

Annual Audit Letter

December 2006



# **Annual Audit Letter**

**Metropolitan Police Authority**

**Audit 2005-2006**

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- auditors are appointed independently from the bodies being audited;
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# Introduction

## The purpose of this letter

- 1 The purpose of this annual audit letter (letter) is to summarise the key issues arising from the work that we have carried out during 2006. Although this letter is addressed to the members of the Metropolitan Police Authority (MPA), it is also intended to communicate the significant issues we have identified, in an accessible style, to key external stakeholders, including members of the public. The letter will be published on the Audit Commission website at [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk).
- 2 This letter has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. This is available from [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk).

## The responsibilities of the auditor and the MPA

- 3 The MPA is an independent statutory body, established under The Greater London Authority Act 1999. The MPA provides a regime of local democratic accountability for policing in London through its role to scrutinise and support the work of the Metropolitan Police Service (MPS). Amongst a number of key tasks, the MPA is accountable for the management of the police budget, although the Commissioner of the MPS retains operational responsibility for all aspects of policing in London.
- 4 We have been appointed as the MPA's independent external auditors by the Audit Commission, the body responsible for appointing auditors to local public bodies in England, including police authorities. As the MPA's external auditors, we have a broad remit covering financial and governance matters. We target our work on areas which involve significant amounts of public money and on the basis of our assessment of the key risks to the MPA achieving its objectives. It is the responsibility of the MPA to ensure that proper arrangements are in place for the conduct of its business and that public money is safeguarded and properly accounted for. We have considered how the MPA is fulfilling these responsibilities. In undertaking our work, we liaise closely with Her Majesty's Inspectorate of Constabulary (HMIC).

## The scope of our work

- 5 Our main responsibility as your appointed auditor is to plan and carry out an audit that meets the requirements of the Audit Commission's Code of Audit Practice (the Code). Under the Code, we are required to review and report on:
  - the MPA's accounts; and
  - whether the MPA has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.
- 6 This letter summarises the significant issues arising from both these areas of work and highlights the key recommendations that we consider should be addressed by the MPA. A list of all reports issued to the MPA in relation to the 2005/06 audit is provided in the closing remarks section of this letter.

## Key messages

- 7 The MPA and the MPS have faced another challenging year. 2006 has seen encouraging progress on a number of fronts. Headline policing performance has improved, with an overall reduction in crime in the capital, while the Safer Neighbourhoods programme has now established local policing in every ward in London. In the face of the continuing operational demands, including counter-terrorism, these successes are impressive. Some significant challenges, however, remain, in particular to improve the systems of control, governance arrangements and behaviours that support the delivery of value for money police services. In addition, in the shorter term, the MPA's hard-won financial stability remains under threat from increasing financial pressures. Corporate focus also needs to be maintained on delivering the modernisation programme that will underpin the delivery of the MPA's and MPS' medium-to-longer term ambitions.
- 8 The following matters should be considered by members.

**Table 1 Conclusions and recommendations**

Area	Conclusions	Recommended action
<b>Accounts</b>		
Opinion	We issued an unqualified audit opinion on 29 September 2006.	Improve fixed asset accounting arrangements. Enhance the arrangements for quality assuring the draft accounts.
<b>Performance</b>		
Direction of travel	The MPA continues to develop its capacity to sustain future improvement.	Ensure that the implementation plan for the MPA's organisational development programme is resourced appropriately and includes clear milestones to allow progress to be monitored.
Police performance assessment (incorporating HMIC's baseline assessment)	The assessment of police performance shows a broadly positive picture, with improved performance in most areas.	Address the areas for improvement identified by HMIC.

Area	Conclusions	Recommended action
<b>Use of resources</b>		
Value for money conclusion	We issued our value for money conclusion on 29 September 2006, concluding that the MPA had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources, except for putting in place arrangements to maintain a sound system of internal control.	Address required improvements in systems of internal control. Regularise the procurement process for the provision of Safer Neighbourhoods' estates, including demonstrating value for money. Embed the principles of good governance throughout the MPA and the MPS.
Police use of resources evaluation (PURE)	The MPA is performing adequately.	Implement action to improve the MPA/MPS's use of resources, in particular by aligning service and financial planning, embedding risk management and mainstreaming value for money.
Financial standing	The MPA successfully managed significant financial pressures to deliver a balanced outturn in 2005/06, although financial pressures are mounting.	Continue to protect the MPA's financial position through robust budget setting, monitoring and action to address emerging overspending.
Best value	We issued an unqualified auditor's report on the MPA's 2006/07 Best Value Performance Plan on 30 November 2006.	None.
Other use of resources work	Our work has identified a range of good practice and opportunities for improvement.	Continue to develop performance management processes so that linkages between corporate priorities and service plans are embedded throughout the organisation. Maintain the momentum on delivering improvements in crime data quality and activity based costing.

## Accounts

- 9 The MPA's arrangements for the production of draft accounts have shown improvements over recent years, and this was sustained in 2005/06. The draft accounts were presented for audit to the agreed timetable and were supported by a thorough set of working papers. However, further improvements are required. Our annual governance report, presented to the Corporate Governance Committee on 22 September 2006, drew a number of significant issues to members' attention arising from the audit of the accounts, although none affected the reported surplus for the year. In particular, four material amendments were agreed with officers in order to:
- recognise the pension fund £1.4b actuarial loss for 2005/06 within the statement of total movement of reserves;
  - transfer £101m of assets brought into use from non-operational to operational assets;
  - amend the disclosure of accumulated depreciation, with a net effect of £57m; and
  - transfer £45m from deferred government grants to recognise the application of grant monies for assets brought into use.
- 10 A number of these amendments reflect weaknesses in the controls for accounting for fixed assets. These control weaknesses were reported in the MPA's Statement on Internal Control. A steering group has been established to address the issues raised. This will be particularly important if the MPA is to develop fit for purpose fixed asset accounting arrangements in advance of the introduction of the more onerous accounting requirements proposed in the 2007 SORP. We will review the MPA's progress in developing its capital accounting arrangements as part of the 2006/07 audit.
- 11 Following these amendments, we were able to issue an unqualified opinion on the accounts on 29 September 2006. We were not, however, able to certify completion of the audit because of the MPA's ongoing enquiries into estates procurement matters. This issue is considered further in the use of resources section of this letter.

<b><i>Recommendations</i></b>
<i>R1 Improve fixed asset accounting arrangements.</i>
<i>R2 Enhance the arrangements for quality assuring the draft accounts.</i>



## Performance

- 12 We have followed up the results of the Initial Performance Assessment (IPA) of the MPA completed in 2004. We did this via a 'direction of travel' assessment, based on the 2006 local government approach, but tailored individually to the context of the MPA.
- 13 We also comment in this section on the results of the Home Office police performance assessment of the MPS, including HMIC's baseline assessment.

## Direction of travel

- 14 The MPA continues to develop its capacity to sustain future improvement. The MPA has integrated its strategic planning with the MPS and its strategic oversight role is being strengthened to achieve a closer focus on key issues. Joint working with the MPS has helped to identify areas for improvement and plans to address them. The MPA is seeking to integrate financial plans with the policing plan, but more work is needed to integrate the monitoring of finance, performance and activity information. The Authority is restructuring to improve its outward focus and its engagement with the London boroughs, other partners and the public. The joint community engagement strategy, approved in September 2006, sets out a clear and structured approach to identifying and meeting the needs of the community.
- 15 Improvement is being underpinned by a considerable programme of organisational development. The MPA is moving into the implementation phase of that programme, although there has been some slippage to date and the pace of change now needs to be increased. The introduction of the new performance management framework and the programme to equip the MPA with the skills and competences in its new leadership model will be important elements in achieving the desired changes in culture and behaviour. Further progress is necessary to improve action planning and monitoring in respect of internal reviews such as those for the organisational development programme. The MPA's human resources (HR) service has been reviewed and capacity is being built, but the MPA is not yet benefiting from a strategic approach to HR. Establishing a training and development programme for members will also enhance the MPA's capacity to meet its obligations.

### **Recommendation**

*R3 Ensure that the implementation plan for the MPA's organisational development programme is resourced appropriately and includes clear milestones to allow progress to be monitored.*

## Police performance assessment

- 16 The assessment of the MPS, published in October 2006, shows a broadly positive picture, with improved performance in most areas.

**Table 2 Police performance assessment**

Performance areas	Delivery	Direction
Reducing crime	Fair	Stable
Investigating crime	Good	Improving
Promoting safety	Fair	Improving
Providing assistance	Good	Improving
Citizen focus	Fair	Improving
Resource use	Good	Improving
Local policing	Excellent	Improving

*Source: Home Office*

- 17 Overall, the MPS fared well on HMIC's baseline assessment, scoring three excellent, 12 good and eight fair ratings, with improvements in reducing volume crime, forensic management and reducing anti-social behaviour. HMIC highlighted a number of successes:
- the response to the 7 July terrorist attacks drew widespread praise, deterred further terrorist activity and reassured the public. The MPS' functions on a broad range of counter terrorist and related security matters are discharged to a standard that is held in high regard within the policing world;
  - the Safer Neighbourhoods programme has now established teams in every ward in London, and is reaping important dividends in terms of crime reduction, as well as increased public confidence;
  - the specialist crime directorate disrupted over 61 identified organised criminal networks during 2005/06, 11 more than the MPS target; and
  - the final set of corporate values and underpinning behaviours approved in February 2006 form an integral part of the Policing London Strategy 2006–2009, and will be a key enabler for the MPS to deliver its strategic outcomes and performance ambitions.

18 HMIC also identified a number of challenges ahead:

- the MPS has developed a coherent strategy to enhance community engagement in tackling terrorism. This will need a sophisticated approach to implementation;
- despite an overall reduction in volume crime in 2005/06, robbery rose by about 16 per cent compared with the previous year;
- given the scale of the corporate ambition over the next three to four years, against a background of a significantly tougher resource environment, the MPS needs to do even more to maximise the delivery of value for money; and
- the MPS has to plan for not only the 60 day period of the 2012 Olympics, but also for the pre-event construction period, which is already generating policing issues and incidents, as well as the legacy issues that will result from London hosting the Games.

***Recommendation***

*R4 Address the areas for improvement identified by HMIC.*

## Use of resources

- 19 We are required to issue a conclusion on whether we are satisfied that the MPA has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the value for money conclusion.
- 20 We are also required to assess how well police authorities manage and use their financial resources by providing scored judgements on the MPA's arrangements in five specific areas. This is known as the Police Use of Resources Evaluation (PURE).

## Value for money conclusion

- 21 We concluded that the MPA had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources, except for putting in place arrangements to maintain a sound system of internal control. This reflects a number of examples of control weaknesses arising during the year that were included in the Director of Internal Audit's annual report and were reported in the MPA's Statement on Internal Control.
- 22 Our detailed findings were set out in the annual governance report presented to the Corporate Governance Committee on 22 September 2006. This drew on the findings of our PURE work reported below. We in particular commented that the MPA has not yet established adequate arrangements for internal control. The assurance framework that supports the Statement on Internal Control is also yet to be fully embedded into the MPA's business processes. As a result, whilst standing orders, standing financial instructions and a scheme of delegation are all in place and have been approved by members, this has not prevented occurrences where significant expenditure has been made outside delegated limits. We therefore recommended as a priority that the MPA implement action plans to address the internal control weaknesses identified in the Statement on Internal Control.

<b><i>Recommendation</i></b>
<i>R5 Address required improvements in systems of internal control.</i>

- 23 The arrangements adopted for the provision of Safer Neighbourhoods' estates were reflected in our conclusion on internal control. Internal audit work is ongoing and will be reported separately to members, but the MPA accepts that key aspects of the procurement process did not accord with standing orders or with EC procurement directives. While the accelerated programme - to provide patrol bases for the Safer Neighbourhoods' teams in every ward in London - remains on course for delivery, the overall value for money from the procurement process adopted has yet to be demonstrated. It is apparent that the MPA's governance structures and procedures have taken second place to the operational policing imperative (in this case, to deliver the estates' programme), a recurring theme in recent years which will be familiar to members. This approach poses significant risks to the MPA's governance.

<b>Recommendations</b>
<i>R6 Regularise the procurement process for the provision of Safer Neighbourhoods' estates, including demonstrating value for money.</i>
<i>R7 Embed the principles of good governance throughout the MPA and the MPS.</i>

## Police Use of Resources Evaluation

- 24 This is the second year we have carried out a use of resources assessment. In 2005, we completed an indicative assessment of four areas (financial reporting, financial management, financial standing and internal control). Our approach for 2006 focused on building on this work and updating it for any changes and improvements to the MPA's arrangements. For the first time, we also completed an assessment of a fifth area, value for money. This year's work was undertaken as part of the national PURE approach.
- 25 Each area was scored from 1 to 4 (1= below minimum requirements, 2 = adequate performance, 3 = performing well and 4 = performing strongly). These scores were converted by the Audit Commission into an overall use of resources score. The MPA was assessed as level 2, performing adequately, that is at minimum requirements.
- 26 The area scores and the overall score are set out in Table 3 below. Our assessments this year were made available to HMIC to inform its baseline assessment.

**Table 3**    **PURE results**

<b>Area</b>	<b>Score</b>	<b>Key recommendations</b>
Financial reporting	2	<p>Ensure that the draft accounts are free from material misstatements.</p> <p>Incorporate the needs of a range of stakeholders into the publication of the summary accounts and the annual report.</p>
Financial management	2	<p>Embed processes so that MPS and MPA business planning drives the medium term financial strategy (MTFS) and resource allocations.</p> <p>Develop further links between the MTFS and corporate objectives.</p> <p>Improve the management of the asset base and IM&amp;T service.</p>
Financial standing	3	<p>Improve arrangements for managing overspending budgets.</p> <p>Document the changing risks and needs that underpin the reserves policy.</p>
Internal control	2	<p>Establish a robust system of internal control.</p> <p>Embed fully risk management arrangements.</p> <p>Document key systems and procedures.</p> <p>Ensure that business continuity plans are in place across all OCUs.</p> <p>Ensure that all OCUs have registers of interests, gifts and hospitality in place and these are regularly reviewed.</p>
Value for money	2	<p>Deliver the managerial and cultural changes necessary to mainstream value for money effectively within the MPS.</p> <p>Evidence the delivery of improved outcomes from the efficiency plan and modernisation programme in terms of reduced costs or improved quality within existing costs.</p>
Overall	2	

**Recommendation**

*R8 Implement action to improve the MPA/MPS's use of resources, in particular by aligning service and financial planning, embedding risk management and mainstreaming value for money.*

## Financial position

- 27 As in previous years, the MPA successfully managed significant financial pressures to deliver a balanced outturn in 2005/06. Net revenue spending was £2.7b, £7m less than the original budget. This underspend was transferred to a number of earmarked reserves.
- 28 The outturn included a number of significant under and overspends within individual budgets. Once again, the principal area of overspending was in police officer and staff overtime payments (£38.7m over budget). Around £23m of these overspends were attributable to the July 2005 bombings, and were mitigated to some extent by underspends on other pay budgets. Nevertheless, the risks that this situation presents to the MPA's control over spending are now familiar to members. Further scrutiny of overtime will remain a priority.
- 29 The Treasurer has indicated that, looking to the medium term, the general revenue balance should be increased in the range 1.5 to two per cent when conditions permit, this being in the Treasurer's view the minimum necessary to protect the MPA against the unplanned financial demands which inevitably arise. The general revenue balance had increased to £28.8 million at 31 March 2006. Looking to 2006/07, the Authority agreed a new uncommitted reserve of £20.1m in June 2006, the emergencies/contingencies fund. Taken together, these reserves represent 1.7 per cent of net revenue expenditure, in line with the revised policy. In the medium term, the Authority's ambition remains to increase this percentage nearer to the two per cent figure.
- 30 Unplanned demands continue to be a feature of spending in 2006/07, as most recently reported to members in November 2006. The costs of specific counter-terrorist operations remain significant, and the Treasurer is currently forecasting a net overspend of £35.4m in 2006/07, including £23.7m of estimated costs related to Operation Overt (investigations into the alleged plot to smuggle explosives onto aircraft). Overspending on police officer overtime (£10.9m) and the forensics budget (£10.0m) is prevalent once again. Actions have been identified by the business groups to reduce expenditure into line with the budget. Members have also agreed an approach to managing the additional unbudgeted costs of Overt, based on minimising spending, seeking additional government funding and, potentially, utilising existing reserves. For its part, the MPS is considering a planned strategy to deliver a managed underspend across existing budgets, possibly over a two year period.

- 31 Further financial pressures have been identified in planning beyond the current year, flowing from a number of strategic risks:
- protecting the capital against further acts of terrorism;
  - completing delivery of the Safer Neighbourhoods programme, while accommodating the reduced funding stream available;
  - preparing to police the Olympics 2012;
  - implementing the four major programmes of change that will be pursued as part of the modernisation programme; and
  - meeting the Mayor's requirement to submit a balanced budget contained within the specified precept increase.
- 32 Members will need to balance these competing priorities, while ensuring that the MPA maintains its controls over spending, if financial stability is to be maintained.

**Recommendation**

*R9 Continue to protect the MPA's financial position through robust budget setting, monitoring and action to address emerging overspending.*

## Best Value Performance Plan

- 33 We issued an unqualified auditor's report on the MPA's 2006/07 Best Value Performance Plan on 30 November 2006.

## Other use of resources work

- 34 Our value for money conclusion has also been informed by a number of pieces of work completed in 2006, as set out in Table 4 below.

**Table 4 Other use of resources work**

Review	Key conclusions
Information and systems strategy	The current family of information strategies do not link clearly to the MPS' policing priorities, and there is recognition that the strategies require revision. Revised strategies will need to show more clearly how information and information systems support the delivery of corporate objectives.



Review	Key conclusions
ICT service delivery	The new contract should support users by ensuring that system failures are addressed appropriately and systems restored as quickly as possible, whilst reducing the number of similar recurring incidents. A comprehensive suite of performance measures is defined, although change management is only partially addressed.
The Bichard inquiry	The MPS has made good progress in complying with the Bichard recommendations. The Police Local Exchange system has been implemented successfully. Progress is being made towards the solution of a national IT system.
Aspects of performance management	The corporate strategy was formally adopted in February 2006. Clear priorities were set following high level consultation with a range of stakeholders across London. Work is underway to develop the golden thread of cascaded performance information through an embedded performance management framework, which links corporate priorities through service plans to the individual. This needs to be completed before the full benefits of the performance management framework can be realised.

### **Recommendation**

*R10 Continue to develop performance management processes so that linkages between corporate priorities and service plans are embedded throughout the organisation.*

### **Crime data quality**

- 35** As part of the Audit Commission's three-year national study to review crime recording in all police authorities and forces, in partnership with the Police Standards Unit (PSU) of the Home Office, we reviewed the arrangements for producing the key police performance data used in the Police Performance Assessment Framework.
- 36** We assessed data quality as 'good' and the crime recording arrangements as 'fair'. This is a significant improvement on the results achieved in 2004/05, and testifies to the MPA's and MPS' positive response since receiving a 'red' rating for data quality in 2004. There is now a clear commitment to achieving National Crime Recording Standard (NCRS) compliance. The profile of NCRS has been raised at corporate senior management and Borough Command Unit (BCU) first line supervision level. There is a greater knowledge of NCRS amongst operational staff, which has contributed to widespread improvements in compliance levels.

- 37 Improvements can, however, still be made. The MPA and MPS agreed an action plan of recommendations contained within our report, and we will consider the progress made during the 2006/07 audit.

### **Activity based costing**

- 38 On behalf of the Home Office, we undertook a review of the MPA's systems to produce accurate activity based costing (ABC) data and also the arrangements in place to use this data as part of its decision-making framework.
- 39 We assessed both the quality of the data submission and the management arrangements as 'fair'. We identified some significant improvements at the corporate level in 2005/06, although there were still areas where improvement was required. While there is no similar mandatory review required in 2006/07, we will monitor progress in implementing agreed recommendations as part of a wider data quality audit.

<b><i>Recommendation</i></b>
<i>R11 Maintain the momentum on delivering improvements in crime data quality and activity based costing.</i>

## Closing remarks

- 40 This letter has been discussed and agreed with the Chief Executive and Treasurer of the MPA and the Interim Director of Resources of the MPS. A copy of the letter will be presented to the Corporate Governance Committee on 15 December 2006 and copies will be provided to members.
- 41 Detailed findings, conclusions and recommendations on the areas covered by our audit are included in the reports issued to the MPA during the year. These are listed in the following table.

**Table 5 Reporting 2005/06**

<b>Report</b>	<b>Actual date of issue</b>
Audit plan	July 2005
Information and systems strategy	April 2006
Crime data quality	May 2006
Activity based costing	May 2006
ICT service delivery	June 2006
Interim report	June 2006
PURE interim report	July 2006
The Bichard inquiry	September 2006
Annual governance report	September 2006
Audit opinion	September 2006
Value for money conclusion	September 2006
PURE final report	November 2006
Opinion on the Best Value Performance Plan	November 2006
Annual audit letter	December 2006

- 42 Finally, I would like to take this opportunity to thank the MPA and the MPS for their assistance and co-operation during the course of the audit.

**Michael Haworth-Maden**

**District Auditor**

December 2006