metropolis. It was established less than 18 months ago as a functional body of the newly created Greater London Authority (GLA) but, apart from Mayoral controls over its annual budget, is vested with its own statutory powers and duties.

The MPA/MPS is a large and complex organisation with an annual spend in excess of £2 billion, 40,000 staff, and a key and high profile national and international policing role. Though the MPA itself is new, the MPS has been around for more than 170 years and has its own culture and traditions which will need to be blended into the vision for future policing in London.

Not surprisingly, this has been a unique and very demanding period for the MPA as it has begun to get to grips with its new role and responsibilities. Early challenges have included:

- forging internal relationships between the MPA and the MPS and external relationships with the Mayor and the GLA at both Member and officer level
- rolling out the vision of the Commissioner and his Management Board for policing in London, including the move from area based policing to Borough based Operational Command Units with a stronger emphasis on local accountabilities
- improving the recruitment and retention of police officers and civilian support staff
- developing and strengthening the core infrastructure of the organisation, in particular across finance and information systems, to ensure that it is better able to respond to future needs
- responding to more rigorous external and internal scrutiny of the MPA/MPS through Best Value, the HMIC, the Mayor and external audit.

This has been, and will continue to be, a daunting agenda. The events of September 11 2001 have added a new and more complex dimension to this agenda. However, there is much to build on from what the MPS already had in place. We have also

been struck by the commitment of Members and senior staff in wanting the changes to succeed and the clear desire to translate the vision for policing in London into reality. There is much to praise in the achievements so far and we refer to these in more detail elsewhere in the Letter.

This is though only a start and a significant amount remains to be done to strengthen the infrastructure of the MPA/MPS and deliver tangible improvements. We recognise that some developments will require cultural changes and that, given the size and complexity of the organisation, these cannot readily be achieved within short time scales. We also appreciate that all these developments have to be handled within limited financial and skilled management resources.

Nevertheless, we expect to see stepped improvements and will monitor progress and support the MPA/MPS with these developments, wherever possible, through our audit. The key messages from our work are set out in the paragraphs below.

KEY MESSAGES

Accounts

The financial statements for 2000/2001 had to be prepared to tight timescales and have to comply with an accounting regime which is fundamentally different from that which had been applicable to the MPS in the past. Given that, the production of the financial statements in a timely manner this year is a considerable achievement.

We expect to conclude our audit of the MPA's financial statements by 31 December 2001. At present, we are minded to qualify our opinion on these statements because of reservations about the adequacy of the provisions set aside to meet third party and police pension liabilities.

Financial aspects of corporate governance

Financial standing

The Authority's financial position is precarious and is of great concern. The current weaknesses in budgetary control arrangements reinforce the need to build up sufficient balances to meet unforeseen needs. Cultural change initiatives that support local accountability and financial control will be essential pre-requisites to driving forward the improvement agenda. The budget round for 2002/2003 will be very difficult and hard decisions about levels of service will need to be taken.

Systems of internal financial control

We recognise the efforts being made to strengthen the finance function within the MPA/MPS. At present, the systems of internal financial control still require significant improvement and leave the MPA/MPS vulnerable to criticism and potential loss.

Performance management

Best Value Performance Plan

Our opinion on the Best Value Performance Plan (BVPP) was qualified due to the omission of certain required performance information. However, the MPA have demonstrated a strong commitment to Best Value and good progress has been made towards developing a performance management framework. The challenge now is to turn these foundations into a review programme that delivers continual service improvements.

Use of Resources

We have assessed the MPA/MPS's management arrangements for ensuring the effective use of resources across a range of activities. They demonstrate good practice in a number of the areas we have looked at. These tend to be discrete areas where teams focus specifically on certain objectives, for example, the management of early retirement or supporting cases going to

employment tribunals. Where organisation wide policy action is required, the results can be inconsistent, for example on the management of overtime, with a resultant failure to gain the available benefits. Efforts need to be continued, to secure greater consistency in applying good practice across the organisation.

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Accounts

- Opinion

The financial statements for 2000/2001 had to be prepared to tight timescales and have to comply with an accounting regime which is fundamentally different from that which had been applicable to the MPS in the past. Given that, the production of the financial statements in a timely manner this year is a considerable achievement.

We expect to conclude our audit of the MPA's financial statements by 31 December 2001. At present, we are minded to qualify our opinion on these statements because of reservations about the adequacy of the provisions set aside to meet third party and police pension liabilities.

The accounts presented for audit were of a generally good standard and were substantially compliant with required accounting practice. They were underpinned by the structured and thorough approach taken to the establishment of the MPA's opening balance sheet. The production of the accounts to the required timetable was a significant achievement, particularly given that they had to comply with the local government accounting regime which is fundamentally different to that which was applied to the MPS in the past. This reflects well on the commitment and professionalism of the staff involved.

There are though a number of areas where improvements are required. The accounts did not comply with the CIPFA Best Value Accounting Code of Practice or with the new accounting standard on charging for the depreciation of fixed assets. These matters, together with the need to account more transparently for pensions, will have to be resolved for 2001/2002.

Our audit fieldwork is now largely complete and we expect to conclude our opinion audit by 31 December 2001. To date two key issues have arisen:

- there is currently no provision made against the third party liabilities carried by the MPA at 31 March 2001. The amounts involved cannot yet be quantified with any degree of precision but are likely to be significant
- the accounts contain an earmarked reserve of £8m in respect of police pension liabilities for officers over the age of 50 who can retire with one months notice. However, at 31 March 2001, the potential pension liability for these officers stood at £44m.

We recognise that the requirements to establish these provisions are new to the MPA. We also appreciate that arrangements are in hand to address the issue of third party liabilities for the future. However, given their magnitude, we are minded to qualify the MPA's financial statements with regard to inadequate provisions for third party and police pension liabilities.

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Financial aspects of corporate governance

We have considered the arrangements in place in the following areas:

- Financial standing
- Systems of internal financial control
- Legality of financial transactions
- Standards of financial conduct and the prevention and detection of fraud and corruption

Financial standing

The Authority's financial position is precarious and is of great concern. The current weaknesses in budgetary control arrangements reinforce the need to build up sufficient balances to meet unforeseen needs. Cultural change initiatives that support local accountability and financial control will be essential pre-requisites to driving forward

the improvement agenda. The budget round for 2002/2003 will be very difficult and hard decisions about levels of service will need to be taken.

General Fund net expenditure for the 2000/2001 financial year (9 months) was £7.9m (0.5%) higher than the total budget. The main causes of the overspend were police overtime and spending on operational supplies and services. To fund this, a transfer from the general reserve was required. This reserve stood at only £13.5 million (0.7% of budget or the equivalent of just 3 days total expenditure) at 31 March 2001, which is below the 1% minimum approved by the Authority in November 2000. The Authority must take action to ensure that future plans and budgets allow for a prudent level of reserves. The volatility of the budget and the difficulties experienced in controlling it makes this more essential than would be the case in organisations with more effective budgetary control systems.

The events of 11 September 2001 have placed further pressure on the already stretched resources of the MPA. There remains an uncertainty over whether or not the Government will provide sufficient additional resources to fully support the increased emphasis on anti-terrorism work. Until this is decided, the Treasurer of the MPA will need to have regard to the statutory responsibilities he has and advise the MPA accordingly as to the effects on the budget position for 2001/2002. Even before taking into account these matters, an overspend of some £13m had been identified on the basis of the first six months of the year. A number of corrective actions have been authorised to contain these pressures but these will have to be monitored carefully to ensure that planned savings are achieved.

We have already made reference to our concerns about inadequate provisions for pension liabilities. Net expenditure on police pensions was £202m in the 9 month year, representing 14% of net operating expenditure. As previously outlined the commuted pensions reserve stands at only £8m, compared with a potential liability of around £44m for officers over 50 who can retire with one months notice. This liability is likely to rise further in the next few years.

The phased implementation of the new accounting standard FRS17 will require fuller disclosure of the assets and liabilities relating to pensions than has previously been the case. It is likely that this will put further pressure on the overall financial position of the MPA/MPS, as the standard clarifies a number of issues that have previously been the subject of debate, including the need to accrue fully for pension liabilities.

Given the matters outlined above, decisions on the 2002/2003 budget and service levels will be very difficult. Concerted efforts by all of those involved with policing in London will be required if the MPA's financial health position is to be brought on to an even keel. Unless this is done longer term planning will be jeopardised. Members will also need to ensure that proactive steps are taken to move the culture of the organisation towards one which places greater emphasis on financial and budgetary management and control.

Systems of internal financial control

We recognise the efforts being made to strengthen the finance function within the MPA/MPS. At present, the systems of internal financial control still require significant improvement and leave the MPA/MPS vulnerable to criticism and potential loss.

Wherever possible we rely on Internal Audit to avoid duplication of effort where responsibilities overlap. To form a judgement on the extent to which we could rely on them, we undertook a detailed assessment of Internal Audit's performance against the standards set out in CIPFA's Code of Practice.

We identified some areas for improvement but we concluded that reliance could be placed on the work of Internal Audit. They have demonstrated a number of strengths in their approach but need to improve on the speed with which they deliver their work and focus more on the resources they consume in delivering audit products.

We also found evidence that management responses to Internal Audit recommendations are sometimes slow. Unless this is corrected, the full benefits of the work could be lost. The MPA should establish a mechanism by which progress on recommendations can be followed up.

We reviewed the key systems which underpin the integrity of the MPA/MPS's financial affairs. We concluded that the system of internal financial control was adequate to cover some, but not all, of the key financial risks faced by the organisation. In particular, significant weaknesses persist in respect of controls over billed income and the management of suspense accounts.

Our principal concern is the lack of high level controls, such as detailed budget reports and system reconciliations, on which management can rely on to gain assurance on the effective operation of the key financial systems. In their absence management rely solely on the effective operation of preventative controls, such as multiple authorisation of invoices, with a resultant higher level of bureaucracy. This means that senior management cannot provide assurance that all key risks are being covered. This is also partly due to a scarcity of financial skills. We welcome the significant investment being made in additional finance staff to overcome this shortfall.

Internal Audit recently reported to the Finance, Planning and Best Value Committee on the control frameworks that need to be in place to allow the effective management of major contracts. This was in response to concerns that exist around a number of existing contracts. Our work in this area has found that the problems are often caused by failures at the contract letting stage. Work is in hand to strengthen arrangements at the MPS in this area, but it will be some time before the effects are seen.

We also undertook an assessment of the overall IT control environment. The MPS is implementing a number of significant initiatives across the whole organisation designed to strengthen its infrastructure. These will absorb significant staff and other resources and will require stronger programme management than has existed in the past, to ensure that they are delivered successfully.

Work is also underway in the MPS to improve co-ordination and control over the significant investment being made in IT. A single more robust network is intended and this is expected to provide improved value for money from IT. Effective delivery will require the MPS to establish and implement the right balance between

standardisation across the organisation and the specific needs of the end users. Much remains to be done to demonstrate the business benefits of the investment being made.

Legality of financial transactions

The Authority's arrangements for ensuring the legality of transactions with financial consequences are developing.

We reviewed the overall arrangements for ensuring the legality of transactions and did not identify any areas of major concern. During the year, we also liaised with the Monitoring Officer (MO) and the MPS legal team. There is a need for the arrangements concerning liaison between the MO and the MPS legal team to be clarified. These currently rely on developing networks rather than established corporate protocols. Furthermore, the role of the MO is not yet fully understood across the whole of the organisation.

Reports to Members do not at present always indicate whether the proposed actions have any legal or human resource implications. Such advice should be included in all reports to safeguard the MPA's position. In addition, in all cases where there is uncertainty regarding the legal basis of transactions, staff in the MPA and MPS should seek legal advice and if necessary, additional external advice, as appropriate.

This year's audit included specific consideration of the steps taken to address the legislative requirements of the Human Rights Act 1998. We found that good progress had been made although there is a need to consider the obligations the MPA/MPS needs to place on its contractors to ensure their compliance with the Act.

We have also considered the approach taken to two PFI schemes this year. On the basis of our work and the representations made by the MPS's external legal and financial advisors, we are satisfied that the approach adopted and the conclusions reached by the MPA, in determining if the schemes were lawful and compliant with the capital finance regime, were appropriate.

Standards of financial conduct and the prevention and detection of fraud and corruption

Arrangements for maintaining standards of conduct, and for preventing and detecting fraud and corruption, are improving.

We undertook an overall assessment of the Authority's arrangements to maintain standards of conduct and prevent and detect fraud and corruption. On the basis of this work, we concluded that arrangements are generally satisfactory although improvements are required in some areas. The introduction of the Standards Committee should assist in strengthening these arrangements.

The 'Right Line' initiative allows people to raise concerns both from inside and outside the organisation. Further work is due to be undertaken to ensure that these arrangements comply with the requirements of the Public Interest Disclosure Act.

Internal Audit undertake a number of initiatives designed to raise the profile of anti-fraud measures. For instance, the issue of fraud 'warning bulletins' to key staff is good practice. Nevertheless, there remains the need for a global MPA anti-fraud and corruption policy to be introduced which clearly documents and publicises the activities currently in hand. Such a policy could usefully assist in improving awareness of the risks in this area, which have, for example, been highlighted by the contract letting and management problems mentioned earlier in this Letter.

Our work found no evidence of impropriety but the MPA/MPS need to improve the level of control exercised over the receipt of gifts and hospitality and declarations of pecuniary interests. In particular, a formal and up to date policy needs to be put in place and Members made aware of it to ensure that the recording of gifts and hospitality is improved.

Performance management

We considered:

- Best Value Performance Plan
- Performance information
- Use of resources

Best Value Performance Plan

Our opinion on the Best Value Performance Plan (BVPP) was qualified due to the omission of certain required performance information. However, the MPA have demonstrated a strong commitment to Best Value and good progress has been made towards developing a performance management framework. The challenge now is to turn these foundations into a review programme that delivers continual service improvements.

The 2001/2002 BVPP was a well presented and useful document. The Authority's Best Value agenda now needs to be fully integrated across the whole organisation and moved forward with vigour, to ensure that tangible service improvements are secured.

The statutory audit report issued on 29 June 2001, included an opinion which was qualified on an 'except for' basis, as not all of the performance information required for 2000/01 was included in the BVPP. We also made a number of statutory recommendations which required a formal Authority response. The MPA responded promptly and positively to our report and produced a detailed action plan within the statutory timetable.

A framework for Best Value is in place and is continuing to develop. However, the culture of continuous service improvement required by Best Value has not yet been universally integrated into management arrangements across the organisation. At this stage, Best Value is still seen as a task outside everyday management responsibilities.

Progress has been made in enhancing performance management arrangements by extending the MPS's performance management framework to all business groups. During the coming year, the MPA/MPS will need to

demonstrate that this initiative has moved beyond implementing a process and on to achieving visible improvements in line with corporate priorities.

While we recognise that most reviews in the programme are complex, progress in completing reviews and implementation of plans has nevertheless been relatively slow. Now that the development of the Best Value framework is largely complete, there is a need to focus on delivering reviews, within acceptable timescales, and securing tangible performance improvements and outcomes.

Performance information

There was no requirement to certify the Authority's Audit Commission performance indicators this year. In previous years these indicators were certified separately, they now form a part of the annual work on the BVPP.

Use of resources

We have assessed the MPA/MPS's management arrangements for ensuring the effective use of resources across a range of activities. They demonstrate good practice in a number of the areas we have looked at. These tend to be discrete areas where teams focus specifically on certain objectives, for example, the management of early retirement or supporting cases going to employment tribunals. Where organisation wide policy action is required, the results can be inconsistent, for example on the management of overtime, with a resultant failure to gain the available benefits. Efforts need to be continued, to secure greater consistency in applying good practice across the organisation.

We have undertaken a range of reviews, the most important being those covering service and financial planning and overtime. The key messages from our work are summarised in the following exhibit.

EXHIBIT 2

Key findings from our work are outlined below

Service reviewed/key findings	Further action
<p>Service and financial planning</p> <p>Effective corporate planning arrangements will be crucial to securing performance improvements. The MPA has clearly recognised the need to develop a longer term corporate strategy. The recent paper to the Finance, Planning and Best Value Committee outlines initiatives currently underway in this area.</p>	<p>As medium term financial planning develops it will need to be become more clearly linked with corporate priorities and operational plans. This will be a vital part of the process of ensuring appropriate accountabilities. Refining the planning cycle and effectively linking work done by the MPA and the MPS will be critical to the success of these initiatives.</p>
<p>Overtime</p> <p>Some £95m is spent annually by the MPS on police overtime. Our work has found the way in which overtime is managed can vary across the organisation. In many cases accountability does not lie with those taking decisions on overtime.</p>	<p>There is a clear need to ensure that the good practices found in some areas are spread across the whole organisation. Accountability for overtime needs to be addressed in the devolution pilots that are due to be launched. The ability of officers to operate effectively over a long period of overtime working also needs to be considered as do disincentives to promotion, caused by significant levels of regular overtime payments. We welcome the MPS review of the highest overtime earners currently underway.</p>
<p>Employment tribunals</p> <p>Our overall conclusion is that cases that go to tribunal are generally managed well and demonstrate a number of good practices.</p>	<p>There has been an increase in the number of tribunal cases arising in recent years. The way staff are managed is a key factor in reversing this trend. There is a need for further performance management training to ensure a consistent approach across the organisation.</p>

Service reviewed/key findings	Further action
<p>Estate management</p> <p>The MPA has developed an estates strategy which links to a number of service strategies. Significant investment in the property portfolio is required.</p>	<p>Communication between the property services group and operational managers needs to be improved to ensure that corporate priorities are reflected effectively at local level and incentivised. Work should also be undertaken to assess how feedback from the public can be better used to ensure that the portfolio matches public needs.</p>
<p>Internal consultancy</p> <p>Some £2m is spent annually on the MPS internal consultancy group. It is clearly well run but does not have a properly defined role at present.</p>	<p>The way in which work is commissioned from the group needs to be clearly set out to help clarify its role. This will allow the team to operate on either a proactive risk based approach or to truly function as an internal consultancy via a trading account. Either route would allow the team to better demonstrate how it adds value to the MPS. We understand work to clarify the role is currently in hand.</p>
<p>Early medical retirements</p> <p>Generally effective arrangements are in place and this is reflected in the fact that the HMIC's good practice target of only 33% or less of all retirements being medical, is being achieved.</p>	<p>We have made a number of recommendations to improve the process further and secure additional improvements. Most importantly, the MPS needs to ensure that a consistent approach is applied across the organisation.</p>

Community safety follow-up

During the 1998 and 1999 audits, auditors reviewed how the MPS were working with key partner agencies to promote community safety at Borough level. A summary report was produced setting out the key issues for the MPS to address. This year we have undertaken a follow-up review to assess the progress made in moving from

community safety strategies to implementation. We found that progress had been made in implementing our recommendations. The MPS has helped to ensure improvements in partnership working at the BOCU level. However, a small number of partnerships are still not functioning effectively and action is needed to address this. In addition, efforts to 'mainstream' compliance with the legislation should continue.

The Efficiency Plan

We reviewed the outturn cashable savings that the Authority identified as efficiency gains for the 2000/2001 Efficiency Plan. This was to support HMIC's assessment of the Plan. We fed back our findings to HMIC, which subsequently certified that the Authority had achieved its efficiency target for the year.

Future audit work

We are currently considering the significant operational and financial risks that face the MPA/MPS that will need to be addressed in next year's audit.

We will discuss our risk assessment with Members and officers before producing an audit plan.

Closing remarks

Members may wish to note that Regulation 16A of the Accounts and Audit Regulations require the MPA to:

- publish the AAL as soon as is practicable following receipt
- keep copies available for purchase by any person on payment of such sum as the MPA may reasonably require.

Finally, I would like to take this opportunity to express my appreciation for the assistance received from officers during the course of our work. Our aim is to provide a high standard of audit service that makes a practical and positive contribution to the work of the MPA/MPS. We recognise the value of your co-operation and support.

Kash Pandya
District Auditor

Date: 19 December 2001

Reports issued during the audit

Best Value report (June 2001)

IT Risks report (July 2001)

Financial systems report (July 2001)

Review of Internal Audit (August 2001)

'Regular as Clockwork' report (September 2001)

Community safety follow-up (September 2001)

Early medical retirement (September 2001)

Employment tribunals (October 2001)

Internal consultancy (November 2001)

Estate management (November 2001)

Client side management (December 2001)

Service and financial planning (December 2001)

Review of overtime (December 2001)