Financial Auditing and Reporting: 2002 - 2003

General Report by the Comptroller and Auditor General for Northern Ireland

Presented pursuant to sections 10(4) and 11(3)(c) of the Government Resources and Accounts Act (NI) 2001.

Ordered by the House of Commons *to be printed* 24th June 2004

HC673 Session 2003-2004
NIA 41/03 *BELFAST*: The Stationery Office £17.50

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The Comptroller and Auditor General is the head of the Northern Ireland Audit Office employing some 100 staff. He, and the Northern Ireland Audit Office, are totally independent of Government. He certifies the accounts of all Government departments and a wide range of other public sector bodies; and he has statutory authority to report to Parliament and the Assembly on the economy, efficiency and effectiveness with which departments and other bodies have used their resources.

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Report by the Comptroller and Auditor General for Northern Ireland

INTRODUCTION

1. This Report brings together the results of financial audit work undertaken by the Northern Ireland Audit office over the last twelve months and highlights issues arising from it. The aim of this work is to provide the Northern Ireland Assembly and Parliament with independent assurance that accounts are properly prepared, and that income and expenditure has been applied for the purposes intended. The report contains the following sections:

- RESOURCE ACCOUNTS

  Significant matters arising from the audit of the Resource Accounts of government departments for 2002-2003.

- EXECUTIVE AGENCY AND NON-DEPARTMENTAL PUBLIC BODY ACCOUNTS

  Significant issues arising from financial audit work undertaken on Executive Agency and Non-Departmental Public Body accounts.

- NORTHERN IRELAND CONSOLIDATED FUND

  Analysis of major items of revenue paid into the fund and analysis of issues from the Fund.

- PRIVATE FINANCE INITIATIVE: REPORTING OF FINANCIAL COMMITMENTS.

Part 1

Resource Accounts

2002 - 2003

Progress on Resource Accounting in Northern Ireland

Introduction

1. This is the second year in which departmental accounts have been prepared on a resource basis. Under the Government Resources and Accounts Act (Northern Ireland) 2001, departments are required to produce commercial-style resource accounts. These accounts are much more complex than the Appropriation Accounts which they replaced. The Appropriation Accounts simply showed the cash spend. The Resource Account is a consolidation of the financial results of the department and its agencies and comprises a series of inter-related statements showing how the department was financed, its expenditure by type and purpose, and its financial position at the end of the year.

Delivery of Resource Accounts

2. The Government Resources and Accounts Act (Northern Ireland) 2001 requires departmental resource accounts to be submitted for audit by 31 July immediately following the 31 March financial year end, and for the accounts to be certified by 31 October. The Department of Finance and Personnel have until 15 November to lay the accounts before the Assembly.

3. In 2002-03 all Northern Ireland Resource Accounts were submitted for audit by 31 July. The statutory requirement to certify the accounts by 31 October was achieved by 16 out of 17 (the remaining account was certified shortly after this date). All Northern Ireland Resource Accounts were presented to Parliament by the statutory publication date of 15 November. This was a considerable improvement on the previous year when three accounts were not presented on time.

Faster Financial Closing

4. In Great Britain HM Treasury has launched an initiative to accelerate the production and audit of resource accounts, its ultimate intention being that all departmental resource accounts will be laid before Parliament before the Summer recess of 2005-06. This replicates the timetable that already applies to the accounts of departments' Executive Agencies. The impetus for this stems in part from a desire to replicate best practice in the commercial sector. It is the intention of the Department of Finance and Personnel that Northern Ireland Departments should follow the same timetable.

Qualified Audit Opinions

5. The quality of accounts submitted for audit has improved from last year. Qualified opinions were issued on seven resource accounts compared to ten in 2001-02. Although some accounts were qualified on more than one count, the nature of the qualifications was

less severe than in the previous year. For example, there was only one instance of a "disclaimed" opinion (Department of Social Development) compared to three in 2001-02. A disclaimer is issued in circumstances where the limitation on the scope of the audit is so extensive that it is not possible to form an audit opinion.

6. Two of the seven accounts that received a qualified audit opinion in 2002-03 would have been qualified anyway under the cash based system of accounting.

Department for Social Development

The audit opinion on this account would have been qualified anyway on the following counts:

- a significant level of estimated fraud and incorrectness in certain social security benefits;
- weaknesses in financial control and monitoring of urban regeneration and community development grants to voluntary and community bodies; and
- weaknesses in financial control and monitoring of grants paid to Registered Housing Associations.

Department of Health, Social Services and Public Safety

My audit opinion on this account would have been qualified anyway under a cash based system on grounds of regularity. There was a material loss of income as a result of patients incorrectly claiming exemption from health service charges. As a result the lost income was not available for the purposes intended.

Technical Accounting Issues Arising

7. Six accounts were qualified on matters arising from the technical demands and higher reporting standards placed on departments under resource accounting.

8. These technical accounting issues are of a specific nature relating to the more demanding standards that resource accounts require and they do not imply that the integrity of transactions recording the inflow and outflow of cash in departments has deteriorated. What this does mean, however, is that some departments have not yet reached the new higher reporting standard set. This was evident in the following areas:

- Monitoring of Expenditure against Budget

  The new resource-based budgeting regime introduced for the first time in 2001-2002 is considerably more complex than the previous cash based system. It requires Departments to forecast and manage the resources they will consume in delivering services, including changes in the value of assets and liabilities for which they are responsible, as well as their cash spending.

Departments have a duty to plan and watch their expenditure in such a way that it will not exceed the amounts provided by the Assembly or Parliament. Departments which incur expenditure in excess of the amounts provided must seek the covering authority of the Assembly or Parliament by means of an Excess Vote at a later stage. Such excesses, however small, are irregular and result in a qualified audit opinion.

Two Excess Votes occurred this year compared to three in 2001-2002. (Department of Agriculture and Rural Development and Department of Enterprise, Trade and Investment). These Excess Votes demonstrate the difficulty encountered by departments in monitoring their expenditure on a resource basis. There remains a need for both better resource planning within departments, and for greater understanding of the resource consequences of decisions that do not have immediate cash consequences such as fixed asset valuations, impairments and provisions.

- Accounting Treatment and Estimates

  Resource accounting requires a much higher degree of estimation by departments than was the case previously with cash-based Appropriation Accounts. My staff reviewed the data, calculations and assumptions on which estimates were based to ensure they were reasonable. In one case, student loans, I was not satisfied that accounting estimates were sufficiently reliable and robust. As a result I qualified my opinion on the Department of Education and Learning resource account. I also disagreed with the treatment of EU income on this account.

- Debtors and Creditors

  In one case (Department for Social Development), systems were unable to fully capture the relevant information.

Management Information Systems

9. Northern Ireland departments continue to rely heavily on management information systems which were designed to operate on a cash basis. As a result, the year end accounts production process requires a disproportionate level of manual effort. The Department of Finance and Personnel is currently taking the lead in developing a new accounting service for all Northern Ireland departments. A progressive roll out of the new service will commence during 2006.

Conclusion

10. I am pleased to report that, in 2002-2003, there was a clear improvement in both the quality and timeliness of Resource Accounts submitted for audit. However, with seven out of seventeen accounts for 2002-03 not receiving a clear audit opinion some departments

have still considerable work to do to bring their financial reporting up to the standard the Assembly and Parliament have a right to expect. In particular there needs to be a greater recognition that the production of accurate and timely accounts at the end of the financial year requires sound financial management throughout the year. The generation of reliable financial information must be a monthly discipline that is not performed for its own sake, but which directly contributes to the financial monitoring and effective management of government departments.

DEPARTMENT OF AGRICULTURE AND RURAL DEVELOPMENT RESOURCE ACCOUNT 2002-03

Excess Vote

1. The Department of Agriculture and Rural Development Resource Account shows expenditure of £4.157 million (7.25%) in excess of the net estimate for Request for Resources B (Reducing the risk to life and property from flooding, promoting sustainable development of the Sea Fishing Industry and maintaining, protecting and expanding forests in a sustainable way), which amounted to £57.294million. It is proposed to ask Parliament to authorise a further supply grant of £4.157million.

2. The excess expenditure relates to the non-cash items in Request for Resources B, which includes depreciation, cost of capital, notional costs, permanent diminution in value and loss on disposal of fixed assets, where outturn exceeded estimate by £5.048million. Net savings of £0.891million in other parts of Request for Resource B reduce the excess to £4.157million.

3. The Department has informed me that the Excess arose through a miscalculation of the requirement for capital charges. At the Spring Supplementary Estimates stage, substantial changes were necessary to this area of expenditure because of classification decisions relating to assets of the Rivers Agency. It was during these amendments that the miscalculation occurred.

4. The Department has informed me that it has reminded all relevant managers of the need to ensure that all estimates are calculated correctly and that all expenditure is monitored effectively whether it is of a cash or non-cash nature.

DEPARTMENT OF CULTURE, ARTS AND LEISURE RESOURCE ACCOUNT 2002-03

Introduction

1. I qualified my opinion on the 2001-02 Department of Culture Arts and Leisure resource account due to a limitation of evidence available to me because: adjustments had been included in the financial statements to balance schedules and reconcile notes to schedules; and the Department was unable to confirm the accuracy of creditors as at 31 March 2001.

2. I undertook at the time of my previous report to keep the above issues under review and report further, if necessary. This report reflects the outcome of my review of the action taken by the Department in response to the issues raised.

3. My report also notes that during the course of the 2002-03 audit a further area of concern was identified in relation to the valuation and completeness of fixed assets held by the Department.

Action taken by the Department of Culture, Arts and Leisure

4. Following my audit of the 2001-02 resource account the Department commenced a review of the adjustments in that account. This resulted in correcting entries to the 2002-03 resource account and its notes of:

- £0.381 and £0.012 million in the movements in working capital other than cash at Note 14 and the Cashflow Statement at Schedule 4.
- £0.381 and £0.009 million in the reconciliation of net operating cost to changes in general fund.

5. However, the Department was not able to complete a full analysis of all the previous years' adjustments. Therefore, the draft 2002-03 account, submitted for audit in July 2003, contained correcting entries for which the supporting information and explanation was incomplete. The Department remains unable to address all the adjustments made in the 2001-02 account and the issues raised in my previous report, and is still unable to provide me with the information and explanations necessary to support the correcting entries in the 2002-03 resource account.

6. I am concerned that the Department of Culture Arts and Leisure procedures for resolving these issues for the 2002-03 account were not adequate with the result that the review did not provide a satisfactory conclusion to ensure these matters were fully addressed on a timely basis. The Department told me that this was due to difficulties in securing and retaining skilled staff, and differences in the accounting systems and procedures used within the core Department and one of its agencies.

7. The creditor information as at 31 March 2001 has been updated and I am satisfied that the appropriate amendments have been made to the accounts this year.

Fixed Assets Completeness and Valuation

8. Within the £16.7 million of tangible fixed assets disclosed in the account at 31 March 2003 the Department is directly responsible for £4.36 million. A professional valuation of these directly managed tangible fixed assets was carried out five years ago by the Valuation and Lands Agency (VLA) and since then the Department has increased the value of these assets using indexation tables provided by VLA.

9. In accordance with the Northern Ireland Resource Accounting Manual the Department is required to obtain a professional valuation of fixed assets every five years. This valuation was due in 2002-2003. However VLA was unable to carry out a full valuation of all the assets within the timescale required and the Department has continued to increase the valuation using indices provided by VLA.

10. A valuation of a proportion of these assets was provided by VLA on 24 October 2003 which was too late to be incorporated in the account before the 31 October deadline. This partial valuation reported that assets held at an indexed value of £3.23 million have a current value of £4.21 million. These assets are therefore understated in the accounts by £0.98 million. As VLA still has to value the remaining tangible fixed assets I am unable to determine the current value of these assets and ascertain the reasonableness of the figures contained in the account.

11. In addition, intangible fixed assets, consisting of sporting and fishing rights are included in the account at an indexed valuation of £0.75 million. These were also due to be valued by VLA for 2002-03 and as the valuation has not been undertaken I am also unable to provide an opinion on the reasonableness of the valuation of these assets in the account. Furthermore, the Department has identified further intangible fixed assets which have not been included in the account or been professionally valued.

12. As a result I conclude that insufficient evidence has been provided to me to support the valuation of tangible fixed assets and the valuation and completeness of intangible fixed assets in the financial statements.

13. I will continue to monitor progress on the issues raised in this report and will report again if necessary.

Conclusion

14. On the basis of my specific findings in paragraphs 4 to 13 I have not obtained sufficient evidence concerning the adjustments and the value of fixed assets. I have therefore decided to qualify my audit opinion accordingly.

DEPARTMENT OF EDUCATION RESOURCE ACCOUNT 2002-03

Introduction

1. I was unable to form an opinion on the 2001-02 Department of Education Resource Accounts due to a limitation of evidence available to me because:

- the Department was unable to confirm the accuracy of the balance of cash at bank and in hand;
- the Department had not implemented certain transitional adjustments and disclosures to the accounts specified by the Department of Finance and Personnel;
- other adjustments had been included in the financial statements to balance schedules and reconcile notes to schedules; and
- the accounting policy in respect of grants to non-departmental public bodies was not in accordance with the Northern Ireland Resource Accounting Manual.

2. I undertook at the time of my previous report to keep each of the above issues under review and to report further, if necessary. This report reflects the outcome of my review of the action taken by the Department in response to the issues raised.

Action taken by the Department of Education

3. Following my audit of the 2001-02 Resource Accounts the Department advised me that it had prepared a detailed action plan for the work to be done to arrive at revised accounts for the 2001-02 year. The Department provided me with a copy of the revised accounts in March 2003.

4. I examined the revised accounts, which form the basis of the restated 2001-02 comparative figures disclosed in the 2002-03 accounts, and, having reviewed the Department's supporting working papers and obtained additional information from the Department, I am satisfied that the Department has taken sufficient action to address the issues raised in my previous report and has provided all the evidence required for my audit. As a result I have been able to give an unqualified opinion on the 2002-03 Resource Accounts.

DEPARTMENT OF EDUCATION - TEACHERS' SUPERANNUATION RESOURCE ACCOUNT 2002-03

Introduction

1. I was unable to form an opinion on the 2001-02 Department of Education - Teachers' Superannuation Resource Accounts due to a limitation of evidence available to me because:

- the Department was unable to confirm the accuracy of the balance of cash at bank and in hand;
- the Department had not implemented certain transitional adjustments and disclosures to the accounts specified by the Department of Finance and Personnel;
- the teachers' pension and teachers' payroll data matching exercise had not been completed; and

I also qualified my opinion on the regularity of income in 2001-02 because the employers' contribution rate was not in accordance with the rate recommended by the Scheme's Actuary.

2. I undertook at the time of my previous report to keep each of the above issues under review and to report further, if necessary. This report reflects the outcome of my review of the action taken by the Department in response to the issues raised.

Action taken by the Department of Education.

3. Following my audit of the 2001-02 resource accounts, the Department advised me that it had prepared a detailed action plan for the work to be done to arrive at revised accounts for the 2001-02 year. The Department provided me with a copy of the revised accounts in March 2003.

4. I examined the revised accounts, which form the basis of the restated 2001-02 comparative figures disclosed in the 2002-03 accounts, and, having reviewed the Department's supporting working papers and obtained additional information from the Department, I am satisfied that the Department has taken sufficient action to address the first two issues raised in my previous report and has provided all the evidence required for my audit. As disclosed in Schedule 1 to the accounts, the effect of restating the 2001-02 comparative figures is a prior period adjustment of £5.520 million.

5. In addition, the data matching exercise has also been completed by the Department. From the 368 cases initially identified 13 cases required overpayments totalling £35,294.82

to be recovered. The Department was already aware of four of these cases amounting to £22,058.02. The Department has now taken action to recover the overpayments in all 13 cases.

6. With regards to these issues I am satisfied the Department has taken sufficient action to address them and has provided all the evidence required for my audit. As a result, I have not qualified my audit opinion on the 2002-03 Resource Accounts in respect of them.

Contribution Rate and Actuarial Valuations.

7. The employers' contribution rate for 2002-03 (7.85 per cent) was based on the results of the actuarial valuation as at 31 March 1986.

8. The Department did not implement the 1991 actuarial valuation (which recommended an employers' contribution rate of 7.35 per cent from 1 April 2000) for the reasons set out in my report on the 2001-02 accounts.

9. Current regulations (The Teachers' Superannuation Regulations (Northern Ireland) 1998) require employers to pay contributions in line with the rate specified by the Actuary.

10. Since my report on the 2001-02 accounts, the Actuary has finalised his valuation at 31 March 1996 and has recommended an employers' contribution rate of 7.0 per cent from 1 April 2004. The actuarial valuation as at 31 March 2001 remains to be finalised.

Conclusion

11. In respect of the matters reported at paragraphs 7 to 10, I concluded that the rate of employers' contributions payable to the Scheme during the year ended 31 March 2003 were not paid in accordance with the recommendation of the Actuary and I qualified my opinion on the regularity of income accordingly.

DEPARTMENT FOR EMPLOYMENT AND LEARNING RESOURCE ACCOUNT 2002-03

Introduction

1.1 I qualified my opinion on the Department's account on two issues:

- the Department's systems for estimating the cost of student loans and associated provisions was insufficiently robust (paragraphs 2.1 to 2.24 below);and
- disagreement on the accounting policy for the recognition of European income (paragraphs 3.1 to 3.10 below).

PART 2: ACCOUNTING FOR STUDENT LOANS

Background

2.1 I qualified my opinion on the Department for Employment and Learning (DEL) 2001-02 resource account as a result of significant inaccuracies in accounting for student loans. The 2001-02 account was the first resource account which DEL had prepared under the Government Resources and Accounts Act (Northern Ireland) 2001.

2.2 In 2001-02 the basis of accounting for student loans of £322 million and associated provisions of £135 million was, in my opinion, not sufficiently robust for such a significant aspect of the Department's accounts.

2.3 I am pleased to report that DEL has made significant progress in properly accounting for student loans of £424 million in its 2002-03 Resource Account. I have not qualified my opinion, this year, on the total amount of loans outstanding. However, I continue to qualify my opinion on the cost of the student loan subsidy and associated provisions. The financial statements include the net cost of student loans of £26 million for 2002-03 and total student loan provisions at 31 March 2003 of £167 million.

2.4 Students in Higher Education may apply for loans as support towards the costs of fees and maintenance. The amount of loan to which a student is entitled is calculated by the Education and Library Boards. A student applies to the Education and Library Board which covers the area in which he or she resides prior to entering Higher Education.

2.5 The administration of loan payments and recoveries is carried out, on a UK wide basis by the Student Loans Company Limited (SLC), a Non Departmental Public Body controlled by the Department for Education and Skills (DfES) and the Scottish Executive. The

Department for Employment and Learning funds the SLC for loans that the SLC issues to Northern Ireland (NI) domiciled students.

2.6 A Financial Memorandum was issued in March 2000 between the three departments (DfES, Scottish Executive and DEL) and the SLC setting out the respective roles and responsibilities of each party. The three parties agreed that DfES would take the lead role in dealings with the SLC.

2.7. Student Loans are long-term and may take up to 30 years to repay fully. Interest on loans is not charged at a commercial rate but is limited to the rate of inflation. In effect, loans are heavily subsidised as they are issued at a zero rate of interest in real terms.

2.8 There are two separate loan schemes, mortgage style and income contingent loans. Mortgage style loans were issued up to the 1998-99 academic year with income contingent loans then replacing them. Mortgage style loans are repaid over a fixed number of instalments depending on the nature of the course undertaken with repayments deferred on a yearly basis if the graduate's income falls below 85 per cent of the national average. Income contingent loans are not repaid over a fixed period as repayments are linked to income so that repayments increase in line with income growth. Repayments only commence when a student's income exceeds a minimum level.

2.9 Students make repayments of mortgage style loans to the SLC who, in turn, forward the proceeds to the respective departments. In the case of income contingent loans, the Inland Revenue collects repayments from employers through the PAYE system and forwards the funds to the respective departments. The amount of repayments under this PAYE scheme is currently small.

Accounting for Student Loans and Associated Provisions in 2002-03

Student Loans

2.10 Loans administered by SLC on a UK wide basis are accounted for as assets by each Government department and not as assets of SLC who solely administer them. Each department must account for its own loans which are determined by the domicile of the student, that is, the region of the United Kingdom where the student resides prior to entering Higher Education. DEL is dependent on information from SLC in recording the amount of loans owing to it. Loan accounts at SLC are 'flagged' to indicate the relevant region and consequent department which has funded the loan, although this data can be technically difficult to extract from the primary accounting system.

2.11 At the end of each financial year the SLC forwards to each Department details of a domicile analysis of the loan book. In 2001-02, the Department did not receive this information in time for the preparation of its annual accounts and consequently had to estimate the amount of loans outstanding from Northern Ireland domiciled students. I was of the opinion that the use of estimated figures was unsatisfactory for such a significant area when actual figures would normally be expected. In my 2001-02 report, DfES told me that it accepted that it needed to do more to ensure that accurate data on loans is available in time for all Departmental accounts and that it was working closely with SLC and with colleagues in NI and Scotland to improve the delivery of data disaggregated between the three administrations. I am pleased to note that in 2002-03 the domicile analysis was received in time and therefore actual not estimated amounts were used in accounting for student loans.

This was a significant development. The actual amount of outstanding Student Loans at 31 March 2003 was £424 million (31 March 2002: £322 million). This balance now represents the actual amount of the outstanding loan book relating to NI students rather than an estimation of the likely level included last year.

2.12 As the amount of student loans in 2001-02 were estimated, an adjustment was required to revise the amount included in the 2001-02 resource accounts at 31 March 2002 to the actual amount provided by SLC. An adjustment was therefore included in the 2002-03 accounts increasing Student loans of £322 million at 31 March 2002 by £9 million.

2.13 DEL sought and received assurances from the SLC's Internal Auditors on the accuracy and robustness of the systems underlying the domicile analysis. It has been agreed by all Departments and the SLC that from 2003-04 onwards such an assurance will be provided by the SLC's External Auditor.

2.14 The Department has this year recognised interest earned on Student Loans of £6 million in its Resource Outturn. In 2001-02 interest earned was not recognised in the Resource Outturn but was instead credited to DEL's General Reserve in the Balance Sheet. I did not agree with this treatment as the interest should have been included in the Resource Outturn. In 2001-02 interest could only be estimated. In 2002-03 the amount of actual interest earned has been obtained from the SLC domicile analysis removing the requirement on DEL to use an estimated amount.

Cost of Student Loan Subsidy and Other Associated Provisions

2.15 The Department must not only accurately record the debt due on loans it has funded, it must also account for the subsidised cost of these loans. The cost to Government, of funding loans until repayment, is estimated at 6 per cent per annum in real terms. The cost of subsidised student loans is therefore substantial given the nil rate of interest earned in real terms, the long repayments period and a 6 per cent cost of capital on the balance of outstanding loans less the Interest Subsidy and Loans Deferment and Default provisions.

2.16 The cost of the life-time subsidy on the loan to the Department must be recognised in the year that the loan is paid to the student. This life-time cost is accounted for by the creation of an "Interest Subsidy" provision, which is reduced to nil as the loan is repaid. The interest subsidy cost in 2002-03 was estimated at £21 million and is included in the interest subsidy provision which totalled £94 million at 31 March 2003.

2.17 A further cost which is provided for each year is the estimated and actual cost of unrecoverable loans. This cost arises as a result of either the death of a student, student income not reaching the income threshold for repayment or the SLC not being able to trace the student. The cost of unrecoverable loans is included in a "Student Loan Deferment and Default" provision and in 2002-03 it was estimated at £7 million. The total amount provided for the cost of unrecoverable loans at 31 March 2003 was £48 million.

Potential Inaccuracies in Accounting for the Student Loan Subsidy and Associated Provisions

2.18 Although the Department has improved the accuracy of its accounting for the amount owing on student loans, the net cost of student loans (£26 million for 2002-03) and the associated provisions (£167 million at 31 March 2003) continue to be determined on the same basis as last year. The Department has once again this year not applied a financial modeling technique, used by both DfES and the Scottish Office, to estimate the cost of their Student Loans and the amount of the associated provisions at 31 March 2003. Instead the Department derives the amount it includes for the cost of its Student Loans and associated provisions from the DfES provisions as at 31 March 2002 on a proportionate basis.

2.19 In my view this approach is not a sufficiently robust basis for estimating such significant costs to the Department. Due to the dynamics involved in loans repayable over long time periods reliable estimates of the lifetime costs of student loans can only be made by using actuarial techniques and financial modeling. There are two problems with the Departments existing approach. First DEL is using out of date information as at 31 March 2002 to estimate the 2002-03 cost of student loans and the provisions figure. Second, the estimation basis assumes the Northern Ireland costs and provisions for student loans are proportional to the England and Wales figure. This may not be an appropriate assumption. For instance, the level of deferment and default may be different for Northern Ireland students.

2.20 The Department told me that it did develop and use the financial model, already devised by DfES, to estimate the Northern Ireland cost of student loans and the associated provisions for 2002-03. However the resulting outputs were not used for accounting purposes. If the financial model had been applied and used for accounting purposes the 2002-03 student subsidy charge and the provisions would have been £4.1 million higher than the charges in the resource account. To date the Department has not yet run the model for prior financial years to establish the financial effect of using a model on prior years. The Department has told me that the financial model will be used and applied for accounting purposes from the 2003-04 financial year. The model will also be run for prior years and if appropriate revisions made to the estimate of the provision in 2003-04.

2.21 The Department has made the following comments on the £4.1 million difference between the amount reported in the accounts and the amount indicated by the model. In the Department's view both figures are estimates and there is no evidence to confirm which is the better estimate. The Department further notes that FRS 12 recognises that estimates, particularly in the case of provisions, are an essential part of the preparation of accounts and do not undermine their reliability. In my view, however, an estimate derived from a carefully constructed financial model with assumptions honed to reflect Northern Ireland circumstances is potentially more reliable than the use of an approximate apportionment of an out of date England & Wales figure to estimate the cost of student loans and the associated provisions.

Conclusions

2.22 The basis of accounting for student loans of £424 million has improved since 2001-02 due to the timely receipt of financial information from the SLC on the domicile split of the loan book. I am pleased that the Department now uses actual rather than estimated figures for the amount owing from Student Loans.

2.23 My concern, however, over the accounting for the 2002-03 net cost of Student Loans of £26 million and associated provisions of £167 million at 31 March 2003 remains unchanged from last year. I have therefore again qualified my opinion on the cost of Student Loans and the amount of the associated provisions as the basis used is not sufficiently robust to support such significant amounts. Using out of date information from DfES is not satisfactory when estimating such an important cost to the Department.

2.24 I recommend that the Department:

- implements the model in 2003-04;
- generates information on loan deferment and default patterns with regard to Northern Ireland domiciled students and feed this Northern Ireland specific information into the model that has already been developed; and
- carry out regular reviews of underlying assumptions surrounding loan deferment and default in the light of changes in economic factors/graduate employment.

ACCOUNTING FOR EUROPEAN INCOME

3.1 I qualified my opinion on DEL's 2001-02 Resource Account as I disagreed with the Department's accounting treatment of European Union (EU) income. My opinion on the 2002-03 account continues to be qualified as the Department's treatment of EU income remains unchanged. The 2002-03 accounts include £28 million of expenditure on European Schemes which can subsequently be recovered in full from the EU.

3.2 The Northern Ireland Resource Accounting Manual (NIRAM) requires European expenditure to be recognised as closely as possible to the time of the underlying event or activity that gives rise to a liability. NIRAM further states that where there is a delay in the receipt of EU funds the amount should be treated as accrued income. In my opinion, this means that European income should be recognised on the basis of eligible expenditure that can be reclaimed and so income should be recognised at the same time that eligible expenditure is incurred.

3.3 The Department's policy however is to recognise European income as claims are submitted to the European Commission. The Department considers that this is the approach required by NIRAM. However, in my view, the effect of this is that European income is recognised later than required.

3.4 The Department's 2002-03 Resource Account includes £111 million in respect of EU income. This includes £71 million in respect of claims submitted to the European Commission in 2002-03. The remaining £40 million is in respect of advances received in previous years but not recognised as income until 2002-03 when the final claim was submitted. A significant element of the £111 million of income recognised in 2002-03 should, in my view, have been recognised in previous years when the eligible expenditure had been incurred. I am unable to analyse this income between 2002-03 eligible expenditure and previous years' expenditure as the information is not readily available.

3.5 The 2002-03 resource account also includes approximately £28 million of EU expenditure incurred during the year which has not yet been claimed and therefore not recognised as accrued EU income. In addition eligible expenditure of around £5 million has also been incurred in previous years which has still not been included in a claim and therefore has not also been recognised as income. In total, debtors for accrued income are underestimated by £33 million. As any European income received must be paid to the Consolidated Fund, an amount payable to the Consolidated Fund of £33 million should have also been recognised. Therefore creditors are also understated by £33 million.

3.6 The Department does not accept that it has not followed NIRAM and insists that it has followed advice given to it by DFP. The Department's views and the reasons why I disagree with them were addressed in detail in my report on the 2001-02 Resource Account. Relevant extracts are re-produced in Appendix 1.

3.7 The Department has emphasised that it is not entitled to payment from the Commission until all audit and vouching activities on relevant expenditure has been completed and confirmed in the claim made to the Commission. It further notes that the accounting treatment of European income generally is scheduled to be reviewed by the Financial Reporting Advisory Board (FRAB).

3.8 My conclusion on the Department's accounting treatment of European income is the same one given in my 2001-02 report. In my opinion, the Department's policy of recognising EU income as claims are submitted to the European Commission does not meet the requirements of NIRAM.

3.9 The Department is completely out of line with the recognition bases applied by all other Northern Ireland Departments and their Executive Agencies on European income in the preparation of their accounts. In my view inconsistency of this nature creates unnecessary difficulties for anyone trying to understand the treatment of EU receipts in Northern Ireland Departments' accounts.

3.10 I have therefore qualified the 2002-03 resource accounts as the Department does not agree with my opinion that NIRAM policy on the recognition of EU income has not been properly applied and will not amend its accounts to:

- include a prior period adjustment for the significant element of the income of £111 million recognised in 2002-03 which should have been recognised in prior years and not in 2002-03;
- recognise additional income and accrued income receivable of some £28 million;

- recognise accrued income receivable of some £5 million on, as yet, unclaimed eligible expenditure of prior years;
- recognise that this additional income is repayable to the Consolidated Fund by increasing creditors by £33 million and reducing General Fund by the same amount.

3.11 I recommend that the Department revises its accounting policy on the recognition of European income so that European income is recognised on the basis of eligible expenditure that can be reclaimed and so income is recognised at the same time that eligible expenditure is incurred.

Appendix 1

Extracts from my 2001-02 Report on Accounting for European Income detailing the Department's Interpretation of NIRAM

1. The Department had told me that its interpretation of NIRAM's "instruction" is as follows:

i. NIRAM 6.5.1 says 'amounts receivable' should be recognised.

ii. What is to be included in the operating statement is subject to the interpretation of the word 'receivable' under Financial Reporting Standards (FRS).

iii. NIRAM 3.1.1/2 (following FRS 5) defines an asset as a right to future economic benefits controlled by (the) entity. It defines control as the ability to obtain the benefits and restrict the access of others. Since control of funding remains with the EU until it approves a claim there is not a case in strict accounting terms for the Department to include such funding as its assets in advance of EU claim approval. Nevertheless the Department has accepted DFP's ruling that amounts in completed but unapproved claims to the Commission must be recognised as income.

iv. FRS 18 makes explicit that more evidence is required for the existence of an asset/gain than for the existence of a loss or liability. Recognising EU income at the point of the Department incurring expenditure ignores the accounting tests for asset income recognition.

v. FRS 12 draws on the concept of tests for the nature and recognition of an asset (as does NIRAM 4.3). The standard states that unless an inflow of economic benefits is virtually certain it does not represent an asset. It further states that where an inflow is probable but not virtually certain it is a contingent asset and to be included in notes to the accounts but not included as income. This suggests that until the EU approves a claim the probable amount concerned should be recorded as a contingent asset.

vi. NIRAM 6.5.2 indicates that "expenditure.... should be recognised in resource accounts as closely as possible to the time of the underlying event or activity that gives rise to a liability". However this paragraph relates to expenditure, not income, and there is no paragraph applying this wording in relation to income.

vii. NIRAM requires that where there is a delay in the receipt of EU funds the amount should be treated as accrued income. By implication this infers that income should be recognised in response to a claim. The Department's approach is consistent with this.

2. The Department notes that its interpretation of NIRAM leads to what it considers to be the proper, conservative approach to the timing of the recognition of European income.

3. I do not accept this interpretation of NIRAM to the recognition of European income, nor do I accept that the Department's more conservative approach complies with the prin-

ciple that EU income should be recognised on the basis of eligible expenditure that can be reclaimed. In short, the European Commission will grant aid eligible expenditure. The Department should be able, in the same way as all other Northern Ireland Departments are able, to determine if expenditure incurred is eligible expenditure and recognise the likely amount of European income receivable on the basis of that eligible expenditure. Indeed the Department would be held to account for amounts paid that are ineligible.

4. The Department pointed out to me that it took independent professional advice which supports its original income recognition approach that only approved final claims should be recognised as income. The Department also had sought the views of DFP on the recognition of European income and there were subsequently full discussions between the Department and DFP on this matter. The Department told me that after these discussions it decided to adopt the recognition of income based on final claims submitted (even if not approved) by EU. Prior to this, its policy was to recognise income only on the approval of the submitted claim by the European Commission, an even more conservative approach than using submitted but unapproved claims.

5. The Department considers that it has already modified its accounting policy in order to comply with DFP's "ruling" that amounts included in completed but unapproved claims must be recognised as income. However, this was only one aspect of the DFP advice. There were two components of the advice.

- EU income should in principle be recognised in the accounts of government bodies to which NIRAM applies on the basis of eligible expenditure that can be reclaimed;
- In practice, completed claims may provide a useful summary of the expenditure that will be repaid, and represent the minimum that should be accrued as income.

6. In my view, the first point clarified NIRAM policy by noting that European income should be recognised on the basis of eligible expenditure that can be reclaimed, which means that income should be recognised at the same time that eligible expenditure is incurred. The second point on the use of completed claims as a basis for recognising EU income, in my opinion, represented a practical means of estimating the amount of European income which should be recorded in the accounts in accordance with NIRAM policy.

7. In my opinion, the estimation basis suggested by DFP, as a minimum approach, could not appropriately comply with the NIRAM policy as, in this case, further claims were not due to be submitted in time for the finalisation of the accounts. The Department explained to me that the completion of final claims were subject to the additional verification that is necessary in finalising the EU Structural Funds 1994-1999 Programme and that the final claims are the only ones remaining to be made. The Department noted that at the time of drafting this report no member state had submitted such final claims to the European Social Fund. Furthermore, the Department made no other attempt, in the circumstances of claims not being completed in time for the preparation of the accounts, to properly apply the NIRAM policy. I therefore believe that NIRAM has not been properly applied towards recognition of European income.

UPDATE ON POTENTIALLY IRREGULAR EXPENDITURE ON THE INDIVIDUAL LEARNING ACCOUNTS SCHEME 2002-03

4.1 I qualified my opinion on the Department for Employment and Learning (DEL) 2001-02 Resource Accounts because of potentially irregular expenditure on the Individual Learning Accounts (ILA) Scheme.

4.2 I have not qualified my opinion on the 2002-03 Resource Accounts as the scheme was closed in November 2001 due to allegations of potentially serious fraud and abuse. Expenditure in 2002-03 was restricted to outstanding payments to some providers (£413,000) and the cost of the termination of the contract with the ILA contractor responsible for the administration of the scheme (£87,000). This compares to the total ILA expenditure of £6.4 million in 2001-02.

4.3 My 2001-02 report referred to potentially irregular expenditure of between £1.3 million and £2 million over the lifetime of the ILA Scheme. In that report I made several recommendations on further investigations and action required by the Department.

4.4 In October 2003 my staff reviewed the progress made on the recommendations and found that only limited progress had been made by the Department towards recovering irregular expenditure from training providers. In my 2001-02 report I emphasised that the Department needed to commit sufficient resources to properly quantify the extent of any fraud within the scheme in Northern Ireland and to recover the overpayments that it was already aware of.

4.5 It is disappointing to report that the Department has not yet engaged directly with relevant providers seeking recovery. Indeed the resources committed by DEL to dealing with irregular ILA transactions dropped to negligible levels following the retirement of two key officials who worked on the scheme. A number of steps have been taken by the Department for example to obtain data from Capita and to validate amounts which need to be pursued. Legal advice on the basis for seeking recoveries was also obtained. Nevertheless I would have expected speedier progress to have been made. The Department has since set up a small team to take forward my recommendations. I will continue to monitor progress.

DEPARTMENT OF ENTERPRISE TRADE AND INVESTMENT 2002-03 RESOURCE ACCOUNT

Excess Vote

Purpose of Report

1. In 2002-03 the Department of Enterprise, Trade and Investment (the Department) expended more resources than the Northern Ireland Assembly and Parliament had authorised. By doing so, the Department breached the Northern Ireland Assembly's and Parliament's control of expenditure and incurred what is termed an 'excess' for which Parliamentary authority is required. I have qualified my opinion on the Department's 2002-03 Resource Accounts in this regard. The purpose of this report is to explain the reasons for this qualification and to provide information on the extent and nature of the breach to inform Parliament's further consideration.

My responsibilities with Regard to the Breach of Regularity

2. As part of my audit of the Department's financial statements, I am required to satisfy myself that, in all material respects, the expenditure and income shown in the Resource Accounts have been applied to the purposes intended by the Northern Ireland Assembly and Parliament and conform to the authorities which govern them; that is, they are 'regular'. In doing so, I have had regard, in particular, to the Supply limits the Northern Ireland Assembly and Parliament have set on expenditure.

3. By incurring expenditure that is unauthorised and is thus not regular, the Department has breached Parliament's controls.

Background to the Excess

4. Parliament authorises and sets limits on departmental expenditure on two bases ñ 'resources' and 'cash'. Such amounts are set out in Supply Estimates for which the Northern Ireland Assembly's or Parliament's approval is given in annual Appropriation Acts.

5. By this means, the Northern Ireland Assembly and Parliament have authorised Requests for Resources for the Department. For each Request for Resources, it thereby authorises amounts for current expenditure which are net of forecast income, known as operating Accruing Resources. The Northern Ireland Assembly and Parliament set limits on the amount of income that can be applied towards meeting expenditure. The amounts authorised for Requests for Resources and operating Accruing Resources together represent a limit on the gross current expenditure that may be incurred under each Request for Resources.

Limits

6. The limits described above for the Department were set out in the Northern Ireland Main Estimates for 2002-03 as amended by the Northern Ireland Spring Supplementary Estimates. The limit for Request for Resources B (Developing and maintaining the equality, policy and regulatory environment necessary to achieve economic growth with equal opportunities for all) was set at net expenditure of £15,807,000. This limit was authorised in the Budget (Northern Ireland) Acts 2002 and the Budget (Northern Ireland) Order 2003. The breach reported below is against this limit.

Amount of Excess-Breach of limit on Request for Resources

7. Schedule 1 to the accounts shows net expenditure on Request for Resources B of £16,135,161.10 which is £328,161.11 (2.07%) in excess of the amount authorised. It is proposed to ask Parliament to make good the amount of Excess by authorising additional resources totalling £328,161.11 for this Request for Resources in respect of the year ended 31 March 2003.

Details and Causes

8. The excess arose primarily because of the need to include in the accounts an additional provision of £1,119,000 in respect of the maintenance of abandoned salt mines. This had not been anticipated, in November 2002 when the Supplementary Estimates for 2002-03 were being finalised. This additional provision was partly offset by savings of £791,000 in other Request for Resources B expenditure lines, reducing the excess to £328,000 (see Schedule 1 of the accounts "Explanation of the variation between Estimate and Outturn" Request for Resources B, note (v)).

9. In the Department's view it would have been difficult, in this case, to anticipate the need for the additional provision at the Supplementary Estimate stage as it was due to an event, the timing of which was completely unforeseeable. The Department has a statutory responsibility for over 2,000 abandoned mines in Northern Ireland and has responsibility for ensuring that these areas are safe including the payment of compensation where damage is caused to properties.

10. In the summer of 2002 Maidenmount salt mines at Carrickfergus partially collapsed and Carrickfergus International salt mine moved and seemed likely to collapse. Consultants were engaged to carry out a risk assessment and estimate the potential costs of repair work. The Department told me that this proved to be a rather complex matter involving the creation of new access roads and a new car park site for a business located near the mine site. A meaningful estimate of the cost of remedial works only became available in July 2003 after many options were considered on the best way to ensure that these mines and the surrounding areas were safe.

Action taken by the Department to help prevent a recurrence

11. The Department told me that it has taken steps to minimise the risk of such an excess recurring. It has already put in place procedures to review all provisions on a quarterly

basis so that all known adjustments can be taken into account. However the Department has emphasised that it will continue to be difficult to manage this non-cash area of the budget in circumstances where the timing and amount of provisions is subject to uncertainty and actual costing is not available until after November, which is the final month for inclusion in Supplementary Estimates.

DEPARTMENT OF HEALTH, SOCIAL SERVICES AND PUBLIC SAFETY RESOURCE ACCOUNT 2002-03

INCORRECT CLAIMS FOR EXEMPTION FROM HEALTH SERVICE CHARGES

1. The Department's Resource Accounts include the accounts of the four Health Boards which have been audited by auditors appointed by the Department.

2. Each of the Board's auditors qualified their opinions on the accounts for 2002/03 on the grounds that income due to each Board in respect of Family Practitioner Services was not received due to patients incorrectly claiming exemption from charges.

3. The total loss of income for 2002/03 was estimated by the Central Services Agency to fall between £8.9 million and £11.1 million. The Central Services Agency processes claims and makes payments to contractors providing Family Practitioner Services on behalf of the Boards.

4. I have qualified my opinion on the Department's Resource Accounts as this income due, but not received, has not been applied to the purposes intended by the Northern Ireland Assembly and Parliament and is not in conformity with the appropriate authorities.

5. The Department told me that following the publication of a PAC report in April 1999 [HC123: Northern Ireland: Controls to Prevent and Detect Fraud in Family Practitioner Service Payments] the Department has introduced a range of measures to counter this type of patient fraud.

6. A Counter Fraud Unit (CFU) has been established to address exemption fraud. This includes exemption from health charges for prescriptions, dental and ophthalmic treatment. The Unit, based in the Central Services Agency and working on behalf of the four HSS Boards, became fully operational in January 2001. It is also responsible for investigating cases of suspected fraud involving primary care cases through the Small Claims Court, as part of the process of recovering unpaid health charges.

7. A Fixed Penalty Charge Scheme has been implemented by the CFU, whereby patients who evade charges for prescriptions, dental or ophthalmic treatment are fined. The maximum Penalty Charge is £100. A surcharge is also due where patients fail to pay the Penalty Charge. Since January 2003, over 500 Penalty Charges have been issued to patients and some 120 surcharges.

8. Legislation has been introduced making it a criminal offense to evade Health Service charges. These powers are targeted at those patients who persistently defraud the health service by evading their health charges. Procedures are currently being finalised to enable such cases to be identified.

9. During the past three years both the prescription fraud and overall exemption fraud

have been reduced significantly. In the case of prescription fraud the reduction is some 12.6% and the overall exemption fraud has been reduced by approximately 11.5%. It is also the case that, in 2002-03, some £29.2m was collected from charges for items dispensed by pharmacists etc. This represented a 3.5% increase over the previous year's figure.

DEPARTMENT FOR SOCIAL DEVELOPMENT RESOURCE ACCOUNT 2002-03

Part 1: Introduction and Executive Summary

Introduction

1.1 The Department for Social Development is responsible for administering a wide range of expenditure aimed at helping those in need, promoting measurable improvements to housing in Northern Ireland and tackling disadvantage amongst individuals and communities. Through the Social Security Agency and the Northern Ireland Child Support Agency, the Department is responsible for the administration of social security benefits and child support. The Northern Ireland Housing Executive is responsible for administering Housing Benefit. The Department's financial assistance to the housing and urban regeneration sectors is administered through its Resources, Housing and Social Security Group and the Urban Regeneration and Community Development Group respectively. In 2002-03, the Department accounted for expenditure of £4.2 billion on these areas, including associated administration costs, in its consolidated Resource Account.

1.2 This report:

- summarises the results of my audit and sets out the reasons for my qualified audit opinion (Part 1);
- reviews the results of my audit of expenditure on non-contributory and means tested social security benefits administered by the Social Security Agency (Part 2);
- reviews the results of my audit of grants paid by the Department to Registered Housing Associations (Part 3);
- reviews the results of my audit of expenditure by the Department on urban regeneration and community development grants (Part 4); and
- examines the reasons for the uncertainties over certain debtor and creditor balances in the Balance Sheet (Part 5).

Executive Summary

On the reasons for my qualified audit opinion

1.3 I have qualified my audit opinion on the account because of:

- significant levels of estimated fraud and incorrectness in certain social security benefits;
- limitations in available evidence which prevented me from testing a significant proportion of Child Benefit payments;
- weaknesses in financial control and monitoring of expenditure in relation to grants paid to Registered Housing Associations;
- weaknesses in financial control and monitoring of expenditure in relation to urban regeneration and community development grants to voluntary and community bodies; and
- weaknesses in the Department's audit trails arising from deficiencies in the interaction between the Department's Programme Accounting Computer System (PACS) and its various benefit systems which resulted in limitations in the evidence available to support significant social security programme debtor and creditor balances.

Fraud and Incorrectness in Social Security Benefits

1.4 The Department estimates that in 2002-03 there were losses in Income Support, Jobseeker's Allowance, Disability Living Allowance and Housing Benefit as a result of errors by officials, errors by customers and fraud amounting to £120.9 million which is 7.6 per cent of expenditure on these benefits. However, there has been a significant decrease in suspected and customer fraud from £39.5 million at March 2002 to £13.1 million in Income Support and from £12.7 million at March 2002 to £10.5 million in Jobseeker's Allowance. The Department considers this improved performance results from the Social Security Agency's programme of interventions and the greater consistency achieved by the Agency across Social Security Districts due to management restructuring and more experienced staff.

1.5 While the Department achieved its Public Service Agreement target in 2002-03 of reducing losses from fraud and error in Income Support by 5 per cent, it is disappointing that its Jobseeker's Allowance target of 5 per cent was not achieved. The Department has various strategies in place to reduce error and fraud in benefits. These include the implementation across the social security network of intervention procedures to prevent fraudulent/incorrect claims entering the benefits systems and additional checks and controls as part of the Social Security Agency's Programme Protection activities.

1.6 I have qualified my audit opinion on the Resource Account due to the significant level of estimated fraud and error in social security benefits.

Child Benefit Awards

1.7 As in previous years, a significant number of Child Benefit cases were unavailable for testing due to the Social Security Agency's former policy to retain supporting case documentation on new Child Benefit cases for only two years, after which period it was destroyed. Measures put in place by the Social Security Agency through its Security and Quality Assurance Project, and the revised policy to retain sufficient case documentation for new Child Benefit awards, have enabled both my staff and staff of the Agency's Standards Assurance Unit to test new claims since 2000-01. However, without the appropriate supporting documentation the Department was unable to fully review individual awards in 2002-03. I have therefore qualified my audit opinion on the Resource Account due to the limitation of the evidence available. Responsibility for the administration of Child Benefit transferred to the Inland Revenue with effect from 1 April 2003.

Grants to Registered Housing Associations

1.8 On the basis of my specific audit findings, I have concluded that the Department's financial controls and monitoring of grants to Housing Associations remain inadequate. In addition, I have concerns over the adequacy of the Housing Associations' financial control and monitoring of expenditure on individual schemes. Weaknesses identified were: inaccurate and inapplicable certifications made by Housing Associations; non adherence by Housing Associations to departmental procedures; insufficient documentary evidence to support key decisions taken by Housing Associations; insufficient control and monitoring of schemes by Housing Associations; and inadequate departmental control and monitoring.

1.9 The Department has various strategies in place to improve financial control and monitoring of expenditure. These include a review of the Housing Association Guide, with the aim of having an on-line version available by mid 2004 and the splitting of the Department's Scheme Audit function from April 2002 into separate Development Compliance Audit and Minor Works and Validation Audit functions. The Department has also carried out a review of the role of Scheme Audit and intends that the Scheme Audit remit should be extended to provide a quality assurance function. Its intention is that a new Regulatory and Inspection Unit will commence operations with effect from 1 April 2004.

1.10 In the absence of proper controls I was unable to certify that expenditure was applied to the purposes intended and was regular. Consequently, I have qualified my audit opinion on the Resource Account.

Urban Regeneration and Community Development Grants to Voluntary and Community Bodies

1.11 On the basis of my audit findings, I have concluded that the Department's financial controls and monitoring of expenditure in relation to grants to voluntary and community bodies continue to be inadequate. Weaknesses identified related to the Department's Belfast Regeneration Office, European Union Unit, Regional Development Office, North West Development Office and Voluntary and Community Unit were:

- insufficient evidence/investigation to support funding decisions;
- insufficient liaison with other funders to establish level of alternative funding available/staging of payments;
- inadequate letters of offer/non compliance with terms and conditions of letters of offer;
- failure to issue revised letters of offer as a result of fundamental changes to projects;
- insufficient evidence to support payments;
- inadequate financial control/monitoring; and
- irregular payments, that is, payments made outside governing authorities.

1.12 The Department has or is currently putting various measures in place to improve financial control and monitoring of expenditure. These include: a Business Improvement Review of the Belfast Regeneration Office, which is nearing completion; a review within the Department's Urban Regeneration and Community Development Group of how payment systems and verification procedures should in future be structured to ensure greater effectiveness and robustness in control; the establishment of business support units in four of the Group's Directorates to provide quality assurance by way of reviewing project files, issuing best practice guidance and undertaking monitoring and verification of funded projects; and the establishment of Quality Assurance and Improvement Units within the North West Development Office and the Regional Development Office.

1.13 In a wide range of the funding activities for which the Department's Urban Regeneration and Community Development Group is responsible the relevant information did not exist to enable me to establish that expenditure was applied to the purposes intended and was regular. I have qualified my audit opinion on the Resource Account accordingly.

Debtor and Creditor Balances

1.14 As a result of weaknesses in the Department's audit trails mainly arising from deficiencies in the interaction between the Department's Programme Accounting Computer System and its various benefit systems, there were limitations in the evidence to support my audit of certain significant social security programme debtor and creditor balances. There is significant uncertainty over the accuracy and completeness of these amounts, which total around £68 million gross. I have assessed whether the impact of the uncertainty over these balances results in the balance sheet giving a misleading view and have concluded the impact is that the net assets of the Department may be significantly misstated. I have therefore qualified my audit opinion on the Resource Account because of the limitations in evidence.

Part 2: Qualified Audit Opinion Arising from the Level of Estimated Fraud and Incorrectness in Social Security Benefits and the Limitation in Audit Scope in Child Benefit Payments

Request for Resources A: Social Security - Administered by the Social Security Agency

Introduction

2.1 This part of my report sets out the results of my audit of expenditure by the Department for Social Development on non-contributory and means tested social security benefits administered by the Social Security Agency.

2.2 In 2002-03 the Department paid £1.89 billion on Social Security benefits, including Income Support £687 million, Jobseeker's Allowance £90 million, Disability Living Allowance £478 million, Child Benefit £306 million and additionally Housing Benefit £339 million. My audit of this expenditure examined the work undertaken by the Agency to establish the level of loss and incorrectness within the benefit system.

Summary of Main Audit Findings

2.3 During 2002-03 the Social Security Agency's Standards Assurance Unit continued to carry out two exercises to establish the level of loss and incorrectness within the benefit system. The two exercises are:

- Decision Making and Payment Accuracy - Unit staff annually examine a large sample of cases from each Social Security benefit and report on the standard of decision making and payment accuracy within the Agency. From 1 April 2002 the Unit has also been reporting on the financial accuracy of Income Support, Jobseeker's Allowance and Disability Living Allowance; and
- Benefit Review - The Agency established a benefit review process to provide a continuous rolling programme of measurement based on an in-depth examination of the circumstances of random samples of claimants, to determine the extent of claimant fraud and error in Income Support, Jobseeker's Allowance and Housing Benefit.

Decision Making and Payment Accuracy

2.4 The Chief Executive of the Social Security Agency through the Standards Assurance Unit (paragraph 2.5) is responsible for monitoring and reporting on the standards of decision making and on the accuracy of payments. To oversee the monitoring arrangements and to provide independent assurance on the Unit's findings, a joint Standards Committee for the Social Security and Child Support Agencies was set up in 1999. The Committee's annual report for 2002-03 summarises the results of the monitoring findings in relation to payment accuracy and the standard of decision making within the Agency for the year. The accuracy check looks at all the evidence, including retrospective evidence that is available to substantiate the amount of benefit awarded while the decision making check focuses on the quality of the decision making process taking account of evidence available at the time the decision is made. Details of the types of decision making errors are outlined in paragraph 2.16.

2.5 The Agency's Standards Assurance Unit examines statistical samples of all benefit awards on a continuous basis. From these samples they are able to monitor the accuracy of payments made and the quality of decision making, and estimate the gross monetary value of error. My staff examined and reperformed a sample of the Unit's case work during the year and I can report that I am content that the work undertaken continues to be of good standard and the results produced by the Unit are accurate and complete. The Standards Committee's 2002-03 report was published in September 2003. Figures 1 and 2 below compare payment accuracy and decision making outturn against targets for the three main non-contributory benefits: Income Support, Jobseeker's Allowance and Disability Living Allowance.

Figure 1: Payment Accuracy [1] Performance Against Ministerial Targets

Benefit		1998-1999	1999-2000	2000-2001	2001-2002	2002-2003
Income Support	Target	87%	88%	89%	90%	90%
	Outturn	88%	87%	88%	88%	91%
Jobseeker's Allowance	Target	87%	90%	91%	92%	92%
	Outturn	92%	92%	93%	94%	95%
Disability Living Allowance	Target	85%	87%	88%	90%	90%
	Outturn	91%	93%	94%	93%	87%

Notes:

(1) The accuracy check looks at all the evidence, including retrospective evidence that is available to substantiate the amount of benefit in payment. The check also takes into account factors outside the decision making process. For example, a decision to award benefit at the weekly rate of £50 could be correct but due to an official error the customer receives two payments for the same period resulting in an accuracy error because the amount of benefit paid is incorrect.

(2) Standards Assurance Team leaders validate the outturn figures, and in turn their work is validated by the Agency's Internal Audit Unit.

Figure 2: Decision Making Standard Achieved Against Benchmark

Benefit		2000-2001	2001-2002	2002-2003
Income Support	Benchmark	90%	90%	90%
	Standard Achieved	79%	69%	88%
Jobseeker's Allowance	Benchmark	94%	94%	94%
	Standard Achieved	85%	82%	92%
Disability Living Allowance	Benchmark	83%	83%	83%
	Standard Achieved	87%	81%	88%

Income Support

2.6 Income Support is payable to people aged 16 or over who satisfy certain conditions and whose income is below set levels. It is made up of: a personal allowance based on age and marital status; age related allowances for dependent children; and additional sums known as premiums and housing costs. From this total amount other income, including other social security benefits, is deducted. The Income Support scheme sets a limit to the amount of capital a person may have and still remain entitled to claim it. Customers must report changes in circumstances and Agency instructions advise staff to identify and review all cases on a regular basis. It is a highly complex benefit, with many different aspects of a claimant's circumstances affecting the correct level of benefit due in any week. All of this contributes greatly to the level of error, including customer error, present within Income Support expenditure. Expenditure on Income Support in 2002-03 was £687 million.

2.7 Although the Income Support payment accuracy rate achieved (Figure 1) has improved gradually from 87 per cent in 1999-00 to 91 per cent in 2002-03, against respective targets of 88 per cent and 90 per cent, the current error of nine per cent remains, in my view, a significant cause for concern. In addition, it is disappointing to note from Figure 2 that the Income Support decision making target of 90 per cent has not been achieved in each of the past three years. While reported performance improved from 69 per cent in 2001-02 to 88 per cent in 2002-03, the Department has told me that this is partly due to a change in the methodology for reporting errors with effect from May 2002, that is, a decision making error is now only reported if a payment error also exists. The Department also considers, however, that the improved performance in 2002-03 can be attributed to the impact of the initiatives taken as noted in my report on the 2001-02 account (HC 27/NIA 45/02). While this improvement is encouraging the error rate in 2002-03 of 12 per cent remains unacceptably high. To improve performance on both payment accuracy and decision making further the Department has told me that training and guidance have been reviewed and updated and further quality review measures have been introduced. The Department has also told me that this has already led to improved decision making results for the first quarter of 2003-04. I intend to review the position during the audit of the 2003-04 account.

2.8 The types of decision making errors in Income Support which arose in 2002-03 are summarised in Figure 3.

Jobseeker's Allowance

2.9 Jobseeker's Allowance is a means of support for unemployed people while they look for work. Claimants must demonstrate at the initial claim stage that they are available for and actively seeking work. The actions they propose to take to find work are set out in a signed Jobseeker's Agreement. The claimant's labour market activity is reviewed fortnightly when they attend a Social Security Office. The complexity of the regulations governing awards of Jobseeker's Allowance, combined with the requirement for claimants to demonstrate that they are available for and actively seeking work, make Jobseeker's Allowance a difficult and complex benefit to administer. Expenditure on Jobseeker's Allowance in 2002-03 was £90 million.

2.10 Figures 1 and 2 indicate mixed results for Jobseeker's Allowance for 2002-03. The payment accuracy rate achieved of 95 per cent exceeded both the target of 92 per cent and the 2001-02 achieved rate of 94 per cent which is encouraging. However, the Agency failed to meet the target set for decision making of 94 per cent for the third consecutive year. While reported performance has improved from 82 per cent achieved in 2001-02 to 92 per cent achieved in 2002-03, this can be partly attributed to the change in reporting methodology indicated in paragraph 2.7. As with Income Support, the Department also attributes the improvement in performance in 2002-03 to the impact of the initiatives taken as noted in my report last year. However, the eight per cent error rate in decision making remains a cause for concern. The Department has told me that to improve performance further it has reviewed and updated its training and guidance and introduced further quality review measures. The Department has also told me that as a consequence of these initiatives decision making results for the first quarter of 2003-04 have improved. Again I intend to review the position during the 2003-04 audit.

2.11 The types of decision making errors in Jobseeker's Allowance during 2002-03 are summarised in Figure 3.

Disability Living Allowance

2.12 Disability Living Allowance is a non-means tested, non-contributory, non-taxable benefit, providing a weekly fixed sum to assist claimants with their disabled needs. Claimants must be under the age of 65 at the date of the initial application. The benefit has two components:

- **Care component** - to help a claimant at home in tending to his personal care requirements or to provide for supervision to prevent danger to himself or others. Claimants must also have needed the help or supervision for at least three months and be likely to continue this need for a further six months.
- **Mobility component** - to help a claimant with mobility problems outdoors or to provide for outdoor supervision to prevent danger to himself or others. This help must be due to the claimant suffering from a physical or mental disablement. Claimants must also have needed the help or supervision for at least three months and be likely to continue this need for a further six months.

Expenditure on Disability Living Allowance in 2002-03 was £478 million.

2.13 Figures 1 and 2 indicate mixed results for Disability Living Allowance during 2002-03. The payment accuracy rate achieved for 2002-03 (87 per cent) is below target (90 per cent) for the first time since 1998-99. The Department has advised me that the accuracy rate has been affected by its difficulty in producing case papers within agreed timescales, which has resulted in cases being classified as in error, and by delays in the provision of information by third parties. It also noted its concern about the slippage in performance in this area and anticipates that new improved technology and the reorganisation of disability benefits should improve both the accuracy standards and the time taken to process claims and appeals.

2.14 Although the decision making standard achieved of 88 per cent exceeded the benchmark of 83 per cent and was above the 2001-02 actual achievement of 81 per cent, I note the Standards Committee comment, however, that the target could have been more robust and that this has been remedied for 2003-04. As noted in paragraph 2.7, the improvement in 2002-03 can be attributed to the change in reporting methodology and, in the Department's view, to the impact of the initiatives taken as noted in my report last year. To improve performance on both payment accuracy and decision making further the Department has told me it proposes to build further on the measures and initiatives put in place last year, particularly targeting those areas most prone to error, for example, standards of evidence gathering. The problem with producing case papers will be addressed by exploiting the opportunities afforded by the Modernisation Programme underway in the Disability and Carers Service. I will keep the position under review during next year's audit.

2.15 The types of decision making errors arising for Disability Living Allowance are summarised in Figure 3.

Types of Decision Making Errors

2.16 The decision making check examines the following main areas:

- Evidence - is there enough evidence on which to base a decision?
- Determination of questions - have all relevant questions been decided?
- Fact Finding - have the correct facts been found from the evidence available at the time of the decision?
- Interpreting and applying the law - has statute law and case law been correctly interpreted and applied?

2.17 Figure 3 below provides details of the percentage of errors identified in each of the above areas in 2002-03 for Income Support, Jobseeker’s Allowance and Disability Living Allowance. The majority of the errors relate to fact finding and interpreting and applying the law which in my view appears to be reasonable given the complexities of the benefit systems and the subjectivity involved in deciding an award.

Figure 3: Types of Decision Making Errors in 2002-03

Benefit	Evidence % of overall errors	Determination of Questions % of overall errors	Fact Finding % of overall errors	Interpreting and applying the law % of overall errors
Income Support	10%	19%	35%	35%
Jobseeker's Allowance	14%	33%	5%	48%
Disability Living Allowance	29%	20%	48%	4%

Financial Accuracy

2.18 From April 2002 new Ministerial financial accuracy targets were introduced for Income Support, Jobseeker's Allowance and Disability Living Allowance. Based on the payment accuracy results (Figure 1), the new target reflects the financial value of benefit paid accurately and was set at 95% for all three benefits in 2002-03. Figure 4 below summarises the 2002-03 performance against target.

Figure 4: Financial Accuracy Performance 2002-03

Benefit	Financial Accuracy	Target
Income Support	97%	95%
Jobseeker's Allowance	98%	95%
Disability Living Allowance	91%	95%

2.19 I note that the target has been exceeded for both Income Support and Jobseeker's Allowance. However the performance achieved for Disability Living Allowance is disappointing (see paragraph 2.21). The estimated monetary value of the financial error arising for each of these three benefits is summarised in Figure 5 below.

Figure 5: Estimated Monetary Value of Error 2002-03

Benefit	Estimated Monetary Value of Error £M @ 31.3.03	Overpayments £M @ 31.3.03	Underpayments £M @ 31.3.03
Income Support	16.8	12.9	3.9
Jobseeker's Allowance	2.0	1.8	0.2
Disability Living Allowance	43.6	29.2	14.4
Total	**62.4**	**43.9**	**18.5**

2.20 This is the first year the Agency has used a common Income Support and Jobseeker's Allowance sample for testing payment accuracy/decision making and for Benefit Review purposes. However, as new claims and dormant cases are not deemed suitable for visits, the sample for Benefit Review purposes is slightly smaller than that used for Payment Accuracy and Decision Making. This has led to differences between the Income Support and Jobseeker's Allowance estimated monetary value of errors figures reported in Figure 5 and the official error figures reported in Figure 7.

2.21 While the estimated monetary value of errors in Income Support and Jobseeker's Allowance payments is disappointing, I am particularly concerned about the £43.6 million error estimated by the Agency for Disability Living Allowance payments in 2002-03. The Department has advised me that the main reasons for the high level of estimated error are the extremely complex nature of this particular benefit and its difficulty in producing case papers within agreed timescales, which has resulted in cases being classified as in error. It has also told me that the initiatives outlined in paragraph 2.14 to improve payment accuracy performance on Disability Living Allowance will automatically impact on the monetary value of errors.

Benefit Review

2.22 The Agency's programme of benefit reviews is designed to produce reliable information on the level of fraud and incorrectness in benefit awards by means of in-depth examinations of the circumstances of random samples of claimants. The programme also provides information on types of fraud which helps the Agency target its anti-fraud measures.

2.23 The Department's Statistics and Research Branch calculates the Agency's estimate of fraud and error. A sample of benefit payments is chosen from all monthly payments. After examination, Standards Assurance Unit staff independent of the review carry out a two-tier validation exercise. My staff have carried out test checks on a number of individual cases and I am content with the Agency's classification of error and fraud.

2.24 The Agency estimates that in 2002-03 there are significant losses in Income Support, Jobseeker's Allowance and Housing Benefit as a result of errors by officials, errors by customers and fraud. The estimated level of fraud and error is summarised in Figure 6.

Figure 6: Benefit Review 2002-03: Estimated Level of Fraud and Error

Benefit	£million*
Income Support	£37.5 (5.5%)
Jobseeker's Allowance	£11.9(11.6%)
Housing Benefit	£27.9 (8.2%)
Total	**£77.3 (6.9%)**

* Estimated level of fraud and error and percentage of expenditure

Income Support/Jobseeker's Allowance

2.25 As Figure 6 indicates, the Agency estimates that losses through error and fraud in Income Support and Jobseeker's Allowance during 2002-03 were £49.4 million, which represents 6.4 per cent of expenditure on these two benefits compared to £68.8 million (7.8 per cent of expenditure) at March 2002. Losses in Income Support amounted to £37.5 million, which represents 5.5 per cent of expenditure compared to an estimated loss of £55.4 million at March 2002 (8.4 per cent of expenditure). Losses in Jobseeker's Allowance amounted to £11.9 million, which represents 11.6 per cent of expenditure compared to an estimated loss of £13.4 million at March 2002 (11.6 per cent of expenditure).

2.26 Figure 7 below summarises the level of fraud and incorrectness reported by the Agency in its two most recent reviews of Income Support and Jobseeker's Allowance. I note that suspected and customer fraud has decreased significantly from £39.5 million at March 2002 to £13.1 million at March 2003 and £12.7 million at March 2002 to £10.5 million at March 2003 in Income Support and Jobseeker's Allowance respectively. While the improvement in Income Support is encouraging, £13.1 million of estimated fraud is, in my view, unacceptable. The Department has advised me that greater consistency has been achieved by the Agency across Social Security Districts due to management restructuring and more experienced staff. This and the programme of interventions has led to improved performance in this area. In my view, the Agency must continue to make every effort to identify and prevent social security fraud and error.

Figure 7: Income Support and Jobseeker's Allowance Incorrectness Due to Fraud and Error

	Income Support				Jobseeker's Allowance (Income Based)			
Category	**Estimated Financial Error* £M @ 31.3.03**		**Estimated Financial Error* £M @ 31.3.02**		**Estimated Financial Error * £M @ 31.3.03**		**Estimated Financial Error * £M@31.3.02**	
Customer Fraud	5.9	(0.9%)	13.4	(2.0%)	7.8	(7.6%)	7.6	(6.6%)
Suspected Fraud	7.2	(1.0%)	26.1	(4.0%)	2.7	(2.6%)	5.1	(4.4%)
Customer Error	9.4	(1.4%)	10.4	(1.6%)	0.3	(0.3%)	0.4	(0.3%)
Official Error	15.0	(2.2%)	5.5	(0.8%)	1.1	(1.1%)	0.3	(0.3%)
Total	**37.5**	**(5.5%)**	**55.4**	**(8.4%)**	**11.9**	**(11.6%)**	**13.4**	**(11.6%)**

* Estimated annual expenditure error and percentage of expenditure

2.27 I am concerned to note from Figure 7 that the official error figures for both Income Support and Jobseeker's Allowance have risen since March 2002. The Department has told me that both the change in methodology reported in paragraph 2.20 and the appointment of new and inexperienced staff have led to this increase.

Housing Benefit

2.28 Housing Benefit, which is administered by the Northern Ireland Housing Executive, is paid to tenants of rented properties who are receiving Income Support and income based Jobseeker's Allowance who qualify without a further means test and to other people who are liable to pay rent who may qualify on a means test. Expenditure on Housing Benefit in 2002-03 was £339 million.

2.29 The Social Security Agency published its first rolling benefit review on Housing Benefit in May 2002 covering the period July 2001 to December 2001. The next report covered a period of twelve months ending June 2002 which has been used to establish a baseline against which future comparisons can be made and the Agency has recently published its report for the year ending 31 March 2003.

2.30 The Agency's report estimates that losses through error and fraud on Housing Benefit in 2002-03 amounted to £27.9 million or 7.5 per cent of total expenditure, of which £20.2 million relates to customer and suspected fraud. These figures are of concern and the Department has told me that to address the issue the Northern Ireland Housing Executive has developed a programme of initiatives to enhance closer working relationships with the Agency's Benefit Investigation Unit and has embarked on joint fraud awareness training for Executive staff. A process of risk assessment has been introduced aimed at identifying areas of high risk in relation to both fraud and error and developing measures to address these risks. In addition, there has been a relatively high influx of new staff involved in the assessment of Housing Benefit claims recently and a training programme for these staff has now been put in place. Refresher training has also been provided for existing staff in view of the high rate of change in Housing Benefit policy and legislation. I intend to keep the implementation and impact of these initiatives under review during the 2003-04 audit. A summary of the levels of incorrectness from each of the reports referred to in paragraph 2.28 is provided in Figure 8.

Figure 8: Housing Benefit Incorrectness Due to Fraud and Error

Category	**Estimated Financial Error* £M** 6 months ending December 2001		**Estimated Financial Error* £M** 12 months ending June 2002		**Estimated Financial Error* £M** 12 months ending 31 March 2003	
Customer Fraud	£4.6	(1.5%)	£7.0	(2.1%)	£7.0	(1.9%)
Suspected Fraud	£2.0	(0.6%)	£21.9	(6.7%)	£13.2	(3.6%)
Customer Error	£2.5	(0.8%)	£2.7	(0.8%)	£2.0	(0.4%)
Official Error	£0.9	(0.3%)	£3.7	(1.1%)	£5.7	(1.6%)
Total	**£10.0**	**(3.2%)**	**£35.3**	**(10.7%)**	**£27.9**	**(7.5%)**

* Estimated annual expenditure error and percentage of expenditure

2.31 I consider the total estimated level of incorrectness on Income Support, Jobseeker's Allowance and Housing Benefit to be unacceptably high.

Programme for Government - Public Service Agreement Targets

2.32 The Northern Ireland Executive, in April 2001, presented its first Programme for Government which sets out in detail its plans and priorities for the following three years. Detailed Public Service Agreements (PSAs) for each of the departments that made up the Northern Ireland Executive are an integral part of the Programme for Government. These set out specific actions and targets linked to budgets and are designed to increase accountability through providing the Northern Ireland Assembly and the public with a clearer sense of what the Northern Ireland Executive plans to achieve within the resources available.

2.33 Within the Department for Social Development's PSA, the Social Security Agency's key priorities have been identified as: an improvement in accuracy levels, to implement the Welfare Reform and Modernisation Programme and to reduce by 5 per cent benefit losses from fraud and error in Income Support, Jobseeker's Allowance and Disability Living Allowance (and other benefits) during the three year period ending 2002-03. The baseline from which the reduction is to be measured is a loss of 7.1 per cent of Income Support expenditure measured at February 1999 and 7.4 per cent of Jobseeker's Allowance payments measured at February 2000. Figure 9 below shows the results achieved against these baseline figures.

Figure 9: Fraud and Error Recorded Measured Against PSA Target

Benefit	Baseline	2000-01 achieved	2001-02 PSA target	2001-02 achieved	2002-03 PSA target	2002-03 achieved	5% reduction achieved in 2002-03
Income Support	7.1% (Feb.1999)	6.5%	6.3%	8.4%	5.95%	5.5%	YES
Jobseeker's Allowance	7.4% (Feb.2000)	8.3%	6.66%	11.7%	6.29%	11.6%	NO

2.34 While I am pleased to note that the PSA target was achieved for Income Support in 2002-03 as detailed in Figure 9, performance for Jobseeker's Allowance is still significantly below target. I intend to keep this matter under review.

Limitation in Audit Scope - Child Benefit Payments: Absence of Supporting Documentation.

2.35 My report on the 1999-2000 Vote 18 Appropriation Account (NIA 36/00) detailed the circumstances surrounding the absence of supporting documentation for a significant proportion of Child Benefit payments. Expenditure on Child Benefit in 2002-03 was £306 million.

2.36 During 2002-03 a significant number of Child Benefit cases were again unavailable for testing due to the Agency's former policy to retain supporting case documentation on new Child Benefit cases for only two years, after which period it was destroyed. Measures put in place by the Social Security Agency through the implementation of its Security and Quality Assurance Project and the policy to retain sufficient case documentation for new Child Benefit awards has enabled both my staff and staff of the Standards Assurance Unit to test new claims since 2000-01. However, I remain concerned that without the appropriate supporting documentation the Department was unable to fully review individual benefit awards and adequately test payments relating to cases started before 2000-01.

2.37 As a result of the problems described in paragraph 2.36, I have been unable to obtain all the information and explanations that I consider necessary for the purpose of my audit or determine whether proper accounting records had been maintained or whether payments made were regular. Consequently, I have decided to qualify my audit opinion on the account on the basis of limitation in scope.

2.38 Responsibility for the administration of Child Benefit transferred to the Inland Revenue with effect from 1 April 2003 therefore from 2003-04 this issue will no longer impact on the DSD Resource Accounts.

Summary of Results

2.39 My audit included an examination of the work undertaken by the Agency's Standards Assurance Unit by reperforming a sample of cases. The Unit administers the

Agency's Benefit Review process and works to improve and maintain the standard of decision making and payment accuracy. My staff examined and reperformed a sample of the Unit's work during 2002-03 and I am content that the work undertaken was to a good standard and the results produced by the Unit are accurate and complete. I will continue to monitor payment accuracy and decision making, and Benefit Review results, and will report in due course, if necessary.

2.40 Through the benefit review process and the Agency's payment accuracy work, the Department estimates that in 2002-03 there are significant losses on benefits totalling £120.9 million. This comprises £37.5 million in Income Support, £11.9 million in Jobseeker's Allowance and £27.9 million in Housing Benefit (Figure 6) as a result of errors by officials, errors by customers and fraud and an estimated monetary value of error in Disability Living Allowance of £43.6 million (Figure 5). As a result I have decided to qualify my audit opinion on the account due to this significant level of estimated fraud and error.

2.41 Where appropriate I have noted changes in the Agency's reporting methodology for decision making, payment accuracy and Benefit Review results in this report. I intend to keep this matter under review during the audit of the 2003-04 account.

2.42 Before April 2000, it was the Agency’s policy to retain supporting case documentation on new Child Benefit claims for only two years, after which period it was destroyed. Although Child Benefit Office put measures in place to retain supporting case documentation in line with the Agency’s agreed documentation retention policy, the Standards Assurance Unit was unable to fully review a significant proportion of the total Child Benefit payments of £306 million. Consequently, I have decided to further qualify my audit opinion on the account on the basis of limitation in scope.

Impact of the Level of Fraud and Incorrectness on the Account and Audit Opinion

2.43 In forming my audit opinion I am required to confirm that the account is free from material misstatement, whether caused by error, fraud or irregularity. I have qualified my audit opinion on the account due to the level of estimated fraud and incorrectness in Income Support, Jobseeker's Allowance and Housing Benefit (paragraphs 2.22 to 2.31) and Disability Living Allowance (paragraphs 2.18 to 2.21) and also due to the limitation in audit scope in Child Benefit payments (paragraphs 2.35 to 2.38).

Part 3: Qualified Audit Opinion Arising From Weaknesses in Financial Control and Monitoring of Expenditure in Relation to Grants to Registered Housing Associations

Request For Resources B : Promoting Measurable Improvements To Housing In Northern Ireland

Introduction

3.1 The Departmental Resource Account (Request for Resources B) provides for expenditure by the Department for Social Development on Housing Association Grant (HAG) to registered Housing Associations. While the Department is responsible for the payment of grant, it has devolved the control and monitoring of expenditure to the individual Housing Associations by way of 'Self Certification' procedures (paragraph 3.9 and Appendix 3). The primary means through which the Department achieves regulation and monitoring through its Housing Associations Branch (excluding the Northern Ireland Co-Ownership Housing Association (see paragraph 3.18)) are:

- Registration - the criteria for registration of new Associations;
- Scheme approval - schemes submitted for approval must conform to the requirements of the Housing Association Guide;
- Performance returns - performance documentation issued by and returned to the Department;
- Investigation/Verification Visits - verification and investigatory visits are carried out following return of performance documentation; and
- Scheme Audits - the process by which the Department checks the validity and accuracy of the certifications given by an Association as part of the scheme work procedures. The Department also monitors the consistency of the housing produced in line with the Department's Design and Contracting Requirements.

A glossary of terms is provided in Appendix 1.

3.2 My audit of grants to Housing Associations in 2002-03 was undertaken in accordance with Section 22 of the Government Resources and Accounts Act (NI) 2001. Following the provision of access rights through the 2001 Act to public bodies such as Housing Associations, I decided to follow up my audit in 2001-02 by examining a further sample of schemes which were completed during 2002-03 and in respect of which HAG had been paid to Housing Associations (paragraph 3.11).

Background

3.3 One of the Department's key strategic objectives is 'to promote measurable improvements to housing in Northern Ireland'. In relation to the payment of grant to Housing Associations, the Department is responsible for the issue of guidance and policy directives to them. In addition, it has a statutory duty to consult with representative housing association bodies.

3.4 Registered Housing Associations were first set up in 1976. There are 39 Housing Associations in Northern Ireland providing social housing for rent, and one, the Northern Ireland Co-Ownership Housing Association, which provides the opportunity for those on low income to become homeowners. A Housing Association is defined under the Housing (Northern Ireland) Order 1992 as a society, body of trustees or company which:

- is established for the purpose of providing, constructing, improving or managing, or facilitating or encouraging the construction or improvement of housing accommodation; and
- does not trade for profit or whose constitution or rules prohibit the issue of capital with interest or dividend exceeding such rate as may be prescribed by the Department of Finance and Personnel, whether with or without differentiation between share and loan capital.

3.5 Prior to 1996, primary responsibility for the provision of general family social housing in Northern Ireland rested with the Housing Executive. Up until that time, Housing Associations had been the principal providers of purpose built accommodation for people with special needs and also provided significant numbers of general needs housing for families and single people. The Housing Policy Review of 1996 transferred responsibility for all future new build social housing provision to Housing Associations. Housing Associations therefore now build all new general and special needs housing in Northern Ireland. The Housing Executive retains a responsibility to develop in circumstances where Housing Associations are unable to do so.

Housing Associations Grant Scheme

Objectives

3.6 The Housing (NI) Order 1992 introduced new mixed funding arrangements for Housing Associations undertaking scheme development. The legislation and the operational framework mirrored that introduced in 1989 by the Housing Corporation in England and Wales. The Housing Corporation is a Non Departmental Public Body sponsored by the Office of the Deputy Prime Minister. A prime policy objective of the legislation and operational framework is the provision of social housing by Housing Associations with maximum private finance input. The key components of the scheme are:

- an increase in the volume of social housing provided from public funds;

- the introduction of private finance to fund a portion of development costs;
- a fixed grant rate and cost control mechanism; and
- the introduction of a system of tranche payments based on 'certifications' made by Associations to avoid the need to draw down private finance before practical completion and the commencement of the rental income. Since the introduction of mixed funding in 1992, £203 million of private finance has been levered in.

3.7 The process of providing social housing involves a number of key players, namely:

- Department for Social Development (DSD);
- Registered Housing Associations;
- Northern Ireland Housing Executive (NIHE);
- Health Trusts and Boards; and
- Northern Ireland Federation of Housing Associations (NIFHA).

The roles and responsibilities of each of the above are detailed in Appendix 2 to this report.

Other key players are:

- Private sector (in financing, designing and building);
- Voluntary sector (in managing special needs housing); and
- Other statutory bodies and initiatives.

Operation of the Scheme

3.8 The provision of general social housing is funded through a mix of grant; approximately 70 per cent is paid by the Department and the remainder through private finance. Special needs housing attracts 100 per cent Departmental grant funding. In 2002-03 the amount of Housing Association Grant paid to Housing Associations who provide accommodation for rent in Northern Ireland was some £50.5 million cash (£52.6 million resource).

3.9 The objective of the system is to maximise the use of private finance in conjunction with grant in order to produce more social housing. The 1996 Housing Policy Review concluded that for every two houses built under the fully subsidised arrangements, Housing Associations with the facility for private finance could build three. The Department's approval system is designed to streamline the development process and relies on a process of 'certifications' by Associations to pay grant. Payment of grant to a Housing Association is triggered when it 'certifies' that the following three stages have been completed:

- Acquisition - deemed to be where the association has a contract with the vendor to take ownership of the site/property;

- Start on Site - deemed to be the date when the contractor took possession of the site/property; and
- Practical completion deemed to be the contract date when the Association took possession of the dwelling or when purchase is completed.

The certification framework was introduced to reduce bureaucracy and to require Housing Associations to take a greater share of the risk in developing schemes, thus giving them the incentive to develop more efficiently. A summary of the various certifications that Housing Associations have to declare is provided in Appendix 3.

3.10 There are two main components of the new capital grant system comprising:

- Total Cost Indicators (TCI); and
- Fixed Grant Rates.

Both components are applied in determining the appropriate amount of grant for each scheme with the objective of securing good value for money. Total Cost Indicators are 'norm costs' which allow for the development of a housing scheme to acceptable standards. They reflect the total cost of provision, including an allowance for on-costs such as professional fees and associated staff and overhead costs. The Fixed Grant Rates establish the normal percentage of grant input into schemes and reflect the likely income achievable from affordable rents and differing management and maintenance costs.

Audit Approach

3.11 On the basis of the serious weaknesses in financial control identified by my audit in 2001-02, I decided to focus my 2002-03 audit on reviewing the work of the Department's Scheme Audit function (paragraphs 3.13 to 3.17) and specifically testing the operation and adequacy of key financial controls by examining a further sample of schemes (paragraphs 3.23 to 3.34). In this regard, my examination focused on schemes where development had been completed and final grant payments made during 2002-03. This involved reviewing each scheme from application and approval stage, with particular emphasis on:

- the extent to which Housing Associations had complied with the certifications made to the Department;
- the procurement and tendering procedures adopted for professional consultants, contractors and other services;
- the monitoring and control of schemes, including all financial aspects, exercised by Housing Associations; and
- the control and monitoring of the schemes exercised by the Department.

I also reviewed the operation of the Northern Ireland Co-Ownership Housing Association (paragraphs 3.18 to 3.20) and the introduction of Constructionline in relation to Housing Association contracts (paragraphs 3.21 and 3.22).

3.12 Due to other priorities, the Department's Internal Audit Unit had to defer two planned audits in this area during 2002-03. Both audits (Follow up review of Housing Associations Branch and an audit of the Northern Ireland Co-Ownership Housing Association) are now under way in the current year and I intend to review the results during my 2003-04 audit.

Audit Findings

Review of Scheme Audit

3.13 The Department's control and monitoring of Housing Association Grant is primarily carried out by Housing Associations Branch.

3.14 The Scheme Audit Team was established in 1998 as an integral part of the new funding arrangements. The process followed by Scheme Audit ensures that Associations are accountable for the public funds they receive and provides assurance to the Department's Accounting Officer that funds are not being exposed to unreasonable risk. Since April 2002, Scheme Audit work has been divided into:

- Development Compliance Audit which focuses on the development issues of schemes with emphasis on the certification process and ensuring that schemes are controlled and monitored by Associations in line with the Housing Association Guide; and
- Minor Works and Validation Audit which aims to confirm that minor issues agreed during the previous development compliance audit have been fully addressed. This includes issues on procurement and procedural requirements and scheme design requirements.

3.15 Where Scheme Audit highlights any significant weaknesses the Department may impose sanctions on a Housing Association by way of reducing financial support or removal from the grant scheme. There are currently six Housing Associations suspended from receiving further scheme approvals as a result of Development Compliance Audits until they can demonstrate that they have introduced acceptable remedial action.

3.16 Following the introduction of the new audit arrangements, Scheme Audit issued nine reports, of which six have been finalised, to individual Housing Associations during 2002-03. Issues raised have included:

- a lack of a formal Procurement Policy within some Associations;
- management committee minutes did not always indicate approval for major development decisions being taken;

- the Department's requirements regarding prompt payment were not always fully implemented by Associations;
- the selection, appointment and briefing of consultants was not always in line with the prescribed guidance;
- in relation to competitive tendering, the contractor selection procedures operated by some Associations did not always follow the relevant guidance; and
- building contracts were not always signed and dated by both parties before works commenced on site.

3.17 My staff reviewed the work of Scheme Audit during the year by examining a number of development compliance and validation audit files. Their work was found to be comprehensive, well structured and well focused. Issues raised were prioritised in terms of importance and good procedures are in place to ensure subsequent follow up of issues raised and implementation of remedial action by Associations. I intend to review the work of Scheme Audit further as part of my audit of the 2003-04 account.

Review of Northern Ireland Co-Ownership Housing Association

3.18 The Northern Ireland Co-Ownership Housing Association (NICHA) was established in 1978 to contribute towards meeting housing need through the promotion and development of the concept of equity sharing (shared ownership) in the private housing sector. It achieves this through the Co-Ownership Scheme. This provides access to home ownership for those who would otherwise enter or remain in rented accommodation, including some existing owner occupiers when their circumstances change for the worse.

3.19 Purchasers take as large a share as they can afford to start with, that is, 50 per cent, 62.5 per cent or 75 per cent, and can increase their share at any time. The larger their share the lower the rent they pay to NICHA. Properties can be sold at any time provided that the purchase price is acceptable to NICHA's valuer.

3.20 As part of the audit my staff examined two property purchases and two sales and noted that financial controls are generally operating satisfactorily. I note, however, that the Association:

- has not been issued with detailed procedural guidance since 1985 (other Associations must comply with the Housing Association Guide);
- is not subject to Scheme Audit; and
- finds it difficult to plan ahead as they are not made aware of the total funding that will be allocated to them until a late stage in the financial year.

The Department has told me that it is currently updating the procedural guidance for the Association. In addition, while NICHA is not subject to Scheme Audit the Department has also told me that it carries out a number of performance and financial checks on the Association and anticipates that NICHA will come under the remit of the proposed

Regulatory and Inspection Unit (paragraph 3.36). In relation to the funding issue, the Department has told me that it is concerned at the levels of funding which are allocated to the Co-Ownership scheme and has commissioned specific research aimed at demonstrating the benefits of the scheme and what it considers to be the excellent value for money it offers to the public purse. I intend to keep these issues under review and will report in due course if necessary.

Review of Construction line

3.21 Constructionline is a Public Private Partnership between Government and Capita Business Service. With effect from 1 November 2002, the single register replaced all existing pre-qualification arrangements for the selection and appointment of consultants and contractors. This change was necessary to comply with the Northern Ireland Executive's policy that all Northern Ireland Government Contracting Authorities, Public Sector Bodies and organisations receiving the majority of its funding from Government sources must use a common UK-wide register of consultants and contractors. Clearly, this includes Housing Association schemes where the Department for Social Development is providing the majority or part of the capital funding. The Department anticipates that the register should reduce the financial and administrative burden on Housing Associations and advice has been issued to Associations on the implementation of this new policy.

3.22 As noted in paragraph 3.11 my staff examined schemes where development had been completed and final grant payments made during 2002-03. It follows, therefore, that Constructionline had not been applied on any of the schemes examined and I have not yet been able to form an opinion on its effectiveness. I intend to review the implementation and application of Constructionline as part of my audit of the 2003-04 account.

NIAO Examination of Scheme Payments

3.23 My staff selected a sample of 15 schemes for examination from a total of 79 schemes on which the final tranche payment was made during 2002-03. In addition, one Special Needs Management Allowance scheme and one Voluntary Purchase Grant scheme were also examined. This involved eleven Housing Associations and the sample included the types of contract as set out in Figure 10.

Figure 10 : Schemes Examined by NIAO

In addition, the sample included both tariff and non-tariff funded Housing Associations, large and small, urban and rural.

Housing Association	Scheme Type	Contract Type
Oaklee	(a) New Build Special Needs (b) New Build General and Special Needs (c) Rehabilitation Scheme	(a) Competitive Tendering (b) Negotiated Tendering (c) Competitive Tendering
Dungannon & District	(a) New Build General Needs (b) Special Needs Management Allowance	(a) Package Deal (b) Special Needs
Presbyterian	New Build General Needs	Competitive Tendering
Ulidia	(a) New Build General Needs (b) New Build General Needs Transfer Scheme	(a) Competitive Tendering (b) Competitive Tendering
Filor	(a) Rehabilitation Scheme (b) Voluntary Purchase Grant scheme	(a) Competitive Tendering (b) Voluntary Purchase
Habinteg	(a) New Build Special Needs (b) New Build General Needs	(a) Design & Build (b) Design & Build
Open Door	New Build Special Needs	Design & Build
Ballynafeigh	Rehabilitation Scheme	Competitive Tendering
Belfast Community	Off the Shelf New Build General Needs	Not Applicable
Ark	New Build Special Needs	Competitive Tendering
South Ulster	New Build General Needs Transfer Scheme	Negotiated Tendering

3.24 The review of the sample of schemes this year has highlighted a significant number of good practice issues which are either already operated by Housing Associations or have been identified by my audit. We have brought these to the Department's attention with a view to consideration being given to disseminating the issues across the Housing Association network. There are, however, a number of other issues which arose from my audit which are detailed in paragraphs 3.25 to 3.34 below.

Inaccurate and Inapplicable Certifications made by Housing Associations

3.25 Housing Associations make their application for Housing Association Grant (HAG) in separate tranche claims at acquisition, start on site and practical completion stages (see paragraph 3.9). When making their application they must certify that they have undertaken a number of specific actions and ensured certain essential requirements have been put in place, as stipulated by the Department. A summary of the relevant certifications is at Appendix 3.

3.26 From the examination of the sample of schemes my staff identified a number of instances where Housing Associations had failed to (i) inform the Department where individual certifications had not yet actually been met; and (ii) delete certifications which were inapplicable to particular schemes. In both instances, Associations had also failed to provide explanations to the Department as required as a condition of grant. I am concerned that some of the failures noted remained after the Department's audits had previously brought them to the Associations' attention. Examples of certifications which had not been met at the time of payment claim and not notified to the Department are:

- outline or full planning permission had not been obtained at application, and/or acquisition and/or start on site certification stage;
- Economic Appraisals had either not been completed or not completed at the right time;
- valuation of land had been carried out retrospectively, that is, after contract price was agreed and project approval given;
- no long term assessment of the financial viability of schemes had been undertaken; and
- building contracts had not been signed to formalise them.

Non Adherence by Housing Associations to Departmental Procedures

3.27 Housing Associations are required to follow procedures and best practice contained in the Housing Association Guide issued by the Department. The Guide sets out the requirements which Housing Associations must follow in relation to Health & Safety regulations, procedure, design and procurement. My staff identified instances where by not adhering closely to the requirements, Housing Associations may have exposed funds to the risk of claims by third parties. This included Health & Safety plans not agreed, approved and/or not in place when contractors went on site.

3.28 In addition, instances were highlighted where I am concerned that Housing Associations did not follow Departmental guidelines in relation to the tendering and award of contracts. For example, my staff noted that:

- the award of contracts and services was in some instances based only on an Association's knowledge and past experience of contractors, etc;

- tender reports did not always have the level of detail required to adequately support the rationale for contractor selection;
- a number of tenders submitted and accepted did not include a prompt payment certificate; and
- in one particular case where an Association maintained a Select List of 29 contractors, only two were invited to tender and the only contractor who actually submitted a tender was accepted.

3.29 The examination of scheme files also revealed that Associations did not always adequately vet building contractors in line with the guidelines, for instance, to:

- confirm their financial standing and capacity to undertake schemes;
- confirm that they held tax exemption and employer/employee public liability insurance; and
- check their VAT status and adequacy of their fair employment policies.

3.30 Other areas of non-adherence to guidelines by Housing Associations related to:

- the appointment and briefing of consultants. On a number of occasions inadequacies were found in design and build briefs which fell short of Housing Association Guide requirements and in letters of appointment which did not always specify the services to be provided and the terms and conditions of appointment;
- the completion of Economic Appraisals. Not all Associations followed the basic steps for completion of Economic Appraisals outlined in the Housing Association Guide; and
- non-compliance with energy efficiency guidance. Under the Design Advice Scheme, Associations must provide an independent energy efficiency report on all new build schemes and rehabilitation in excess of 500 square metres. A number of instances of non-compliance were noted.

Insufficient evidence to support key decisions taken by Housing Associations

3.31 The examination of scheme files also highlighted various instances where there was little evidence to support the rationale behind key decisions taken by Housing Associations. Examples are:

- where appointed consultant architects and/or quantity surveyors were responsible for evaluating applications for inclusion on select lists, evaluating tenders and recommending contractors for selection, Housing Associations did not always ensure that sufficient evidence was made available to them to support the decisions and recommendations made;
- in two cases the rationale for selecting a package deal procurement option was not clearly documented;
- in another case where the negotiated tender option was used there was no clear evidence to support either the procurement route followed or the figure agreed;
- decisions taken during site meetings regarding the monitoring of progress of schemes were not always documented on file; and
- while all the Associations visited during the audit retained minutes of their management committee meetings, the level of detail varied significantly. In a number of instances there was no evidence to support key decisions taken with regards to individual schemes, for example, with regards to specific design and build requirements, contractor selection, the approval of schemes and contract variations.

Insufficient Control and Monitoring of Schemes by Housing Associations

3.32 The Housing Association Guide requires Housing Associations, as part of the Economic Appraisal process, to monitor progress of schemes during development against plans and specification forecasts, and evaluate any variations against the appraisal conclusions. In addition, Housing Associations are required to evaluate construction and refurbishment costs as soon as possible after scheme completion.

3.33 As I have already indicated, Housing Associations largely devolve the process of contractor selection and the control and monitoring of schemes to their appointed consultants. Housing Associations commented that consultants are engaged for their expertise, local knowledge and professional judgement and as a result they are content to place reliance on their decisions. Nevertheless, I would expect Housing Associations not to be over-reliant on consultants. Specific examples of where insufficient control and monitoring of schemes may have led to risks arising are:

- a failure to ensure that relevant insurance cover was renewed during the lifetime of schemes;
- incomplete contract documentation, for example, in relation to the main contractor's treatment of prompt payment by sub-contractors and suppliers; the retention percentage was incorrect in one scheme contract; and
- on a number of occasions documentation had to be obtained by Associations from

consultants to enable my staff to complete their review. This highlights the need for Associations to ensure that all key documentation relating to individual schemes is retained on their scheme files for proper monitoring purposes.

The Department has told me that consultants have to be appointed by Housing Associations because of their lack of expertise in relation to the variety of works associated with any building scheme. However, I consider that Housing Associations should work with and challenge consultants and the Northern Ireland Housing Executive Design Groups to ensure good value for money is obtained.

Inadequate Departmental Control and Monitoring

3.34 The audit highlighted some weaknesses in relation to the Department's control and monitoring of grant paid to Housing Associations. Examples are:

- a lack of monitoring by the Department over the certifications given by Housing Associations at site acquisition, pre-completion and pre-approval and payment authorisation stages. In particular, the Department did not undertake any checks on the certifications made by Housing Associations by reviewing supporting documentation. However, from February 2003 the Department introduced a new evidence based certification process, which required Housing Associations to provide supporting documentation with their certifications. In addition, the Department undertook a retrospective evidence based check of Housing Associations on certificates submitted from November 2002; and
- an overpayment of voluntary purchase grant due to the Department's lack of challenge of an Association's claim calculation.

Summary of Audit Findings

3.35 My audit findings in paragraph 3.13 to 3.34 indicate that a number of fundamental weaknesses in financial control and monitoring at both Departmental and Housing Association levels remained during 2002-03. However, it is encouraging to note this year that a number of areas of good practice are being operated by some Associations (paragraph 3.24). I have also noted that in a significant number of instances following initial audit visits a number of Associations had already taken action to implement change and strengthen controls by the time of the follow up visits. Clearly, Associations are becoming more aware of their role and responsibility in accounting for the public funds paid to them and I would expect to see further improvement in control and monitoring during my 2003-04 audit.

3.36 As indicated in paragraph 3.14, the work of the Department's Scheme Audit Team was enhanced from April 2002 by dividing it into separate Development Compliance Audit and Minor Works and Validation Audit functions. The Department has told me that as a result of the findings of my 2001-02 audit, a review of the role of Scheme Audit has been carried out by the Department's Business Improvement Unit who recommended that the Scheme Audit remit should be extended to provide a quality assurance function. The Department has also told me that funding for the additional posts indicated by the recommended structure for the New Regulatory and Inspection Unit has been sought and it is the intention that the unit will commence operations with effect from 1 April 2004. In my view, the establishment of such a unit is essential if the control and monitoring of Housing Association Grants is to improve to an acceptable level. I intend to keep this matter under review during my 2003-04 audit.

3.37 I indicated in my report last year (HC 27/NIA 45/02) that the Department was reviewing the Housing Association Guide and that arrangements were being made to consolidate and reissue on an annual basis. The Department has told me that it is on target to complete the review and to have an on-line version of the guide available by mid 2004. In the meantime, urgent or topical guidance issues in the period of the review are being issued as Housing Association Circulars. The guide is clearly a key control and monitoring mechanism and I intend to review the implementation of the new version during next year's audit.

3.38 As I have also indicated in paragraphs 3.20 I intend to keep a number of issues regarding the Northern Ireland Co-Ownership Housing Association under review and report if necessary. In addition, I propose to review the implementation and application of Constructionline by Housing Associations during my 2003-04 audit (paragraph 3.22).

Conclusion

3.39 On the basis of my specific findings in paragraphs 3.13 to 3.34 I have to conclude that the Department's financial controls and monitoring of grants to Housing Associations remain inadequate. In addition, I have concerns over the adequacy of the Housing Associations' financial control and monitoring of expenditure on individual schemes. In the absence of proper controls I am unable to certify that expenditure was applied to the purposes intended and was regular. I have, therefore, decided to qualify my audit opinion accordingly.

Part 4: Qualified Audit Opinion Arising from Weaknesses in Financial Control and Monitoring of Expenditure in Relation to Urban Development and Community Development Grants to Voluntary and Community Bodies

Request For Resource C : Urban Regeneration and Community Development

Introduction and Background

4.1 The Department for Social Development Resource Account (Request for Resource (RfR) C) provides for expenditure by the Department for Social Development on urban regeneration and community development. It provides for physical and social regeneration by way of Urban Development grant in Belfast and Londonderry, expenditure on Comprehensive Development and Environmental Improvement Schemes, grants under the Community Regeneration Improvement Special Programme in urban areas outside Belfast and grant in aid to Laganside Corporation. It also provides for the implementation of the Making Belfast Work and Londonderry Regeneration initiatives, the payment of grants to voluntary bodies, Gap funding and for the facilitation of payments from certain European Funds and Programmes. Much of the expenditure is administered through third parties such as: Intermediary Funding Bodies; community groups; voluntary organisations; and statutory bodies.

Previous Reports

4.2 In November 1997 the Committee of Public Accounts at Westminster reported on the Control of Belfast Action Teams' Expenditure (Sixth Report of the 1997-98 Session, HC 382) following my report on this matter (November 1996, HC 63). Belfast Action Team and Making Belfast Work Initiatives had been amalgamated in April 1995.

4.3 In July 2001 I reported on the outcome of investigations into suspected fraud within the former Suffolk Action Team and the lessons to be learned from the Department's handling of the case (NIA 72/00). I also reported in March 2002 on the measures taken by the Department to recover loans totalling £8 million, which were given to community groups between 1989 and 1996 under the Community Economic Regeneration Scheme and the Community Regeneration and Improvement Special Programme (NIA 59/01). The Public Accounts Committee at the Northern Ireland Assembly considered both reports at an evidence session in June 2002. However, due to the suspension of the Assembly the Committee has not yet issued a report.

4.4 The Department for Social Development published its 2001-02 Annual Report and Resource Account in November 2002 (HC 27/NIA 45/02). I qualified my audit opinion and reported on the Resource Account due to a number of reasons, including the weaknesses found in financial control and monitoring of expenditure in relation to urban regeneration and community development grants to voluntary and community bodies.

Analysis of Expenditure

4.5 Gross expenditure in 2002-03 recorded in the Resource Account Operating Cost Statement against RfR C is £45.4 million (2001-02, £65.0 million), analysed in Figure 11 below:

Figure 11 : Analysis of Request for Resource C Gross Expenditure (excluding non-cash items and accruing resources)

	2002-03		**2001-02**	
	£m	**£m**	**£m**	**£m**
Central administration		6.6		6.0
Urban Regeneration Programmes:				
Belfast Regeneration Office	13.6		13.5	
Regional Development Office	4.3		6.1	
North West Development Office	1.3		4.8	
Laganside Corporation	6.7		7.1	
		25.9		31.5
Grants to voluntary bodies		7.8		7.1
Grants under the EU Peace and Reconciliation Programme to Voluntary bodies, community groups and statutory bodies, including GAP Funding between EU programmes		3.6		14.5
Grants under the European Regional Development Fund to district councils, community groups, statutory bodies and the private sector		0.6		5.5
Grants under the European Social Fund to community groups and executive programme funds		0.5		0.4
Community Initiatives		0.4		-
Total		**£45.4**		**£65.0**

The decreases in 2002-03 EU Peace and Reconciliation Programme expenditure and ERDF grants to district councils, etc were due to delays in starting up a number of new European Union programmes. In addition, the decrease in Urban Regeneration grants made by the Regional Development Office and the North West Development Office during the year was due to slippage on commencing a number of Executive Programmes relating to both capital and current programmes.

Previous Financial Audit Findings

4.6 **1999-00** - this expenditure was accounted for in two separate Appropriation Accounts: Vote 10: Environmental and Other Services and Vote 16: Miscellaneous Health and Personal Social Services. I qualified my audit opinion on both those accounts on the basis of fundamental financial system weaknesses and errors in payments found as a result of testing carried out by my staff (NIA 36/00). I also qualified my opinion on the Vote 16 account on the basis of limitation in scope as, in relation to expenditure under the European Union Special Support Programme for Peace and Reconciliation and on Special Initiatives, I was unable to obtain all the information and explanations that I considered necessary for the purpose of my audit or determine whether proper accounting records had been maintained or whether payments made were regular.

4.7 **2000-01** - expenditure on urban regeneration and community development was solely accounted for in DSD Vote C Appropriation Account: Urban Regeneration and Community Development. I again qualified my audit opinion on that account on the basis that the Department's financial controls and monitoring of expenditure were inadequate. I also qualified my opinion on the account on the basis that, in a wide range of the funding activities covered by the account, the relevant information did not exist to enable me to establish that expenditure was applied to the purposes intended and was regular (NIA 34/01).

4.8 In view of the nature of weaknesses in financial control and monitoring of expenditure which recurred in 2000-01, in April 2002 the Northern Ireland Assembly's Public Accounts Committee invited the Department's Accounting Officer to comment on the actions taken by his Department in response to the findings and conclusions made in my report on DSD Vote C. In his response dated 17 May 2002, the Accounting Officer acknowledged that weaknesses existed and errors had occurred, but indicated that, while the Department had acted upon the recommendations made, progress had not happened as quickly as the Department would have wished mainly due to difficulties in maintaining staff numbers to the desired level. However, as a consequence of the appointment of additional staff the Accounting Officer further indicated that it was felt some good progress had been made to address highlighted weaknesses which, he considered, would result in enhanced business efficiency.

4.9 The Accounting Officer's response also provided an update on the status of the specific measures being implemented by the Department to address the problems identified, as set out in my report on DSD Vote C, together with details of additional measures which have or are being undertaken. These measures represented a significant commitment by the Department in addressing the various weaknesses.

4.10 **2001-02** - expenditure on urban regeneration and community development was accounted for the first time in the Department's Resource Account (HC 27/NIA 45/02). I again qualified my audit opinion on that account on the basis that the Department's financial controls and monitoring of expenditure remained fundamentally inadequate. I also qualified my opinion on the account on the basis that, in a wide range of funding activities for which the Department's Urban Regeneration and Community Development Group (URCDG) is responsible, the relevant information did not exist to enable me to establish that expenditure was applied to the purposes intended and was regular.

Audit Approach

4.11 On the basis of the serious weaknesses in financial control identified over the last three years, I again decided to focus my 2002-03 audit on those areas which I considered to be of greater risk to public funds. These are:

- urban regeneration grants made by Belfast Regeneration Office (BRO) and the North West Development Office. This includes grants under the Making Belfast Work and Londonderry Regeneration Initiatives;
- grants under the EU Special Support Programme for Peace and Reconciliation; and
- grants to voluntary bodies and community groups made by the Department.

4.12 The approach to the audit was threefold:

- a review of the work undertaken by the Department's Internal Audit Unit across URCDG in 2002-03 and an assessment of the impact of the Unit's findings;
- a review of the work of Belfast Regeneration Office's Quality Assurance and Improvement Unit and its Review Panel; and
- specifically testing the operation and adequacy of key financial controls by examining a sample of projects funded by the Department during the year. The findings of my audit are set out in paragraphs 4.13 to 4.33 below.

Audit Findings

Review of Internal Audit work

4.13 The first stage in the investigation process was a review of the work undertaken in 2002-03 on behalf of the Urban Regeneration and Community Development Group (URCDG) by the Department's Internal Audit Unit.

4.14 The programme of work conducted by Internal Audit included an audit of European Union Interim Funding arrangements (or GAP Funding) during 2001-02. The audit covered Interim Funding awarded by the Department in May and June 2001 for the period 1 April 2001 to 31 October 2001 in anticipation of the introduction of the following European

Union Structural Funds:

- Programme for Building Peace and Prosperity, Priority 3: Urban and Social Revitalisation; and
- Peace and Reconciliation II Programme, Priority 2: Social Integration, Inclusion and Reconciliation.

Residual Interim Funding payments continued to be paid during 2002-03. Internal Audit examined all awards during the period and expressed concern on the assessment process carried out in respect of Interim Funding applications, in particular:

- the lack of documentation in support of applications to enable the Department to adequately determine eligibility;
- inadequate weighting of the scoring criteria against European aims and inadequate evidence provided by bodies to support how projects met the eligibility criteria leading to a risk of inappropriate awards of funding;
- inconsistent assessment of applications;
- the risk of duplicate funding from other funding bodies due to the absence of detailed checks to other potential funders; and
- the absence of monitoring and evaluation procedures.

As a result of these findings, Internal Audit gave a 'No Assurance' opinion rating, that is, 'control is generally weak, leaving the system open to significant error or abuse'. This report is a major cause for concern and I note that all the recommendations made by Internal Audit to strengthen controls have been accepted by the Department and implementation is currently ongoing.

4.15 During the year Internal Audit also undertook a follow up high level review of BRO's implementation of the Making Belfast Work (MBW) Initiative. While the report acknowledged that BRO has instigated a comprehensive programme of action, it noted that many financial control/budgeting weaknesses require more attention. A 'Limited Assurance' opinion rating was therefore given, that is, 'weaknesses in the system of control are such to put the system objectives at risk.'

4.16 A follow up audit of BRO (MBW) project payments was also carried out during 2002-03. Despite the introduction of a number of initiatives by BRO aimed at addressing issues previously raised by Internal Audit and NIAO, testing revealed that weaknesses were still occurring. Based on these findings, Internal Audit considered that an opinion rating of ‘No Assurance’ was still applicable. The main concerns raised with management were:

- insufficient evidence to support the decision to award funding;
- bank statements not obtained or analysed to establish if an alternative means of project funding is already available to the group;

- no contact with other funders to establish the need for BRO funding; and

- inadequate vouching of documents.

4.17 Other audits carried out during the year included:

- assignments relating to the European Union Closure Statements under Commission Regulation 2064/97 aimed at expressing an independent opinion on the final declaration of expenditure in respect of the various European Union Funds/Programmes administered by the Department. Five of the seven assignments received a 'No Assurance' opinion rating with the other two receiving Limited Assurance ratings. These ratings were based on:

  - the systemic weaknesses identified by NIAO, Internal Audit and the Department's European Union Verification Unit;

  - the high rate of error identified by the Verification Unit; and

  - the number and value of uncleared irregularities.

- a review of the European Union Verification Unit's performance against its objective of completing the European Union verification exercise referred to above. Internal Audit considered the Unit had performed well and gave a 'Substantial Assurance' opinion rating, that is, while there is basically a sound system there are weaknesses which put some of the objectives at risk.

4.18 The overall assurance rating given by Internal Audit for the Department's Urban Regeneration and Community Development Group in 2002-03 was 'No Assurance'. My staff reviewed the internal audit papers relating to the examination of the European Union Interim Funding arrangements and have concluded that their work was thorough and effective. The various weaknesses in key financial controls and monitoring of expenditure identified by Internal Audit throughout URCDG once again correspond closely to the findings of my audit (paragraphs 4.25 to 4.33). Where appropriate, the issues raised by Internal Audit have been addressed in the Statement on Internal Control provided by the Accounting Officer in relation to the Resource Account.

Review of the Work of Belfast Regeneration Office's Quality Assurance & Improvement Unit and its Review Panel

4.19 During this year's audit my staff again reviewed the work of the BRO Quality Assurance and Improvement Unit (QAIU) which checks samples of payments on a regular basis for compliance with policies and procedures. In NIAO's view the Unit has continued to provide management with sound independent assurance on the quality of decision making and accuracy of payments. I note that the examples of non-compliance highlighted by the Unit correspond closely to the findings of my audit (paragraphs 4.25 to 4.33).

4.20 The Review Panel was established within BRO in October 2002 and its aim is to provide management with independent assurance on the quality of decision making. It comprises representatives from URCDG's Planning and Governance Unit and BRO. The Panel considers all evidence on the project file to support the funding decision, but does not approve projects. Staff from QAIU carry out an initial check to ascertain whether Area Teams have fully and accurately completed a pre-approval checklist, raising any concerns with the Panel. Responsibility for ensuring the effective implementation of recommendations made by the Panel rests with the Area Team Leaders, not the Panel. However, where issues raised are deemed to be significant, the Panel may recall any project for reconsideration.

4.21 Initially the Panel considered all projects above £20,000 which had been recommended for approval (pre approval check) and 20 per cent of projects below £20,000 which were approved during the previous month (post approval check). However, given the high level of comments being raised by the Review Panel, the Director of BRO decided to lower the level for referring cases to the Panel from £20,000 to £15,000 with effect from 11 April 2003. As a consequence of the Panel's further findings, it was determined that all project files should be referred to the Review Panel from 29 July 2003.

4.22 The work of QAIU and the Review Panel is clearly key to improving the effectiveness of BRO checking procedures through the identification and introduction of preventative measures aimed at reducing the level of error. The Review Panel has recently issued a draft Evaluation Report to BRO management covering the period 1 January 2003 to 28 July 2003. I note, with some concern, that after 10 months in operation the Review Panel is continuing to find a high level of non-compliance with procedures. As a consequence, I intend to review the extent to which management has accepted and implemented the Panel's recommendations during my audit of the 2003-04 Resource Account.

4.23 In last year's report (HC 27/NIA 45/02) I noted that through the work and experience of the BRO Quality Assurance and Improvement Unit the Department intended to share best practice procedures and guidelines across all administrative, financial and management activities within its Urban Regeneration and Community Development Group. I indicated my support for this proposal and felt that priority should be given to introducing a quality assurance function within the North West Development Office (NWDO - formerly the Londonderry Development Office). I am concerned at the level and nature of the weaknesses in financial control and monitoring of expenditure highlighted by this year's examination of NWDO projects (see Figures 12 and 13), and consider therefore that the introduction of a quality assurance function must now be actively pursued by the Department. The Department has told me that a Quality Assurance and Improvement Unit has recently been established in NWDO. The Unit will initially concentrate on addressing audit recommendations by providing guidance to staff and reviewing live files to secure audit compliance. I intend to review the operation of the new Unit during my audit of the 2003-04 account.

NIAO Examination of Project Payments

4.24 The final stage of the investigation involved testing the operation and adequacy of key financial controls by examining a sample of projects funded during the year within the risk areas identified in paragraph 4.11. My staff examined a total of 35 projects selected randomly within the different areas under investigation. The detailed findings are set out in paragraphs 4.25 to 4.33 below.

Figure 12: Summary Of Projects Giving Rise To Audit Findings

REF	PROJECT	SPONSORING BRANCH	ACCOUNT AREA (see Figure 11)
A	**The Women's Tec** - grant towards provision of skills training	Belfast Regeneration Office (North Team)	Grants under Urban Regeneration Programme
B	**Wheatfield Primary School Project Group** - grant towards classroom refurbishment and salary costs	Belfast Regeneration Office (North Team)	Grants under Urban Regeneration Programme
C	**Vine Centre Ltd** - capital grant towards new build project	Belfast Regeneration Office (North Team)	Grant under Urban Regeneration Programme
D	**Play Resource Warehouse** - grant toward new build fit our cost	Belfast Regeneration Office (North Team)	Grant under Urban Regeneration Programme
E	**Belfast Learndirect** - grant towards salary and other running costs	Belfast Regeneration Office (Inner West Team)	Grants under Urban Regeneration Programme
F	**Clonard Amateur Boxing Club** grant towards refurbishment, equipment and running costs	Belfast Regeneration Office (Inner West Team)	Grants under Urban Regeneration Programme
G	**Feile an Phobail** - grant towards festival running costs	Belfast Regeneration Office (Inner West Team)	Grants under Urban Regeneration Programme
H	**Belfast Harlequins RFC** - grant towards youth development officer's salary and other running costs	Belfast Regeneration Office (Outer West Team)	Grants under Urban Regeneration Programme
I	**Footprints Womens Centre** -grant towards salary and other running costs	Belfast Regeneration Office (Outer West Team)	Grants under Urban Regeneration Programme
J	**The Hopkins Partnership** - grant towards provision of professional advice in respect of the Dairy Farm Project	Belfast Regeneration Office (Outer West Team)	Grants under Urban Regeneration Programme
K	**Short Strand Partnership** - grant towards provision of play area and environmental improvements	Belfast Regeneration Office (South & East Team)	Grants under Urban Regeneration Programme
L	**NI Volunteer Development Agency** grants towards the administration of the Community Volunteering Scheme	Voluntary & Community Unit	Grants to voluntary bodies
M	**Law Centre NI** - revenue grant towards administration costs	Voluntary & Community Unit	Grants to voluntary bodies
N	**The Nucleus -** GAP funding towards running costs	Central Business Unit (European Union Unit)	Grants under EU Special Support Programme for Peace and Reconciliation
O	**North Belfast Partnership Board** - grant towards running costs	Central Business Unit (European Union Unit)	Grants under the European Regional Development Fund
P	**Tullyvalley and District Development Group** - grant towards furnishing new resource	North West Development Office	Grants under Urban Regeneration Programme Continued

REF	PROJECT	SPONSORING BRANCH	ACCOUNT AREA (see Figure 11)
		furnishing new resource	
Q	**Two Cathedrals Festivals 2000** - grant towards festival running costs	North West Development Office	Grants under Urban Regeneration Programme continued
Q	**Two Cathedrals Festival 2000** - Grant twoards festival running costs	North West Development Office	Grants under Urban Regeneration Programme
R	**Naiscoil Na Rinne** - grant towards purchase and erection of mobile classroom	North West Development Office	Grants under Urban Regeneration Programme
S	**Football in the Community** - grant towards salary costs	North West Development Office	Grants under Urban Regeneration Programme
T	**Castledawson Development Enterprise Ltd** - grant towards extension and refurbishment of building	Regional Development Office	Grants under Urban Regeneration Programme
U	**Armoy Community Association** - grant towards provision of community based economic project	Regional Development Office	Grants under Urban Regeneration Progrqamme

Summary of Main Audit Findings

4.25 Of the 35 projects examined by my staff, I have concerns in respect of 21 projects which are summarised in Figure 12 below which also indicates the relevant Departmental sponsoring branch and the associated area of grant assistance. Projects handled by each of the BRO Area Teams, the Central Business Unit's European Union Unit, the Regional Development Office, the North West Development Office and the Voluntary and Community Unit are involved. The examination of the sample of projects this year highlighted a significant number of good practice issues which are either already operated by the Department or have been identified by my audit. We have brought these to the Department's attention with a view to consideration being given to disseminating the issues across the Urban Regeneration and Community Development Group.

4.26 Figure 13 below summarises the main audit findings and attributes them to individual projects. While in a number of cases one administrative weakness has automatically resulted in another, there are other instances where the weakness is stand-alone, that is, not interdependent. Unfortunately, the findings once again serve to illustrate the numerous and significant weaknesses in the Department's financial control and monitoring of the payments it makes to the various bodies through its Urban Regeneration and Community Development Group. While the Department has been committed to addressing the issues raised as a result of both this and my previous audits a continued concerted effort clearly needs to be taken to strengthen key financial controls in all areas where risk has been identified. This view is supported by the Internal Audit findings on European Union Interim Funding arrangements, BRO's Making Belfast Work project payments and the European Union Closure Statements on the final declaration of expenditure in respect of the various European Union Funds/Programmes administered by the Department (paragraphs 4.14 to 4.17).

Figure 13: Summary of Main Audit Findings

Audit Findings	Projects (Figure 12)																				
	A	**B**	**C**	**D**	**E**	**F**	**G**	**H**	**I**	**J**	**K**	**L**	**M**	**N**	**O**	**P**	**Q**	**R**	**S**	**T**	**U**
Insufficient evidence/investigation to support funding decisions						X	X	X												X	X
Insufficient liaison with other funders to establish level of alternative funding available/staging of payments	X	X						X	X							X	X				
Inadequate letters of offer/non-compliance with terms and conditions of letters of offer	X		X	X					X	X			X		X	X	X	X	X	X	
Failure to issue revised letters of offer as a result of fundamental changes to projects	X								X	X							X			X	
Insufficient evidence to support payments	X								X		X			X	X	X	X				
Inadequate financial control/monitoring of of expenditure	X	X	X	X	X		X	X	X	X	X		X		X	X	X		X		
Irregular payments ie payments made outside governing authorities		X										X					X			X	

4.27 In my report on the 2001-02 DSD Resource Account I noted that the Department was reviewing the administrative and financial systems and procedures operating within BRO. This was being addressed through the establishment of a review group within BRO to oversee and co-ordinate a programme of action to address areas of concern. The Department has told me that while a review group has not yet been established, a Business Improvement Review of BRO is nearing completion. The aim of the Review is to evaluate functions within BRO to ensure that:

- the optimal organisational and management structures are in place to deliver regeneration objectives and strategies, as set out in the Department's Neighbourhood Renewal Strategy 'People and Place';
- BRO is properly resourced to best meet its business needs and services; and
- the grading and loading of posts are consistent with Treasury grading standards.

The steering group will take forward the accepted recommendations in the final report. I intend to monitor the implementation and impact of the recommendations in due course.

4.28 I also understand that an internal review within URCDG of how payment systems and verification procedures should, in future, be structured to ensure greater effectiveness and robustness in control is currently under way. This review follows on from a number of audit exercises, including those by my staff, and also builds on the results of a number of pilot initiatives to enhance control and effectiveness. The Department has informed me that the initial work involved in scoping the Review highlighted that considerably more processes had to be examined than originally planned. Both audit findings and preliminary work undertaken in the Review indicated that additional staff resources were needed to deal with grant administration, appraisal and control functions within URCDG's main business areas. Ten new posts have been agreed for this area of work, all of which will be filled by December 2003. A further recommendation, which is under consideration, is the formation of a Central Team to deal with monitoring and verification functions throughout the Group, to provide a standard approach across main business areas. The establishment of such a team will require reorganisation of existing structures and some additional staff resources. Again, I propose to monitor progress in this area.

4.29 As I reported last year the Department is also engaged in setting up a computerised database of funding to the voluntary and community sector in Northern Ireland. This development, together with the Department's contribution to the development of IT systems to support the management and delivery of the new round of European structural funds programmes, should help to address some of the problems identified, including minimising the risk of duplicate funding. Development of the database is progressing well and an evaluation of a pilot application commenced in the Department and the Department of Health, Social Services and Public Safety in August 2003. Following evaluation of the pilot, it is planned to roll out the application to other government departments by March 2004.

4.30 Other measures which have and are being undertaken by the Department include:

- the establishment of business support units in four of the URCDG Directorates to provide quality assurance by way of reviewing project files, issuing best practice guidance and undertaking monitoring and verification of funded projects;

- the establishment of a 'Good Practice in Governance and Finance Group' led by the Voluntary Community Unit (VCU), which is working with representatives from the voluntary and community sector to produce a guidance manual for use by the sector;
- working with Internal Audit to consider the development of an indicator to enable the Group to measure 'audit' performance internally;
- the introduction of monitoring in NWDO by way of project visits;
- the provision of training on a new BRO Contract for Funding (CFF) (formerly Letter of Offer). The CFF is currently with Heads of Branches for final approval;
- an exercise currently underway to revise and simplify both the grant application form and the application process; and
- a centralised system of payments, verification and monitoring has been established in VCU ensuring clear separation of duties. In addition, a procedures manual providing clear guidance to all staff has been compiled which draws on best practice both internally in URCDG and externally from other key funders.

4.31 Further measures, which have been undertaken to enhance corporate governance across the Group, are:

- the establishment of a Group Management Board;
- the establishment of an independent URCDG Audit Committee (the previous Audit Committee was combined with the Resources, Housing and Social Security Group);
- the establishment of a dedicated Planning and Governance Unit tasked with carrying out business planning and corporate governance;
- the development of a risk management system which incorporates risk registers, updated on a quarterly basis;
- the reconstitution of the BRO Review Panel to review all project applications;
- the revision of forward job plans, linked to performance, to emphasise the need for audit compliance;
- the production of monthly reports to the Deputy Secretary as a consequence of deficiencies identified in projects assessed by the Review Panel;

- quarterly Review Panel reports to the Deputy Secretary detailing its findings. Issues raised are communicated across the Group by way of best practice;
- agreement from the Departmental Management Board with regard to filling URCDG vacancies as a matter of priority; and
- the improvement of project monitoring arrangements across URCDG.

4.32 As part, and in advance, of the restructuring of the Regional Development Office a number of measures have been worked up to address governance and audit requirements, namely:

- roles and responsibilities of the various branches of the restructured Division have been agreed, documented and worked into staff job descriptions;
- an outline of the project handling process which clearly sets out the roles and responsibilities of the various branches and managers in the Division at each stage of the process has been agreed;
- the production of detailed procedures manuals for the Neighbourhood Renewal and Town Centre Reinvigoration Strategies as part of the restructuring exercise; and
- the establishment of a Quality Assurance and Improvement section which will be responsible for: ensuring that adequate procedures have been developed; ensuring that procedures manuals are maintained; ensuring that procedures have been adhered to on project files presented for approval; and ensuring that project payments are valid and regular.

I intend to monitor the progress and impact of the initiatives set out in these two paragraphs in due course.

4.33 Examples of specific weaknesses in financial control and monitoring of expenditure highlighted by my audit are set out below (Figures 12 and 13):

Insufficient Evidence/Investigation to Support Funding Decisions

- at application approval stage, the Department failed to establish the extent to which groups had attempted to secure appropriate funding from other sources before committing Departmental funds;
- the Department failed to ensure that groups provided sufficient supporting evidence with applications of other funding obtained, such as copies of applications, letters of offer, etc;

- the Department failed to ensure that up to date quotations for work were obtained by a group prior to the commencement of the project; and
- the Department failed to adequately confirm that an initial instalment of grant had been appropriately disbursed by a group in line with the letter of offer before paying the second instalment.

Insufficient Liaison with other Funders to Establish Level of Alternative Funding Available/Staging of Payments

- where groups had secured other funding, the Department failed to seek independent confirmation from those funders as to the level of alternative funding actually available to projects before committing Departmental funds;
- the Department did not always agree the staging of grant payments with other funders or ensure that the alternative funds offered by them had actually been received by groups in line with the relevant letters of offer before committing its own funds; and
- the Department did not always seek to establish the extent to which groups could fund projects from their own resources.

Inadequate Letters of Offer/Non-compliance with Terms and Conditions of Letters of Offer

- eligible costs on which grant was paid were not sufficiently itemised by the Department in letters of offer to facilitate subsequent accurate checking against claims for payment;
- letters of offer were often not specifically explicit regarding the timing of receipt of project evaluation reports;
- the conditions of a letter of offer relating to the drawdown of grant was not complied with by one group;
- the Department failed to issue a letter of offer in one instance clearly resulting in no formal contract between the Department and the group;
- incorrect grant conditions were included in one letter of offer; and
- inability of the Department to enforce certain pre-conditions of letters of offer.

Failure to Issue Revised Letters of Offer as a Result of Fundamental Changes to Projects

- a letter of offer was not revised to take account of a higher than anticipated project deficit incurred by a group;
- letters of offer were not revised where the Department was aware that grant conditions could not or would not be met by groups;
- letters of offer were not revised by the Department to take account of subsequent changes to the grant payment schedule; and
- the Department failed to revise letters of offer where original grant conditions were later found to be incorrect or no longer applicable.

Insufficient Evidence to Support Payments

- P11 forms (Inland Revenue form showing salary payments and income tax deducted) not submitted by bodies to support salary grants prior to payment by the Department;
- the Department did not always ensure that full supporting documentation such as bank statements and paid cheques was supplied by groups with grant claims to enable it to adequately vouch expenditure incurred;
- on occasions the Department failed to ensure that sufficient evidence was received from groups to evidence there was no overlap of funding with other funders;
- on a few occasions grant was paid by the Department on the basis of 'unpaid' invoices received from groups, that is, prior to expenditure actually having been incurred by groups; and
- instances were noted where the Department had paid the final amount of agreed grant prior to the completion of projects.

Inadequate Financial Control/Monitoring

- failure by the Department to ensure that proper tendering procedures were followed by groups, including obtaining quotations as appropriate;
- overpayment of grant by the Department due to clerical error, for example, where staff had failed to identify ineligible expenditure claimed by one group and incorrectly calculated grant due in another instance;

- failure of Department to ensure actual receipts supporting grant claims accurately matched the letter of offer analysis of expenditure;
- failure by the Department to ensure groups had physically received goods before paying grant;
- failure by the Department to ensure project progress and final evaluation reports outlining the outputs achieved against targets were received in accordance with letters of offer before paying final grant instalments; and
- instances were noted where the Department had failed to rigorously check that grant had been applied by groups as intended by letters of offer. For example, in one case grant was paid towards salary costs in respect of a post which has not yet been filled.

Irregular Payments, that is, Payments Made Outside Governing Authorities

- payment of grant by the Department in advance of a commitment having been entered into by a grant recipient;
- payment of grant to an Intermediary Funding Body (IFB) in advance of a full commitment having been entered into by the IFB with individual groups. This included monies paid by the Department in previous financial years which were retained by the IFB and not refunded to the Department;
- retrospective application and approval to funding after the end of a project and the resultant retrospective payment of grant by the Department to the group; and
- payment of grant by the Department in advance of pre-conditions of the letter of offer having been met by the group.

Holywell Trust

4.34 I first noted my concerns regarding the European Regional Development Fund (ERDF) grant paid to Holywell Trust by the Department's Voluntary Activity Unit (now the Voluntary and Community Unit) in my report on the 2000-01 Department for Social Development Vote C Appropriation Account (NIA 34/01). In particular, I was concerned at the adequacy of financial controls and monitoring of expenditure operated by both the Unit and Holywell Trust.

4.35 Following further investigations by my staff during 2001-02, I noted in my report on the Department's 2001-02 Resource Account (HC 27/NIA 45/02) that the Department was to carry out an investigation in relation to the Community Organising and Capacity Building Programme (COCBP) run by the Trust, with emphasis on determining the full extent of any financial irregularity through an examination of all transactions carried out during the Programme. This investigation has now been completed and a report issued to Departmental management.

4.36 The main conclusion of the investigation is that the criteria for payment of grant under the ERDF Measure of the Community Infrastructure Physical and Social Environment Sub-Programme were not met, therefore the Holywell Trust application to fund the COCBP should have failed. In addition, the investigation found that the letter of offer under which grant was awarded was breached to the extent that relevant changes of circumstances were not reported when they came to light. This included the failure by Holywell Trust to notify the Department of unspent grant monies totalling £1,629 which have since been recovered. It is of concern that the failure of a number of procedures and controls has contributed to incorrect payments arising from ineligible and incorrect charges made against COCBP totalling some £60,000. However, none of the incorrect payments identified were considered by the investigators to have contained any element of misappropriation arising from false accounting and/or deception.

4.37 Clearly, the Department's investigation has highlighted a number of key control lessons which should be applied to applications of this nature. I intend to assess the Department's detailed response to the investigation's conclusions and recommendations, together with the extent to which controls weaknesses have been strengthened, as part of my audit of the 2003-04 account. In the meantime, the Department has told me that in terms of the recovery of incorrect payments it intends to identify the amount of overpayment and to pursue recovery as recommended in the report.

Conclusion

4.38 On the basis of my specific findings in paragraphs 4.25 to 4.33 I have to conclude that the Department's financial controls and monitoring of expenditure remain inadequate. Clearly my audit has confirmed that there are continuing fundamental weaknesses in financial control and monitoring of expenditure. As I have previously mentioned, the Department has informed me that it is committed to addressing these. Nevertheless, in a wide range of the funding activities for which the Department's Urban Regeneration and Community Development Group is responsible, the relevant information does not exist to enable me to establish that expenditure was applied to the purposes intended and was regular. I have decided to qualify my audit opinion accordingly.

Part 5: Qualified Audit Opinion Arising from Uncertainties over Certain Debtor and Creditor Balances

Background

5.1 There are weaknesses in the Department's audit trails, mainly arising from deficiencies in the interaction between the Department's Programme Accounting Computer System (PACS) and its various benefit systems. These deficiencies result in limitations in the evidence available to support significant social security programme debtor and creditor balances. I therefore cannot be sure as to the accuracy and completeness of these balances. The relevant PACS accounting system, which the Department utilises, is operated and managed by the Department for Work and Pensions (DWP) in Great Britain. Similar limitations therefore impact on the DWP Resource Account balance sheet.

5.2 I have assessed whether the impact of the uncertainty over these balances results in the balance sheet giving a misleading view and have concluded the impact is that the net assets of the Department may be significantly misstated. Consequently, I have decided to qualify my audit opinion on the account on the basis that the scope of my audit was limited.

Contributory and Non Contributory Benefit Overpayment Debtors - £40,474,000 (Gross)

5.3 Overpayments to customers arise as a result of errors by officials and through fraud or error on the part of the customer. During 2002-03, the Department recovered £5.5 million of debt against a target of £4.5 million.

5.4 When an overpayment is identified, local social security offices notify Debt Management Unit (DMU). DMU records the amount of the overpayment on their debt management system, the Overpayment Recovery System (OPREC) and pursue recovery. However, these and subsequent movements in debts outstanding are posted to the PACS general ledger in total rather than by the individual debt amounts. As a result, no listing of individual customers owing money was available to my staff to test from the PACS general ledger system in relation to 2002-03.

5.5 I noted in my report last year (HC27/NIA 45/02) that the OPREC system was not able to generate a list of individual customers. For 2002-03 the Department has been able to produce such a list. However at 31 March 2003, the debtor balance recorded in the PACS general ledger did not agree with the balance from the OPREC collated database. The Department considered the PACS general ledger balance to be the more accurate and, being lower, the more prudent balance. I also note that the cumulative difference between the PACS general ledger debtor balance and the OPREC balance has increased from £1.3 million in 2001-02 to £2.4m in 2002-03. The Department has advised me that this increase is due to system limitations. The Department is currently preparing an Action Plan to address the underlying problems they have identified based on the investigative work they have conducted to date. I intend to keep this matter under review.

5.6 In the absence of a satisfactory audit trail between the PACS general ledger and the more detailed information held on the OPREC system, my examination of overpayment debtors was again severely limited. Therefore, having taken account of evidence that the information held on the OPREC system is unreliable and incomplete, I conclude that there is significant uncertainty over the accuracy and completeness of the debtors balance held on the PACS general ledger. I understand, however, that the Department has devoted considerable work and effort to reducing the level of non -system error through enhanced communication with staff and detailed reconciliations of information held on the PACS general ledger. I intend to review any further progress during my audit of the 2003-04 Resource Account.

Encashment Control Creditor (£27,599,000)

5.7 This balance represents the Department's estimate of the total value of order book foils, payable orders and girocheques which had been issued to customers but remained unencashed at the year-end.

5.8 The Department is unable to confirm the actual encashment of individual order book foils and the majority of girocheques as encashment data from the Department's paying agents does not provide this level of detail. The Department's accounting systems, although able to provide total order book and girocheque issues, are unable to capture detailed accounting information for individual order book foils and girocheques produced manually and issued to customers. I note that for payable order expenditure (£740,000) the Department has been able to provide detailed accounting information this year. For girocheques the Department is able to support a figure for unencashed girocheques using statements from Girobank plc. Overall, the Department is unable to provide detailed evidence from its PACS accounting systems to support the encashment control creditor balance at 31 March 2003, except for the payable order element of £740,000.

5.9 To provide a reasonableness check, the Department has estimated the likely unencashed amount at 31 March 2003 based on statements provided by Post Office Limited, previously known as Post Office Counters Limited. Previously a predictive model was used. In view of the complexities surrounding customer encashment patterns, the Department decided not to use the predictive model, as it would not have provided sufficient certainty that the encashment control creditor balance for order books was accurately stated.

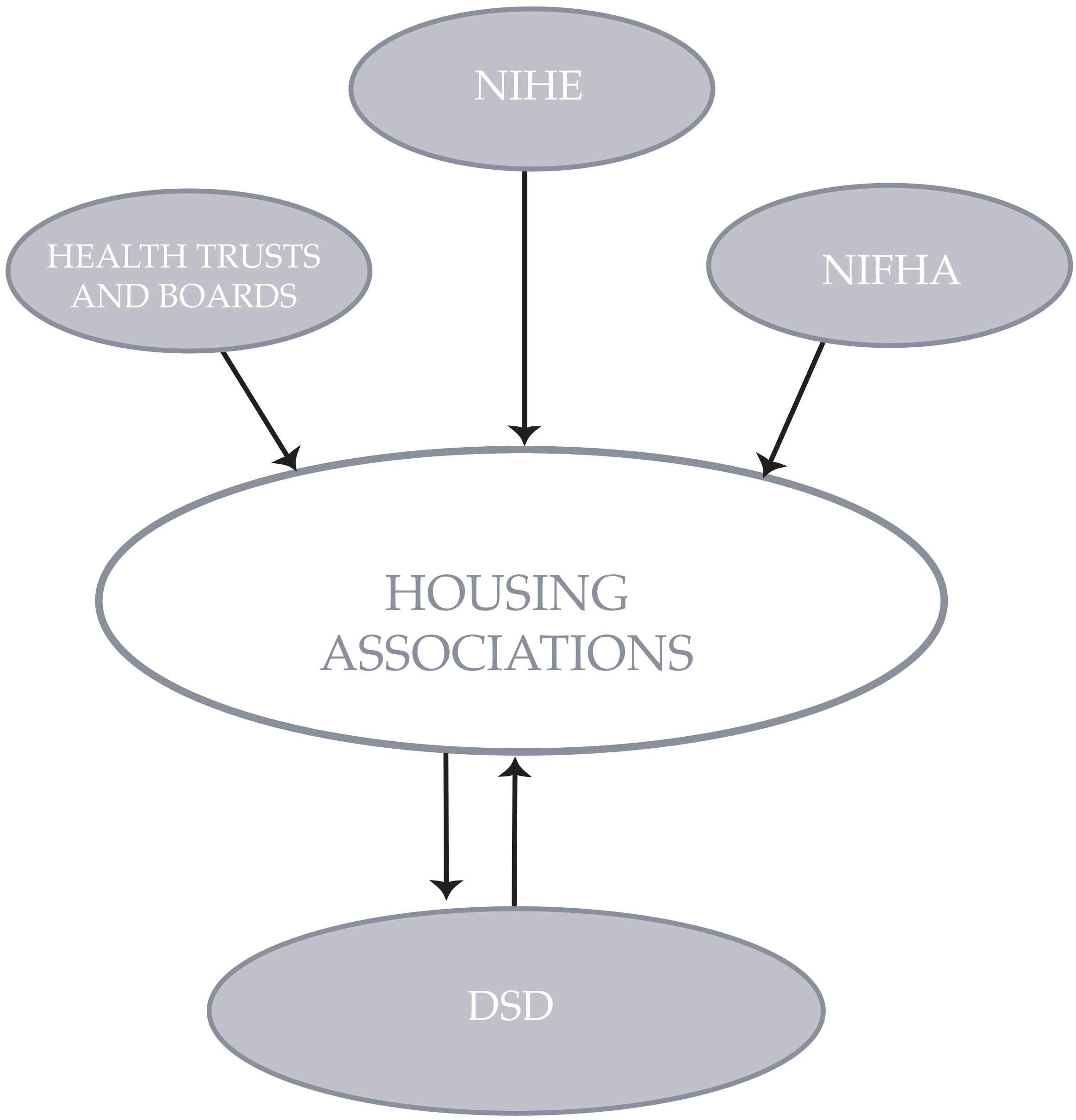
5.10 I therefore conclude that there is significant uncertainty over the encashment control balance. The Department expects that the introduction by 2005 of Direct Payment of benefits will reduce this creditor balance substantially.

Appendix 1

Housing Associations - Glossary and Abbreviations

HAG	Housing Association Grant - payment of grant under Article 33 of the Housing (NI) Order 1992
SNMA	Special Needs Management Allowance - payment of an allowance to meet the additional housing management cost incurred in Special Needs Housing
General Needs Housing	housing to meet the requirements of those not requiring special needs accommodation
Special Needs Housing	housing to meet the needs of particular user groups with special needs, that is, frail elderly, learning difficulties, etc
Competitive Tendering	tendering for services and contracts through open competition in accordance with Departmental guidelines
Package Deal	negotiated tendering with a Design and Build contractor who normally owns a site which he sells to the association on the basis that he gets the building contract
Transfer Schemes	NIHE own the land, design the scheme and transfer it to an association for development
Competition Schemes	NIHE own the land, has designed the scheme and asked associations to bid for it on the basis that the lowest amount of HAG wins
Existing Satisfactory Schemes	associations buy existing properties from the open market
Rehabilitation Schemes	associations buy existing buildings which require major repair and improvement
Purchase and Repair Schemes	associations buy existing properties that require a degree of repair or improvement not exceeding £10k
Tranche Payment	the amount of Housing Association Grant made to the Housing Association at the major stages of development
Tariff Funding	funding based on 100 per cent of Total Cost Indicator (TCI) x the Grant Rate. There is no provision for additional grant in schemes over TCI or where outturn costs increase
Non-Tariff Funding	grant is based on actual TCI costs x the Grant Rate. Schemes will not be approved at more than 130 per cent of TCI. Also, costs are reviewed at project completion and grant eligibility recalculated, that is, eligible outturn cost x the original Grant Rate. Grant will not be paid on an outturn cost greater than 110 per cent of that approved at project approval or 130 per cent of TCI whichever is the lower.

Appendix 2


NIHE
HEALTH TRUSTS AND BOARDS
NIFHA
HOUSING ASSOCIATIONS
DSD

Roles and Responsibilities

Department for Social Development

The Department's main functions in relation to registered Housing Associations are:

- to establish and maintain a register of Housing Associations;
- to promote, assist and facilitate the development and proper performance of registered Housing Associations;
- to exercise supervision and control;
- to make grants or loans; to publish guidance as to the management of accommodation by registered Housing Associations; and
- to ensure that registered Housing Associations work within the legislation prescribed under Article 14 of the Housing (Northern Ireland) Order 1992.

Registered Housing Associations

Their primary role is providing, constructing, improving or managing, or facilitating or encouraging the construction or improvement of housing accommodation. In addition they may:

- provide land, amenities or services;
- provide, construct, repair or improve buildings for the benefit of the associations residents;
- acquire, or repair and improve, or create the conversion of houses or other property, houses to be disposed of on sale or lease by equity sharing lease;
- construct houses to be disposed of by equity-sharing lease;
- manage houses which are held on leases or other lettings or block of flats;
- provide services of any description for owners or occupier of houses in arranging or carrying out works of maintenance, repair or improvement, or encouraging or facilitating the carrying out of such works; and
- encourage and give advice on the formation of other Housing Associations or provide services for, and give advice on the running of, such associations and other voluntary organisations concerned with housing, or matters concerned with housing.

Northern Ireland Housing Executive

The Housing Executive is responsible for the formulation of a needs based, prioritised, province wide social housing programme. This is a three year 'rolling' programme which is formulated in draft form, and forwarded to the Department for Social Development for approval, on an annual basis. The social housing programme contains a mixture of schemes to meet the requirements of applicants with General Housing Needs, and those with Special Needs. In addition to this and in relation to housing associations they also:

- provide needs clearance in regard to the development and acquisition of social housing in Northern Ireland;
- distribute land to registered housing associations held within their land bank under their 'transfer schemes';
- offer the services of their professional design team to housing associations; and
- hold and maintain a common waiting list with housing associations of prospective tenants in need of social housing.

Health Trusts and Boards

The function of Health Trusts and Boards in regard to the provision of social housing is in regard to the identification of tenants with a need for a more supportive and intensive style of housing management. The following are examples but the list is not exhaustive:

- people with physical and mental disabilities;
- people with drug and alcohol related problems; people leaving prison;
- vulnerable people including women at risk and young people; and
- frail elderly people.

In addition they will jointly manage a scheme with an Association and identify and recommend the need for adaptations to existing dwelling for the physically disabled.

Northern Ireland Federation of Housing Associations (NIFHA)

The main functions of NIFHA are to:

- represent Housing Associations to all those in a position to influence their future and in particular relevant statutory bodies and Government Agencies;
- provide general research and information;
- provide training and advice to Associations and staff through conferences, seminars, workshops and publications;

- manage the Northern Ireland Continuous Recording (NICORE) system; and
- provide a policy development facility for the Federation.

Its aim is to increase the awareness of Associations as to their rights and responsibilities in relation to communities' housing related needs. In addition, it represents Associations through a Liaison Group with the Housing Executive and is also involved in developing the Housing Market Review and a strategic approach to the planning and provision of special needs housing.

Appendix 3

Certifications Provided by Housing Associations

Acquisition Stage

The Association Certifies that:

- any conditions of the Project Approval applying to the acquisition have been met;
- the purchase price does not exceed the value of the property as assessed by an independent qualified valuer, whose valuation must be no more than twelve months old at the date of execution of the contract; and
- the property to be acquired offers good title.

Property already in the Association's ownership complies with the above

- any necessary consents have been obtained prior to execution of the contract;
- it has executed the purchase contract;
- it will inform the Department immediately of any change in the modified date for completion of the purchase; and
- if the completion does not occur within two weeks of receipt of Grant, the Grant will be returned to the Department with interest.

Off the Shelf Schemes

The Association Certifies That in Addition:

- Building Regulations approval and detailed Planning Permission have been obtained (where appropriate);
- any necessary topping up funding has been obtained and is guaranteed for a minimum of twelve months, with commitment in principle for ongoing support;
- it has completed the Joint Management Agreement, where the project is to be managed in partnership with another body; and

- it will, within three weeks of receipt of Grant, forward to the Department a certification from its solicitor confirming that completion of the purchase has taken place, the date of completion and the consideration.

Start on Site

The Association Certifies that:

- the scheme complies with the Department's Design and Contracting Requirements;
- no change has occurred in the units to be produced which affects the calculation of TCI;
- Detailed Planning Permission for the scheme has been obtained (where appropriate);
- Building Regulations approval for the scheme will be obtained prior to Practical Completion;
- it will meet the cost of any shortfall on capital or revenue funding including the cost of any non-qualifying items;
- any necessary topping-up funding has been obtained and is guaranteed for a minimum of twelve months with commitment in principle for ongoing support;
- it has completed the Joint Management Agreement, where the project is to be managed in partnership with another body;
- no non-qualifying items are included in the costs for Grant funding; and
- it has entered into the Building Contract and the possession of the site has passed to the contractor.

Works Only Projects

The Association Certifies that:

- the property to be developed is in the Association's ownership and offers good title;
- no covenants or other restrictions exist which impede development of the site/property; and
- any necessary consents have been obtained prior to start on site.

Tariff Funded Scheme at Practical Completion

The Association certifies that:

- the dwellings produced comply with the Department's Design and Contracting Requirements;
- no change has occurred in the units produced which affects the calculation of TCI; and
- Building Regulations approval has been obtained (where appropriate).

All Claims

The Association certifies that:

- any material divergence from the (revised) development timetable included on this claim will be reported immediately to the Department;
- to the best of its knowledge and belief the contents of this application are complete and accurate;
- no member, employee, agent or consultant of the Association has any interest in the proposed vendor, contractor or the land or property to be acquired. This declaration extends to any firm, partnership or organisation in which they or their families are involved as partner, director or shareholder. (If such a declaration cannot be made without reservation, a statement must be attached giving a full disclosure of the interests of the people concerned); and
- all previous certifications made by the Association at project approval and/or previous grant claim stages in relation to this scheme shall continue to apply.

I certify that the conditions listed above have been complied with.

Signed

Certifications provided by Housing Associations

Project Application

1. the Association has the vendor's agreement of terms;
2. the purchase price does not exceed the value of the property as assessed by an independent qualified valuer;
3. the Association has undertaken a long term assessment of the ability of the Association's rental income to cover operational costs including repayment of loan principal and interest;
4. the Association has or will obtain long term private finance (mixed funded schemes only);
5. the Association will, where giving security to a lender in the form of a charge over land, comply with the Departments requirements in respect of Article 13 of the Housing (Northern Ireland) Order 1992;
6. the Association has an offer of development capital/has resolved to use its own reserves* (mixed funded schemes only);
7. the Association will meet the cost of any shortfall on capital or revenue funding, including the cost of any non-qualifying items;
8. no capital contributions (including other public subsidy) exist/details of capital contributions are supplied*;
9. where the scheme is to be managed in partnership with another body, the Joint Management arrangements conform to the Department's requirements;
10. any necessary topping up funding can be obtained;
11. the scheme will comply with the Department's Design and Contracting Requirements;
12. works cost forecasts are based on technical consultants' estimates and no non-qualifying items are included in the costs for Grant funding;
13. the Association will insure and keep insured the accommodation provided for its full replacement value, both during and after the development;
14. the Association will notify the Department immediately if, at any stage during the development of the scheme, forecast costs exceed the Drawing Limit for loans to be specified by the Department at Project Approval (public funded schemes only);
15. the scheme meets the Special Needs eligibility criteria and form TS1 is enclosed (Schemes requiring SNMA only);
16. any material divergence from the development timetable will be reported to the Department forthwith;

17. no member, employee, agent or consultant of the Association has any interest in the proposed vendor, contractor, or the land or property to be acquired. This declaration extends to any firm, partnership or organisation in which they or their families are involved as partner, director or shareholder. (If such a declaration cannot be made without reservation, a statement should be attached giving a full disclosure of the interests of the people concerned);
18. the Association has carried out an economic appraisal of the proposed development where this is required as part of the Department's procedures;
19. the Association has outline or full Planning Permission; and
20. to the best of our knowledge and belief, the contents of this application are complete and accurate.

***Delete the inapplicable**

Certifications 1 and 2 should be deleted in the case of works only projects where the land or property is already in the Associations ownership

Please delete any of the above certifications which cannot be made by the Association, and give the reason(s) in a covering letter

Signed:

Part 2

Executive Agency and Non Departmental Public Body Accounts

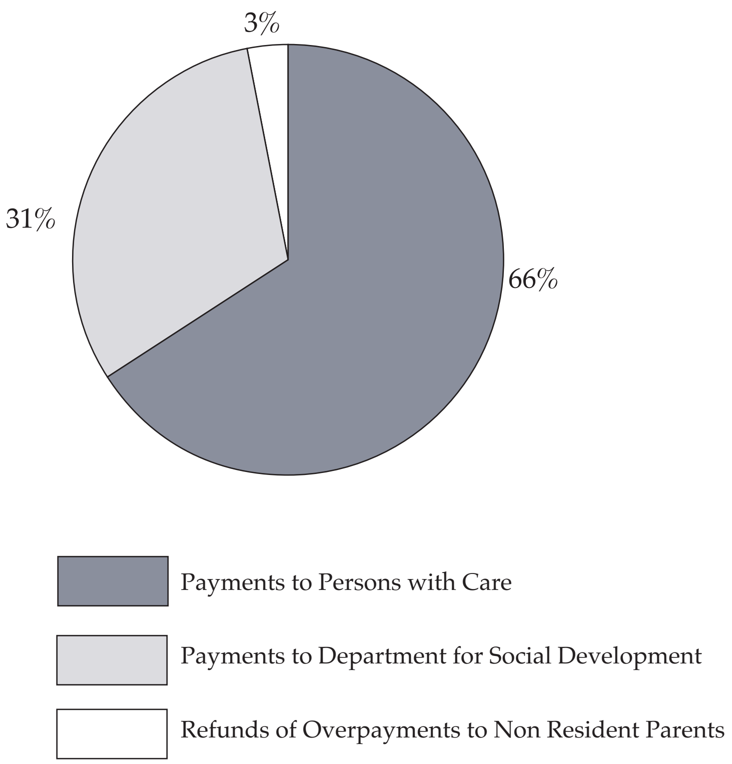
NORTHERN IRELAND CHILD SUPPORT AGENCY CLIENT FUNDS ACCOUNT 2002-03

Introduction and Executive Summary

1. The Northern Ireland Child Support Agency was established as an Executive Agency of the former Department of Health and Social Services (now the Department for Social Development) in April 1993 to operate the system of child maintenance introduced by the Child Support (Northern Ireland) Order 1991. The main purpose of the Agency is to ensure that non-resident parents formally meet assessed maintenance responsibilities towards their children.

2. The Agency's Client Funds Account shows that £12.5 million was received from non-resident parents during 2002-03 and £12.6 million, which includes a residual amount from the previous year, was paid out by the Agency. As figure 1 shows, of the £12.6 million subsequently paid out in respect of child maintenance during the year, £8.3 million (66 per cent) was paid over to persons with care of children and £3.9 million (31 per cent) was paid to the Department for Social Development, where persons with care are in receipt of income support. The balance of £0.4 million (3 per cent) comprised refunds of overpayments to non-resident parents. At 31 March 2003, the total value of maintenance balances outstanding, excluding amounts which the Agency regards as probably uncollectable, was £10.4 million.

Figure 1: Maintenance Payments 2002/03



3. I am required under section 11(3) of the Government Resources and Accounts Act (Northern Ireland) 2001 to examine and certify the Northern Ireland Child Support Agency Client Funds Account. This report brings to Parliament's attention significant matters arising from my examination of the Account for 2002-03.

4. My report is structured to:

- provide background information on the Northern Ireland Child Support Agency and its activities, outline the method of calculating a maintenance assessment, detail the accounting arrangements of the Client Funds Account and discuss the Agency's progress under the Corporate Governance Framework (paragraphs 1.1 to 1.18);
- set out the results of my examination of the 2002-03 Client Funds Account, including a review of the levels of compensation paid out by the Agency, explain why I have qualified my opinion, and provide a comparison with previous years' results (paragraphs 2.1 to 2.23);
- consider progress that the Agency has made in achieving its key performance targets, in particular the cash value accuracy of maintenance assessments (paragraphs 3.1 to 3.11); and
- review the position following the implementation of the Child Support Reforms (paragraphs 4.1 to 4.10).

Main Findings and Conclusions

Basis for Qualified Audit Opinion

5. I have qualified my audit opinion on the Agency's Client Funds Account for 2002-03 because, following my examination of a representative sample of cases, 10 per cent of receipts from non-resident parents, 43 per cent of full maintenance debt balances and 33 per cent of interim maintenance debt balances were for the wrong amount. This is mainly as a result of errors in the underlying maintenance assessments and incorrect adjustments to customers' accounts. In total, my staff examined 30 receipts/full maintenance case units involving some 96 assessments (2001-02: 182 assessments) and 30 interim maintenance case units involving 35 assessments (2001-02: 33 assessments). An analysis of the percentage of incorrect receipts and debt balances since 1997-98 is provided in figure 2 below. These figures clearly highlight the history of significant errors in receipts and debt balances (paragraph 8).

Figure 2 : Analysis of Incorrect Receipts and Debt Balances Found from Audit Testing

	Percentage Incorrect					
	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03
Receipts from non-resident parents	19	20	49	47	30	10
Full maintenance balances	22	56	80	63	70	43
Interim maintenance balances	11	25	23	33	17	33

6. Based on the 2002-03 results, I estimate that overpayments by non-resident parents amounted to £61,500 while there were no underpayments. I also estimate that at 31 March 2003 debts relating to full maintenance assessments contained overstatements of £414,000 and understatements of £118,000, and debts relating to interim maintenance assessments contained overstatements of £67,500 and understatements of £3,400.

7. I have examined representative samples of receipts from non-resident parents and maintenance debt balances. The results of these examinations allow me to confirm the existence of material error within the account but are subject to margins of statistical uncertainty. While, therefore, it is not usually possible to reach firm conclusions about variations between years, the second part of this report summarises trends in errors made by the Agency since 1997-98.

8. My previous reports on this account have highlighted that the Agency's poor performance around the accuracy of maintenance assessments has left a legacy of error. The results of both my 2002-03 audit and of the Agency's Case Monitoring Team's examination (paragraph 10) indicate that although high error rates continue (see also figure 2), some improvement has been noted.

Compensation Payments

9. As a consequence of the errors and delays in the provision of its service, the Agency has had to make compensation payments to either non-resident parents or persons with care. Since 1995-96 the Agency has paid out compensation totalling £1.1 million in 2,183 cases, at an average cost of £507 (figure 10). In my view, the number and value of compensation payments which have been paid out of Exchequer Funds due to errors and delays by the Agency is still very high.

Progress Against Key Targets

10. The Agency achieved all its key Ministerial targets during the year including the cash value accuracy of maintenance assessments. Based on the Agency's Case Monitoring Team's examination, the Independent Standards Committee's Annual Report notes that the cash value accuracy of the last decisions on assessments checked during the year improved from 82 per cent in 2001-02 to 86 per cent in 2002-03, against the Ministerial target of 80 per cent. While these figures are encouraging, the results of my testing in 2002-03, set out in

Part 2 of this report, indicate a high level of error in new assessments made during the year. On this basis there is little room for complacency in reducing further the level of inaccurate decisions which lead to the wrong amount of maintenance being calculated. I intend to continue closely monitoring accuracy levels as part of my audit of the 2003-04 account.

Child Support Reforms

11. Under the Child Support Reform programme the implementation of simplified rules relating to maintenance assessment, the modernization of operational processes and the introduction of a new computer system is expected to promote more accurate and timely maintenance assessments with improved payment compliance.

12. The reforms were introduced on 3 March 2003 for new claims only, following a deferral of the original implementation date of April 2002. This follows a programme of pilot testing of the new systems in a live environment. As a consequence of the delayed implementation only one claim had been processed by 31 March 2003. I will therefore be considering the impact of the reforms on the accuracy of maintenance assessments as part of my audit of the 2003-04 account.

Part 1 : Background to the Agency and the Client Funds Account

Introduction

1.1 The Northern Ireland Child Support Agency's principal activities are summarised at figure 3.

Figure 3 : The Northern Ireland Child Support Agency's Principal Activities

Establishing Child Support By:

- contacting non-resident parents;
- arranging the resolution of paternity disputes; and
- calculating child maintenance.

Establishing Regular Payment Patterns:

- notifying non-resident parents and parents with care of the amount of maintenance to be paid and arranging a suitable payment method, monitoring payments to ensure that a pattern of regular payment is established;

- collecting and relaying payments at the request of either party;
- pursuing missing or late payments promptly; and
- taking action to recover arrears and re-establishing payment using the full range of the Agency's enforcement powers.

Maintaining Child Support By:

- keeping assessments up to date when a change is reported;
- preparing and presenting appeals to be heard by the Appeals Service; and
- liaising with other Government Departments, Agencies and public bodies.

The Maintenance Assessment

1.2 The method of calculating a maintenance assessment described in paragraphs 1.3 to 1.7 is based on the old child support scheme prior to the introduction of the new scheme under the Child Support Reforms. The new scheme was introduced with effect from 3 March 2003 for all new cases.

1.3 Legislation prescribes how applications for child support maintenance should be assessed. Using formulae contained in the regulations Agency staff calculate a basic maintenance requirement in each case together with the assessment of a non-resident parent's ability to pay. This allows determination of the maintenance due.

1.4 To calculate a maintenance assessment, Agency staff have to obtain information about the personal circumstances of both the non-resident parent and the person with whom the child mainly resides (the 'person with care'). This process is very complex and involves gathering many separate pieces of information about income, housing costs and other expenses from people who may be reluctant to provide this information. Consequently, there is a significant risk of error inherent in the assessment process.

1.5 There are two types of maintenance assessments:

- full maintenance assessments where both the person with care and the non-resident parent provides the Agency with all the information requested. The average weekly value of a full maintenance assessment in 2002-03 was £13.59.
- interim maintenance assessments where the Agency is unable to obtain sufficient information about parents' personal circumstances to make a full maintenance assessment. The average weekly value of an interim maintenance assessment in 2002-03 was £94.94.

The majority of interim maintenance assessments are set at punitive rates to encourage compliance and take no account of non-resident parents' ability to pay. Experience to date has shown that most of the amounts outstanding under this type of assessment are unlikely to be collectable.

1.6 The application of maintenance assessment formulae may produce an inequitable outcome in certain cases. The Child Support (Northern Ireland) Order 1995 provided the Agency with the powers to depart from the formulae assessment in prescribed circumstances, for example, where non-resident parents incur high costs in maintaining contact with their children.

1.7 The complexity of the formulae means that the majority of the Agency's resources are spent on assessing child maintenance rather than maintaining compliance. The maintenance of compliance involves:

- collecting and passing on payment;
- chasing up missing or late payments;
- taking action to recover arrears and re-establishing payment; and
- updating assessments when changes in circumstances are reported.

1.8 From 3 March 2003 the methodology employed by the Agency to calculate maintenance assessments was substantially altered for new claims. The new methodology is significantly less complicated than the previous scheme and the Agency believes that this will result in an improved accuracy rate for maintenance assessments and provide other associated benefits. I intend to monitor the full impact of the new scheme on levels of error in maintenance assessments.

The Northern Ireland Child Support Agency's Client Funds Account

1.9 Since 1995-96, the Northern Ireland Child Support Agency has prepared separate Administration and Client Funds Accounts which I audit. The Administration Account is an Income and Expenditure Account which shows, on an accruals basis, income received for the provision of assessment and collection services and the net cost of operations. The net cost of operations, which amounted to £13.5 million in 2002-03, represents the value of work undertaken by the Agency on behalf of the Department for Social Development. The Client Funds Account on the other hand, is prepared on a cash basis and primarily shows the amounts received by the Agency from non-resident parents. It also shows the maintenance subsequently paid over to persons with care and the sums paid to the Department for Social Development, where persons with care are in receipt of income support.

1.10 The Agency maintains accounting records on its Child Support Computer System and also now on the Child Support 2 (CS2) system for individual non-resident parents which show:

- the maintenance due;
- the amounts paid; and
- any accounting adjustments.

The maintenance outstanding at 31 March 2003 disclosed at notes 6.1 and 7.1 to the Client Funds Account is derived from the balances on these individual accounts.

1.11 The Client Funds Account shows that during 2002-03 the Agency received £12.5 million (2001-02 £11.7 million) from non-resident parents and £12.6 (2001-02: £11.5 million), which includes a residual amount from the previous year, was paid out by the Agency. Of the £12.6 million subsequently paid out in respect of child maintenance during the year, £8.3 million (2001-02: £7.4 million) was paid over to persons with care and £3.9 million (2001-02: £3.7 million) to the Department for Social Development, where persons with care are in receipt of income support. The balance of £0.4 million (2001-02: £0.4 million) comprised refunds of overpayments to non-resident parents.

1.12 Balances due under full maintenance assessments and movements in those balances during 2002-03 are shown in note 6.1 to the Client Funds Account. Equivalent information is given for interim maintenance assessments in note 7.1. At 31 March 2003, the balance of full maintenance assessments outstanding totalled £9.3 million (£8.7 million at 31 March 2002) while the balance of interim maintenance assessments outstanding totalled £1.1 million (£2.8 million at 31 March 2002). The balances disclosed in notes 6.1 and 7.1 in relation to full and interim maintenance amounts outstanding exclude balances that the Agency regards as probably uncollectable.

1.13 The Agency undertook a debt analysis exercise at 31 March 2003 which established three categories for the total debt, that is, collectable, possibly uncollectable and probably uncollectable. Similar debt analysis exercises were undertaken in the previous five years. The probably uncollectable amounts are written down in year and relate to amounts which are likely to be very difficult to collect due, for example, to the lack of recent payments from the non-resident parent or the personal circumstances of the non-resident parent. However, the amounts outstanding on individual cases still remain due in full and the Agency continues to consider any new facts brought to its attention regarding collectability. It has not waived its discretion to take action in the future to collect any amount outstanding which becomes collectable. My staff tested a sample of cases from the debt analysis exercise to ensure that the Agency had properly classified the total debt as at 31 March 2003.

1.14 Notes 6.1(iv) and 7.1(iv) to the Account show that this accounting policy has resulted in full maintenance assessment balances shown in note 6.1 being reduced by £18.8 million and interim maintenance assessment balances shown in note 7.1 being reduced by £14.9 million at 31 March 2003 (figure 4).

1.15 Figure 4 below compares the key Client Funds Account figures year on year since 1996-97, while figure 5 provides a percentage comparison of these figures. At 31 March 2003, debt outstanding (including uncollectable debt) totalled £44.1 million, representing a 12 per cent increase over 2001-02. However, as figure 5 shows, although the total debt outstanding continues to increase annually, it has been doing so at a much reduced rate compared to 1997-98. This demonstrates the efforts being made by the Agency to collect maintenance payments from non-resident parents.

Figure 4 : Northern Ireland Child Support Agency : Key Client Funds Account Figures

	1996-97 £m	1997-98 £m	1998-99 £m	1999-00 £m	2000-01 £m	2001-02 £m	2002-03 £m
Receipts	**5.5**	**7.9**	**9.2**	**10.5**	**11.2**	**11.7**	**12.5**
Debt Balances:-							
Full Maintenance Assessments	6.7	6.4	8.3	8.3	7.5	8.7	9.3
Interim Maintenance Assessments	2.4	2.3	2.7	2.4	2.3	2.8	1.1
Debt Classified as Uncollectable:-							
Full Maintenance Assessments*	4.0	6.9	7.3	9.6	13.4	15.5	18.8
Interim Maintenance Assessments	5.1	6.6	8.3	11.1	11.9	12.4	14.9
Total Debt	**18.2**	**22.2**	**26.6**	**31.4**	**35.1**	**39.4**	**44.1**

*Prior to 1999-2000 movements in deferred debt were classified as uncollectable (paragraph 2.19). Following a change in accounting treatment in 1999-2000, deferred debt is no longer treated as uncollectable and the figure for 1998-99 has been restated accordingly.

Source: Published Accounts

Figure 5 : Northern Ireland Child Support Agency: Key Client Funds Account Figures Percentage Change Year On Year

	1996-97 %	1997-98 %	1998-99 %	1999-00 %	2000-01 %	2001-02 %	2002-03 %
Receipts	67	44	16	14	7	4	7
Debt Balances:-							
Full Maintenance Assessments	8	-4	30	0	-10	16	7
Interim Maintenance Assessments	-33	-4	17	-11	-5	22	-61
Debt Classified as Uncollectable:-							
Full Maintenance Assessments	111	73	6	32	40	16	21
Interim Maintenance Assessments	42	29	26	34	7	4	20
Total Debt	**19**	**22**	**20**	**18**	**12**	**12**	**12**

Negative figures represent a decrease.
Source: Published Account

Corporate Governance

1.16 In accordance with Department of Finance and Personnel guidance, the Agency introduced a corporate governance framework and risk management system in 2000-01 which enabled the Chief Executive of the Agency, as Accounting Officer, to provide a signed statement on the Agency's system of internal financial control with the 2000-01 annual accounts. During 2001-02 and 2002-03 this system was further embedded throughout the Agency at all levels to allow the Chief Executive to sign a full statement on internal control, prepared in accordance with updated Department of Finance and Personnel guidance.

1.17 The Agency's Corporate Governance Framework specifies the decision making process in the Agency and the roles and responsibilities of the various committees and Directors of the Agency. The Agency recognises that an important aspect of Corporate Governance is the need for a risk management system and its current system:

- identifies and manages the significant risks of the Agency in relation to it delivering its objectives; and
- provides an assurance chain that the proper controls are in operation to enable the Agency to identify the risks to delivering its business objectives.

1.18 The Agency's Internal Audit Unit provides the Accounting Officer with an independent view on whether the system of internal control is operating effectively. I review whether the statement on internal control reflects the Agency's compliance with the Department of Finance and Personnel's guidance and report if it does not meet those requirements, or if it is misleading or inconsistent with other information I am aware of from my audit. In my view, the 2002-03 statement adequately complies with the Department of Finance and Personnel guidance, reflects the inherent weaknesses in the Agency and sets out its plans to address these weaknesses.

Part 2 : Examination of the Client Funds Account

Introduction

2.1 This part of my report sets out the results of my examination of the Northern Ireland Child Support Agency's Client Funds Account for 2002-03. It summarises the outcome of the audit by the Northern Ireland Audit Office of transactions and balances and explains why I have qualified my audit opinion on the Account. It also compares previous years' audit results and reviews the levels of compensation paid out by the Agency.

Audit Results

2.2 I have examined representative samples of receipts from non-resident parents and maintenance debt balances. The results of these examinations allow me to confirm the existence of material error within the account but are subject to margins of statistical uncertainty. In 2002-03 my staff examined 30 receipts/full maintenance case units involving some 96 assessments (2001-02: 182 assessments) and 30 interim maintenance case units involving 35 assessments (2001-02: 33 assessments). While the number of full maintenance assessments examined fell significantly in 2002-03 compared to the previous year, the percentage of errors found rose from 40 per cent in 2001-02 to 50 per cent in 2002-03 (figure 8). In my view:

- the reduced number of incorrect receipts and the corresponding reduced levels of over and underpayments of receipts in 2002-03 (figure 6); and

- the reduced number of incorrect full maintenance balances and the corresponding reduced levels of over and understatements in these balances during the year (figure 7)

should not be wholly viewed as indicating a significant improvement in the Agency's performance in the accuracy of assessments, but rather may have resulted from the statistical uncertainty surrounding the sample of case units selected. Notwithstanding the reduced numbers and levels of error, the audit results set out in paragraphs 2.3 to 2.14 indicate that the levels of error in receipts and full maintenance balances in 2002-03 remained material and indeed the number of errors found in new assessments during the year were also significant (figure 8).

Receipts and Payments

2.3 From the representative sample of receipts from non-resident parents in 2002-03, I found that in 90 per cent of cases examined the receipt was correct. In 10 per cent of cases the receipts were for the wrong amount, because of errors in the underlying maintenance assessments.

2.4 The Agency's Case Monitoring Team reported that the accuracy of the cash value of decisions made in 2002-03 was 86 per cent against a target of 80 per cent. The Agency's method of calculating cash value accuracy was changed from 2001-02 so that only the accuracy of the last decision on an assessment was measured, rather than looking back over decision making throughout the life of the claim. My audit, on the other hand, examines the cash value of client funds received each year and subsequently paid out by the Agency, together with the amount of maintenance outstanding at the year end. This involves examining each assessment decision over the life of the claim. Due to this difference in approach and reporting methodology the Case Monitoring Team's results are not directly comparable to my results in respect of receipts. Nevertheless, both sets of results show unacceptable levels of inaccuracy.

2.5 The sampling techniques used in the audit have enabled me to extrapolate the results to provide an estimate of the level of monetary error in the receipts and payments account. I estimate that overpayments by non-resident parents amounted to £61,500 (0.5 per cent of the £12.5 million collected in 2002-03), while there were no underpayments. The total of estimated overpayments by non-resident parents is a material sum and I have qualified my audit opinion because of this.

2.6 Figure 6 below summarises the levels of error in receipts from non-resident parents reported by me since 1997-98. The Agency has had a history of material error in maintenance received, due, as I have previously pointed out, to the legacy of errors in the underlying maintenance assessments.

Figure 6 : Summary of the Levels of Receipt Errors

	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03
Percentage of receipts incorrect	19%	20%	49%	47%	30%	10%
Value of overpayments	£0.4m	£1.4m	£1.3m	£1.1m	£1.1m	£0.1m
Percentage of overpayments against total receipts	5%	15%	12%	10%	10%	0.5%
Value of underpayments	£0.05m	£0.1m	£0.4m	£0.05m	£1.5m	Nil
Percentage of underpayments against total receipts	0.6%	1%	4%	0.5%	13%	Nil

Maintenance Balances

2.7 I examined a representative sample of balances due from non-resident parents in 2002-03. This required verification of all transactions supporting each balance and a re-performance of the assessments, charges, transactions and adjustments made throughout the lifetime of the case.

2.8 My staff identified errors in 43 per cent of full maintenance balances and errors in 33 per cent of interim maintenance balances examined. However, as interim maintenance assessments are set at punitive rates which do not take into account the non-resident parent's ability to pay, approximately 93 per cent have been written down in the Account as probably uncollectable.

2.9 Extrapolation of the audit results indicates that the £9.3 million shown in note 6.1 to the Account as due at 31 March 2003 from non-resident parents for full maintenance assessments is likely to include overstatement errors amounting to an estimated £414,100 (4 per cent of the amount outstanding). Understatement errors amounted to an estimated £118,000 (1 per cent of the amount outstanding).

2.10 Similarly, I estimate that the £1.1 million shown in note 7.1 as due at 31 March 2003 for interim maintenance assessments is likely to include overstatement errors amounting to an estimated £67,500 (6 per cent of the amount outstanding). Understatement errors amounted to an estimated £3,400 (0.3 per cent of the amount outstanding).

2.11 A summary of the levels of error in full and interim maintenance balances reported by me since 1997-98 are summarised in figure 7 below.

Figure 7 : Summary of the Levels of Errors in Full and Interim Maintenance Balances

	1997-98		1998-99		1999-00		2000-01		2001-02		2002-03	
	Full	Interim	Full	Interim	Full	Interim	Full	Interim	Full	Interim	Full	Interim
Percentage of balances incorrect	22%	11%	56%	25%	80%	23%	63%	33%	70%	17%	43%	33%
Value of overstatements **£m**	0.8	0.3	4.0	0.2	2.9	0.1	2.1	0.3	3.2	0.1	0.4	0.7
Percentage of overstatements against total balance	13%	11%	48%	6%	35%	4%	28%	13%	37%	4%	4%	6%
Value of understatements **£m**	1.8	0.02	1.5	0.07	0.6	0.2	1.7	0.01	4.4	0.01	0.1	0.01
Percentage of understatements against total balance	28%	0.7%	18%	2%	7%	8%	23%	0.3%	51%	0.3%	1%	0%

2.12 I found that misstatements in full and interim maintenance balances were frequently attributable to combinations of errors made in 2002-03 and earlier years. Some errors will have had a single impact on the amounts due or adjustments made, but most will have had recurrent effects on regular maintenance due and sums received. Figure 8 analyses the errors found from the full maintenance assessments examined during the audit into time bands.

Figure 8 : Analysis of Errors found from 2002-03 examination of Full Maintenance Assessments

Period of Assessment	Number of Assessments Examined	Number of Errors	% of Errors per Number Examined
Pre 1 April 1997	19	14	74%
1 April 1997 - 31 March 1998	10	7	70%
1 April 1998 - 31 March 1999	11	6	55%
1 April 1999 - 31 March 2000	17	6	36%
1 April 2000 - 31 March 2001	12	1	8%
1 April 2001 - 31 March 2002	17	9	53%
1 April 2002 - 31 March 2003	10	5	50%
Total	**96**	**48**	**50%**

The above analysis is based on a sample extraction of maintenance assessments. The 50 per cent error rate in 2002-03 compares to a 40 per cent error rate in 2001-02.

2.13 Since many of the errors in balances at 31 March 2003 arose from errors made in earlier years, the balances brought forward at 1 April 2002 also contained material amounts of error. These erroneous balances and the continuing impact of errors in charges and adjustments, along with a high level of additional errors made in 2002-03 resulted in the total level of misstatements in full and interim balances at 31 March 2003. The significant number of errors made (50 per cent compared to 40 per cent in 2001-02) in my view is disappointing.

2.14 In the light of these results, I have concluded that the amounts reported in notes 6.1 and 7.1 as being due from non-resident parents at 1 April 2002 and 31 March 2003 are materially misstated. Since these notes do not properly present the maintenance balances due I have qualified my audit opinion.

Causes of Error

2.15 The majority of errors in receipts from non-resident parents in 2002-03 referred to in paragraphs 2.2 to 2.6 were caused by mistakes in the underlying maintenance assessments. Most maintenance assessment errors arose from mistakes by the Agency's staff in calculating the income element of assessments, applying the incorrect effective date, applying incorrect housing costs and recording adjustments incorrectly on the Child Support Computer System (figure 9). Errors in receipts will also have an effect on the accuracy of outstanding balances. A major contributor to poor performance has been insufficient evidence recorded by decision makers to substantiate their decisions (see also paragraph 3.9). Historically the difficulty for staff has been the high volumes of intake, the frequency of changes in information, the clearance target deadlines and competing priorities. Figure 9 below analyses the causes of error in 2002-03. In most cases examined, a number of different causes were highlighted.

Figure 9 : Analysis of the Causes of Error in Receipts and Maintenance Balances in 2002-03

		Number of Errors		
Causes of Error	**Receipts**	**FMAs**	**IMAs**	**TOTAL**
Incorrect earnings applied	2	10	-	12
Incorrect benefits rates applied	-	3	4	7
Incorrect effective date applied	4	13	3	20
Incorrect adjustments to Child Support Computer System	-	8	3	11
Incorrect housing costs applied	-	7	-	7
Incorrect number of qualifying children	-	-	1	1
Other	1	7	-	8
Total	**7**	**48**	**11**	**66**

2.16 While the problems associated with the system undoubtedly impact on the levels of accuracy, the Agency accepts that there is further room for improvement. It continues to explore ways of improving performance in the accuracy of assessments and the range of initiatives which have been implemented, aimed at delivering sustained improvement in cash value accuracy, have included improving the quality loops in the operational areas so that staff learn from their mistakes and increasing the frequency of managerial checks in order to reduce the number of errors. The introduction of the new child support scheme will also lead to an improvement in accuracy as the maintenance calculation has been greatly simplified. This will mean that there will be less chance of making an error.

2.17 In my previous reports on this account I have stated that the Agency's poor performance has left a legacy of error. The results of both my audit and of the Agency's internal performance measuring unit (paragraph 3.8) suggest that there continued to be concerns over the Agency's performance in 2002-03. The Agency has reiterated that it had been very difficult to make substantial improvements under the old child support scheme regulations largely because staff had to process the complex information required to make an assessment using a dated and inadequate computer system. It appears to me that the Agency is relying heavily on the new legislation to simplify the child support arrangements which was effective from 3 March 2003 (paragraphs 4.1 to 4.10). However, these arrangements have only recently been put in place and during 2003-04 the Agency must ensure that it continues to provide the highest possible service to its customers.

Compensation Payment

2.18 As a consequence of the errors and delays in the provision of its service, the Agency has had to make compensation payments. Compensation is awarded by the Agency in accordance with guidelines set by the Department for Social Development in consultation with the Department of Finance and Personnel. In my report on the 2001-02 Client Funds Account (NIA 51/01) I drew attention to the significant amount of compensation being paid out by the Agency to non-resident parents and persons with care. In 2002-03 the Agency made 548 payments totalling £218,000 (2001-02 : 545 payments totalling £177,100) and these are disclosed in the Agency's Administration Account.

2.19 In addition, 10 further payments totalling £16,600 (2001-02 : 27 payments totalling £38,300) were made by the Agency in respect of deferred debt. From April 1995, the Agency has been able to defer some debt indefinitely where the accumulation of arrears was a direct result of processing delays on the part of the Agency. Provided non-resident parents meet certain conditions on payment of regular maintenance and the remaining debt outstanding, the Agency can, in cases of hardship, settle debts with the persons with care out of monies provided by the Exchequer and take over the ownership of the debts. These payments are also accounted for in the Agency's Administration Account. Figure 10 below shows the number and value of compensation payments, including deferred debt payments, made by the Agency from 1995-96 to date.

Figure 10 : Compensation payments made by the Agency between 1995-96 and 2002-03

Year	Number	Value £
1995-96	22	15,700
1996-97	70	50,000
1997-98	129	91,500
1998-99	152	133,500
1999-00	273	142,200
2000-01	407	224,800
2001-02	572	215,400
2002-03	558	234,600
Total	**2,183**	**1,107,700**

2.20 As Figure 10 indicates, since 1995-96 the Agency has paid out compensation totalling £1.1 million in 2,183 cases, at an average cost of £507. This is of some concern as it reflects the errors and delays made by the Agency in calculating maintenance assessments. As I indicated in my report on the 2001-02 Account (NIA 51/01) the only effective way that the number and value of payments can be reduced to an acceptable level is if the Agency processes applications and assessments correctly and promptly.

2.21 The Agency has told me that during 2002-03 it initiated a process in which its Finance Management, in conjunction with its Quality Development Team, examined the reasons and causes behind compensation payments being generated. The aim is to try to reduce and eliminate the need to make compensation payments. This work is currently ongoing. In addition, in 2002-03 the Agency's Internal Audit Unit reviewed the processing of compensation payments by the Agency and concluded that while there were adequate controls in place a number of key controls were not operating effectively. Internal Audit further concluded that the controls in place to ensure compensation payments are accurately recorded, monitored and reported to management are inadequate. Work on improving these controls is also ongoing. Overall, Internal Audit considered that the weaknesses in the system of control were such as to put the system objectives at risk and considered limited assurance was appropriate for the overall system in operation. The Agency has also told me it considers that the recent introduction of the new child support scheme will remove many of the complexities staff have had to deal with under the old scheme and expects it to assist in reducing the number and value of compensation payments. I intend to continue to keep compensation payments under review during the audit of the 2003-04 Account.

2.22 Compensation paid out to non-resident parents and persons with care is made up of a number of elements covering consolatory payments for inconvenience or distress, actual financial loss and repayments of maintenance overpaid by non-resident parents. The amounts paid out by the Agency in 2002-03 for each of these elements, including payments of deferred debt, are set out in figure 11 below.

Figure 11 : Breakdown of the 2002-03 Total for Compensation

Element	Amount £
Consolatory	22,100
Actual financial loss	42,500
Repayments of maintenance	141,000
Payment of deferred debt	16,600
Other	12,400
Total	**234,600**

2.23 The largest single amount of compensation paid in 2002-03 was £5,224 in respect of the repayment of maintenance overpaid by a non-resident parent. This was an 'arranged' case where the non-resident parent paid the maintenance directly to the parent with care as opposed to through the Agency. The case was subsequently closed as the qualifying child became ineligible for maintenance through age. Unfortunately the Agency failed to inform the non-resident parent of the case closure with the result that he continued to (over)pay maintenance to the parent with care. The compensation paid represented the actual amount of maintenance overpaid by him. Payments of this magnitude are, however, exceptional and the average payment made by the Agency in 2002-03 was £420.

Part 3 : Progress Against Performance Targets

Introduction

3.1 This part of my report details the progress made by the Agency against targets set by the Minister for Social Development.

3.2 In 2002-03 the Northern Ireland Child Support Agency was set key targets covering a number of aspects of its performance, focusing upon providing better customer service:

- **accuracy** - the cash value based on the last decision only on all assessments checked (2002-03 target : 80 per cent). [Up to and including 2000-01, the Agency was required to report on the cash value accuracy of all full assessments in the year];
- **cash compliance** - the measure of the proportion of the total amount of child maintenance which is due for payment that is actually being paid (2002-03 target : 72 per cent);
- **case compliance** - a measure of the proportion of cases where the non-resident parents are paying child maintenance (2002-03 target : 74 per cent);
- **customer service standards:**

  (a) aim to pay parents with care (or into their bank or building society) their child support maintenance within 10 days of receiving it from the non-resident parent (2002-03 target : 98 per cent);

  (b) aim to answer customer phone calls first time if they telephone with an enquiry during normal working hours (2002-03 target : 85 per cent); and

  (c) aim to resolve the majority of customer complaints within 20 working days of receipt (2002-03 target : 68 per cent).

3.3 Figure 12 summarises the Agency's achievement against its 2002-03 key Ministerial targets (paragraph 3.2), comparing performance with 2001-02.

Figure 12 : Key Ministerial Targets 2002-03 (2001-02 comparative figures are in brackets)

	Target %	Outturn %	Achievement Yes/No
Accuracy			
On the last adjudication for all assessments checked (see paragraph 3.2)	80 (78)	85.5 (81.9)	Y (Y)
Cash Compliance			
Proportion of the total amount of child maintenance due for payment that is actually being paid	72 (72)	75.9 (73.4)	Y (Y)
Case Compliance			
Proportion of cases where the non-resident parents are paying maintenance	74 (74)	79.9 (77.8)	Y (Y)
Customer Service Standards			
(a) See paragraph 3.2	98 (98)	99.3 (99.2)	Y (Y)
(b) See paragraph 3.2	85 (85)	96.6 (88.7)	Y (Y)
(c) See paragraph 3.2	68 (68)	100.0 (78.6)	Y (Y)

3.4 Figure 12 confirms that the Agency achieved all its key Ministerial targets in 2002-03. The outturns achieved have been validated by the Agency's Internal Audit Unit.

Accuracy of Maintenance Assessments

3.5 While recognising the complexity of the process involved when assessing maintenance, I expressed concerns in previous reports over the high levels of inaccuracy in maintenance assessments and the impact this has on receipts from non-resident parents and outstanding balances. The Agency's performance against Ministerial targets for the accuracy of the cash value of assessments since 1996-97 is summarised in Figure 13.

Figure 13: Summary of Performance against the key Ministerial target for Accuracy

	Target	Achieved %
1996-97	85 (a)	86
1997-98	85 (b)	87
1998-99	75 (c)	85
1999-00	80 (c)	81
2000-01	80 (c)	67
2001-02	78 (d)	82
2002-03	80 (d)	86

(a) target related to month of March only.

(b) target related to whole year average.

(c) target related to last full assessment.

(d) target related to last decision only.

3.6 As indicated in paragraph 3.2, the target for accuracy and reporting methodology was changed in 2001-02. Instead of reviewing the entire accuracy of an assessment as before, the measure of accuracy is now based on the last action or adjudication decision taken on a case. This may involve a minor change in circumstances, for example, an increase in rates payable by the non-resident parent. The Agency, therefore, no longer measures historic error or other errors in year. I understand from the Agency that the change was made to 'reflect Ministers' acknowledgement that legacy errors over the years obscure the impact of process developments which have been introduced, and their desire that more recent decision-making has improved as a result'.

3.7 To help achieve and maintain good standards of decision making, the Agency has the assistance of a Standards Committee, which also acts on behalf of the Social Security Agency, under the direction of an independent chairperson. The Committee examines regular reports from the Agency's independent Case Monitoring Team which conducts a systematic examination of decisions, reports on standards and recommends action for improvement. The Standards Committee reports annually to the Agency's Chief Executive. The Department for Social Development is required by legislation to prepare a report on the Committee's findings on standards and a copy of the 2002-03 report, scheduled for distribution and publication in July 2003, will be placed in the Northern Ireland Assembly library.

3.8 The 2002-03 report notes that the figures for cash value accuracy continued to improve in 2002-03. Figure 13 indicates an accuracy rate of 86 per cent in 2002-03 compared to 82 per cent in 2001-02 indicating a further upturn in performance and achievement of the Ministerial target for 2002-03 of 80 per cent. While these figures are encouraging, the results of my testing in 2002-03, set out in Part 2 of this report, indicate a high level of error in new assessments made during the year (figure 8). In my view, therefore, there is little room for complacency in that there remained a high level of decisions which contained an inaccuracy that led to the wrong amount of maintenance being calculated.

3.9 The Committee's report also indicates that insufficient evidence accounted for 15 per cent of decision making errors during 2002-03. An insufficient evidence comment is made when the decision maker has failed to fully investigate and/or record their decision. The report further points out that although the lack of evidence on which to base a decision continues to be a contributory factor to decision making errors, the Agency has seen a 72 per cent reduction in the number of insufficient evidence comments made in 2002-03. The main areas of insufficient evidence comments during the year reported by the Committee were in the calculation of earnings, the application of incorrect housing costs and applying the incorrect effective date. These areas of concern are similar to those highlighted by me as a result of testing in 2002-03 (see paragraph 2.15 and figure 8).

3.10 I met with the Standards Committee Chairman during the year to discuss our respective review and reporting methodologies and my staff further liaised with him to discuss the findings of my 2002-03 audit and the results of the Case Monitoring Team's work during the year. This proved to be mutually beneficial.

3.11 Clearly, the fact that around one in seven maintenance assessments monitored during 2002-03 revealed that an incorrect amount of maintenance was being sought remains unacceptable. The impact of this level of inaccuracy on receipts from non-resident parents and outstanding balances is very significant, as borne out by the findings of my 2002-03 audit set out in Part 2 of this report. The Agency has clearly still much to do to meet the levels of accuracy expected by Parliament and its clients. In my view, the child support reforms should not be viewed as a panacea for all of the problems Child Support Agency customers have endured over the past ten years. It should be recognised that the new scheme incorporates a simplified maintenance calculation meaning that there will be less chance for error. The new IT system has had significant initial teething problems and is being subjected to a consolidation programme to improve performance. I intend to again closely monitor accuracy levels as part of my audit of the 2003-04 Account.

Part 4: Child Support Reforms

Introduction

4.1 The objectives of the Child Support Reforms are to:

- be simple, clear and easy to understand so that under the new scheme non-resident parents will know immediately how much they need to pay for their children, and how much they will have left to meet their other responsibilities;
- put the needs of their children first, making it clear that the parents' legal and moral responsibilities to their children overrides other day-to-day expenses;
- give extra help to children on Income Support through the child maintenance premium;
- be streamlined and customer friendly such that maintenance is assessed and collected within a few weeks of receipt of an application; and

- offer a personal, localised service that integrates child support with other family support services.

4.2 The original date for the implementation of the reforms was April 2002. However, this was deferred because both the Agency in Great Britain and the Northern Ireland Agency were not satisfied that the required technical infrastructure and IT functionality had been sufficiently tested. Following further piloting and detailed testing of the new IT system the reforms were introduced on 3 March 2003, from which date all new applications for maintenance could expect to be subjected to the new rules.

4.3 As at 31 March 2003, 756 new cases were being processed under the new rules with full maintenance assessments having been made in one case. There were a further 360 cases initiated before 3 March that were linked to a new application and had therefore been migrated to the new system, some of which remained on old rules. At 31 March the total live case load on the old system was 33,000. The Agency is therefore now dealing with three distinct types of case:

- those held on the old computer system and being processed using old rules;
- those held on the new computer system being processed using old rules; and
- those held on the new computer system being processed using new rules.

Continuing Challenges

4.4 Child Support Reforms represent an ambitious and complex undertaking which impacts on all aspects of the Agency's operations. The reforms encompass a range of initiatives and pose a number of challenges yet to be fully addressed by the Agency. In particular, these include:

- improved accuracy and case compliance;
- migration;
- conversion; and
- system functionality.

Improved Accuracy and Case Compliance

4.5 Historically errors in maintenance assessments identified by the Northern Ireland Audit Office have primarily related to the calculation of housing costs and net income. Under the reforms, the former are no longer a component of the assessment formula and the latter is now calculated on a much simpler basis. These developments and a new IT system which offers on-line support provide a basis for improved accuracy rates.

4.6 In 2001-02, a new system was introduced that integrates debt management with the Agency's main operational processes. This now enables the Agency to identify a non-resident parent's failure to pay maintenance on a timely basis, and take appropriate action.

Migration

4.7 Successful migration of case information from the original computer system to the new one is a critical step in implementing the Child Support Reforms. This will involve:

- reactive migration when a new application is made which includes a non-resident parent or parent with care already involved in a current case. The existing case is transferred from the old system to the new system to enable both cases to be handled on the new system;
- bulk migration when large numbers of cases remaining on the original computer system will be moved to the new system. The Agency recognises the risks inherent in an exercise of this type and has put arrangements in place aimed at securing the accurate and complete transfer of data from one system to the other.

4.8 At 31 March 2003, 789 cases had been identified as linked to new applications and of these 360 had been successfully migrated to the new system. Bulk migration will commence when the Agency is satisfied that the new system is stable. It is planned that this will be preceded by a full dry run which will include reconciliation at case level to ensure that data will be transferred accurately.

Conversion

4.9 Once migration has been completed, conversion is the process whereby all existing maintenance assessments will be recalculated using the new rules introduced by the reforms. The Agency accepts that this will result in both 'winners' and 'losers' amongst non-resident parents and parents with care. It has a strategy in place to deal with complaints from customers and has set up customer contact centres to ensure queries from customers whose assessments have changed can be dealt with quickly. As part of the strategy a mailshot has been sent to customers describing the forthcoming changes. Further mailshots are planned to keep customers advised of the changes.

System Functionality

4.10 When the new system went live the Agency recognised that there were a number of issues which could not be resolved immediately. Alternative processes have been introduced, including manual procedures, until the relevant enhancements to the computer systems are developed, tested and implemented.

Invest Northern Ireland Financial Statements 2002-2003

Introduction

1. I qualified my opinion on Invest Northern Ireland's accounts as insufficient evidence was available to me on the recording, monitoring and use of funds by third party organisations (TPOs). TPOs are private sector or voluntary bodies which Invest NI contracts to deliver initiatives by means of financial assistance, advice or other services to customers who otherwise would have received such assistance directly from Invest NI. TPOs include, for instance, local enterprise centres delivering the Business Growth programme, Enterprise NI managing the the Northern Ireland Business Start Programme and other entities managing loan or venture capital funds. Invest NI paid some £6 million TPOs in 2002-03. Many of these TPOs also receive funds from other sources such as the International Fund for Ireland and District Councils.

2. On its formation on 1 April 2002, Invest Northern Ireland (Invest NI) inherited contracts with TPOs from the Local Enterprise Development Unit (LEDU). I was not LEDU's auditor as it was a company limited by guarantee and therefore audited by a private sector firm under the terms of the Companies (Northern Ireland) Order 1986 but I did have inspection rights.

Into the West

3. In December 2001, anonymous written allegations of financial impropriety and poor value for money were received concerning one of these TPOs, Into the West (Tyrone and Fermanagh) Limited (ITW). ITW received public funds of £386,000 including £189,000 from LEDU between October 1997 and March 2002. My report on the independent investigation of ITW is appended (Appendix 1). The investigation questioned the adequacy of the supervision and control arrangements exercised by LEDU and the application of these by LEDU staff involved.

Review of Contracts with Third Party Organisations

4. In 2002 Invest NI commissioned consultants to conduct a review of the TPO contractual relationships inherited from LEDU. This was a desk review of contractual arrangements for contracts with a value over £20,000. Twenty eight contracts were examined. The consultants' report was finalised in February 2003 and concluded that Invest NI's contractual and purchasing arrangements with TPOs were deficient. The main findings were that:

- contracts were not clear as to the services required and the expected outputs were often omitted;

- a number of contracts were let without any tendering process; and
- there were no formal monitoring systems to provide Invest Northern Ireland with assurance that TPOs were complying with the terms and conditions of the contracts.

5. In response to these findings, Invest NI introduced revised procedures over new contracts in 2003-04. New guidance has been issued and an Audit and Control function set up to manage the budget to TPOs. These revised procedures did not apply during the period of these accounts. Payments made by LEDU in years prior to 2002-03 were not supported by an adequate system of controls. These deficiencies were inherited by Invest NI from its formation and applied to payments made during 2002-03. I note, in particular, that the desk review carried out by the consultants in 2002-03 was not underpinned by a programme of inspection visits to TPOs. In the absence of a structured inspection programme of TPO books and records, insufficient evidence is available to me to confirm that public funds issued to these bodies have been used for the purpose intended by the Northern Ireland Assembly or Parliament.

Loan and Venture Capital Funds

6. The Chief Executive refers in the Statement of Internal Control to action taken to investigate specific governance, contractual and monitoring weaknesses in particular contracts. In addition to a general review of TPO contracts inherited from LEDU, Invest Northern Ireland, in January 2003, commissioned an investigation into the establishment and management of Emerging Business Trust (EBT Loan Fund) and EBT Venture Fund Limited (EBT Venture Fund). The Trust was established in 1996 with funds provided by the International Fund for Ireland and LEDU. The Trust assists in the financing of emerging businesses from disadvantaged areas in Northern Ireland.

7. The investigation is still in progress but major weaknesses in LEDU's oversight of both funds have been identified. Significant governance and regularity issues including LEDU's handling of potential conflicts of interest are still being explored. I intend to report further on the EBT Loan Fund and the EBT Venture Fund Limited when the investigation is completed.

8. In addition, my staff identified a lack of proper monitoring and control over another TPO, Ortus which manages a number of loan funds on behalf of Invest NI. Between 1988 and 1998 the former LEDU paid £1.1 million to Ortus to set up these funds. By December 2002 the funds had diminished significantly to £476,000 as a result of high levels of bad debts and annual management charges. I qualified the 1997-98 accounts of the then Department of Economic Development Vote 2 with regard to payments to Ortus, via LEDU, as there was insufficient evidence to support the use of funds due to inadequate monitoring of the TPO by LEDU. I found that there was an absence of signed loan agreements, insufficient documentation of decisions on recovery of loans and debt write-offs, incomplete records including having only one bank account for various loan Funds creating significant difficulty clarifying balances remaining on each Fund. I concluded that LEDU had not ensured that sufficient procedures were in place. My current review concluded that while monitoring of Ortus had improved, performance criteria recommended by consultants in November 2000 had not been introduced. In January 2004, Invest NI told me that it was in the process of agreeing with Ortus the full extent of the performance indicators that will be practical to implement.

Conclusions and Recommendations

9. Invest NI has acted to improve its own procedures on entering into new contracts with TPOs and has itself identified significant weaknesses in the oversight of contracts inherited from LEDU. However, on the basis of work done by Invest NI at the time of writing this report, I have not been able to obtain sufficient assurance to provide an unqualified report on third party organisations.

10. I recommend that to evaluate the impact of the significant weaknesses identified over existing contracts, Invest Northern Ireland introduce a risk based inspection programme of TPO books and records to confirm that public funds issued to these bodies in 2002-03 and previous financial years have been used for the purpose intended by the Northern Ireland Assembly or Parliament.

11. I intend to report separately on the significant matters arising out of Invest Northern Ireland's own investigation into the EBT Loan and Venture Funds once that investigation is completed.

Appendix 1

Into the West (Tyrone and Fermanagh) Limited

1. 'Into the West (Tyrone and Fermanagh) Limited' (ITW) is a company limited by guarantee and not having a share capital. It was incorporated in 1997, through an initiative led by the former Local Enterprise Development Unit (LEDU), in which LEDU worked in partnership with five District Councils (Cookstown, Dungannon, Fermanagh, Omagh and Strabane) to provide a platform to promote local economic development.

2. In December 2001, I received anonymous written allegations of financial impropriety and poor value for money concerning the activities of ITW. The allegations were also sent to the Department of Enterprise, Trade and Investment (the Department) and the Department of the Environment (DOE - the lead department with responsibilities for Local Government).

3. This report outlines the allegations made, the main findings of the investigation into those allegations and the actions taken by the Department, the DOE and the ITW Board in the wake of the investigation.

Background

ITW Administration and Activities

4. 'Making it Back Home' (MIBH) was a LEDU programme which sought to identify young graduates who had emigrated, in order to encourage them to return to Northern Ireland and play a key role in the economy, preferably by starting their own businesses. In 1997, it was agreed that MIBH would jointly meet LEDU's and the five District Councils' economic development objectives and so ITW was formed. LEDU permitted the company to hold Board meetings in its Western Regional Office, where financial and administrative support was provided by LEDU staff. This was subsequently supplemented by part-time administrative staff hired by ITW. The administrative support was under the management of LEDU's Western Regional Office Manager, who was its representative on the ITW Board and who played a prominent operational role in the company.

5. The Chief Executives of the five District Councils and the LEDU Regional Office Manager became the founding company directors. Council Members later joined the Board from November 1999. Joint funding was provided by the District Councils (which included European Union funding), LEDU and the International Fund for Ireland (IFI) ñ the 'funding bodies'. As well as encouraging ex-patriates to return to the area, the company's primary activities included developing international strategic business alliances and joint ventures between Northern Ireland and overseas companies. A major part of the company's activities involved 'Business Development Visits' to North America, Australia and New Zealand.

ITW Funding

6. Over the period October 1997 to March 2002, the funding bodies provided sums totalling £890,000 to the company, as well as 'in-kind' contributions (management and administrative support) with an estimated value of £302,000 - see Figure 1. (Further funding amounting to some £565,000 for other activities was also provided to the company but this was for activities which fell outside the allegations of waste and impropriety.)

Figure 1: Funding of ITW, October 1997 to March 2002

Funders	Funding[1] (£)	"In-kind" Contributions (£)
District Councils	375,000	113,000
LEDU	197,000	189,000
International Fund for Ireland	318,000	-
Private sector contributions[2]	23,000	-
Total Core Funding	913,000	302,000

Source: DETI
Notes: (1) Based on figures from ITW's audited annual accounts to 31 March 2001 and funding commitments for 2001-02.
(2) Contributions from business delegates on overseas Business Development Visits.

Allegations of Financial Impropriety and Poor Value for Money

7. The allegations received in December 2001 claimed that the vast majority of public money given to ITW had been used on expensive business class air travel and hotel accommodation all over the world, with large groups of councillors and officials having taken part in trips costing up to £50,000. There were three main allegations made:

- Councillors had been receiving cash-in-hand payments of £100 per day for expenses, when food and board was actually being paid, and also claiming a full range of Council allowances;
- the misuse of the ITW credit card to enhance personal payments, with an example quoted of the LEDU Regional Manager charging expenditure to the card during a visit to Boston that was unrelated to ITW work and being accompanied by his wife;
- that LEDU staff within the Western Regional Office had been pressured and intimidated into falsifying documentation in respect of IFI funding.

8. Following discussions between the Department, Local Government Audit (LGA - responsible for the audit of District Councils) and later, the Secretary of ITW, the Board of ITW fully endorsed the need for a joint enquiry and invited the Department's Internal Audit Service (IAS) and LGA to satisfy themselves regarding the probity and propriety of ITW spending. A steering group of senior officials from the Department, DOE and the Department of Finance and Personnel was established to consider matters arising out of the joint investigation.

9. Prior to the commencement of the joint investigation, and following advice from the police, LEDU commissioned independent consultants to investigate the allegations that LEDU staff had been pressured into falsifying documentation in respect of IFI funding. The consultants reported, in January 2002, that the LEDU staff involved were adamant that they had not been pressured or intimidated into making or signing any false declarations.

10. As the joint investigation commenced in February 2002, LEDU's Western Regional Office Manager was relocated to its Belfast Headquarters and later, in June 2002, suspended on full pay. All funding was frozen and ITW's activities were suspended from March 2002. In addition, Invest Northern Ireland (which assumed LEDU's responsibilities from April 2002) established a working group to examine any wider implications arising from the ITW case for its other related activities and control procedures.

Joint Investigation by Internal Audit Service and Local Government Audit

11. The joint investigation team examined each of the specific allegations made. While not all of the allegations were substantiated, a number of areas of concern were highlighted. Details are set out in the attached.

12. In the course of their work, the joint investigation team also noted a number of other matters of concern which they felt required specific consideration by the ITW Board and the funding bodies. These related largely to the use of corporate credit cards and the handling of overseas Business Development Visits involving ITW Board Members, LEDU officials and other delegates. In particular, the team found that:

- **On Corporate Credit Cards** There was no evidence of official Board approval for the credit cards issued to the then Chairman and Secretary; the Board did not ensure that formal systems and procedures were in place with regard to the usage and accounting for credit card expenditure; and a number of receipts and invoices had not been provided by the credit card holders for ITW records. Among the most serious findings were concerns that, out of a total of £155,000 sampled, some £40,000 of expenditure was unsupported by receipts and invoices and cash withdrawals amounting to some £5,600 remained to be properly accounted for.

- **On Overseas Business Development Visits** The Board did not have policies in place for corporate hospitality, travel and subsistence; it did not have adequate formal arrangements to consider and approve requests for financial assistance for all overseas visits; there was no evidence that the Board monitored specific costs of overseas visits; and an estimated £20,000 could possibly have been saved if public sector rates of subsistence had been used.

13. While recording the explanations provided by various individuals who had been involved with the company, including former directors, the joint investigation team concluded that there had been very poor standards of administration, involving considerable sums of public money. They also concluded that, overall, the ITW Board did not exercise the level of control and challenge that would normally be expected of a Board of Directors. However, they did note the ITW Board's view that it had exercised an acceptable level of care and control in respect of the public funds for which it had been accountable. The report also questioned the adequacy of the supervision and control arrangements exercised by LEDU in relation to ITW and the LEDU staff involved.

14. The report made a number of recommendations aimed at improving the Company's strategic and operational framework and its relationships with funding and other bodies. In particular, the report recommended that, should ITW continue in its present form, robust and reliable control systems and procedures to facilitate proper accountability for public funds should be established immediately.

Value for Money Review

15. In June 2002 the funding bodies commissioned consultants to undertake a value for money review of ITW's activities. The consultants report in March 2003 noted that, while a value for money review requires actual outcomes to be compared with a set of objectives established at the outset, in ITW’s case objectives had not been clearly defined. They also commented that this difficulty was compounded by the fact that ITW's role developed over time. Within the context of these difficulties, the consultants carried out a detailed examination of ITW's activities, since its establishment in 1997.

16. In their key findings, they noted that ITW's achievements must be considered within the context of the original concept - the requirement for a platform for collaboration between a number of parties charged with developing economic activity in Northern Ireland. In the consultant's view, given the historical difficulties in achieving co-operation between different parties in Northern Ireland, perhaps ITW's most important and valuable output was that it had been established in the first place. In addition, the cross-community composition of the ITW overseas delegations provided positive evidence of the ability of people from both traditions to work together for mutual benefit. This assisted in reinforcing a positive image of Northern Ireland in the international marketplace.

17. The consultants also reported that all of the stakeholders viewed ITW as a success and noted that ITW's achievement and profile has resulted in it being adopted as a template for economic development in other regions in Northern Ireland. The consultants also commented that a substantial majority of ITW's client companies had responded positively to their enquiries regarding the benefits of taking part in ITW activities - a view which they said was shared both by companies that had been successful in establishing alliances/creating jobs and those that had not.

18. As regards ITW overseas trips to North America, Australia and New Zealand, on which the main items of expenditure had been travel, accommodation and subsistence, the consultants were clear that these costs could have been reduced - for example, by travelling

economy rather than business class, or by a reduction in the numbers travelling. Nevertheless, they concluded that, overall, in judging actual outcomes and costs against the outcomes and costs that could reasonably have been expected at the outset, ITW had provided value for money.

Response to the Joint Investigation and Value for Money Review

19. On completion of the joint investigation and the value for money review in March 2003, the reports were made public. Since then, a number of actions have taken place:

- following consideration of the wider implications of the case by the Invest Northern Ireland working group (paragraph 10), consultants were appointed to review its contractual arrangements for the funding of 'third party organisations', where relationships similar to ITW might exist.
- Invest Northern Ireland also undertook formal disciplinary action against a number of its (former LEDU) staff. As a result, the former LEDU Western Regional manager, who played such a prominent role in the company, was dismissed. In addition, disciplinary penalties were imposed on two other former LEDU staff.
- on completion of the joint investigation, the Department provided the police with a copy of the report and asked them to consider whether there were any grounds for a criminal investigation. The police subsequently concluded that there is no likeilhood of a successful prosecution against any person and indicated that they will not take any action in this case unless and until further evidence comes to light.
- DOE wrote to the Chief Executives and Chairmen of all 26 District Councils asking them to review their financial and legal arrangements with companies and any other bodies that receive Council funding. Responses from the five Councils which funded ITW indicated that lessons had been learned and that arrangements in relation to other bodies being funded were being reviewed. The 26 Councils were also referred to the HM Treasury handbook on 'Regularity and Propriety' which provides guidance on the personal responsibilities of members and officials of Councils serving as Directors on bodies receiving funding.
- DOE is also planning to bring forward legislative proposals which will extend the Local Government Auditor's authority to include access to documentation held by bodies in receipt of District Council funding. Currently, no right of access exists - in the case of the ITW review, the joint investigation team had to secure

the agreement of the ITW Board in order to examine the company's papers. DOE expects to introduce the new arrangements in 2004-05.

- the ITW Board told me that, following suspension of the company's activities in March 2002, revised procedures and controls were agreed by the Board as the nature of the weaknesses became clear. The Board also said that it has acted on the various recommendations set out in the joint investigation report.
- as regards the future of ITW, the Board has developed a plan to put the Company into voluntary liquidation. The Board expects all creditors to be paid in full. A detailed proposal to bring the affairs of the Company to a conclusion has been approved by all of the funding bodies.

20. I will continue to monitor developments in this case and, where appropriate, will report further on my findings.

Annex 1
(paragraph 11)

Allegations of Impropriety and Poor Value for Money: Findings of the Joint Investigation Team

1. ***"Councillors have been receiving cash in hand payments of £100 per day for expenses when food and board is actually being paid on the ground as well".***

The Review Team confirmed that ITW Directors, Officials, Councillors (and other Business Development Visit participants) did receive the £100 daily allowance intended to cover meals and expenses, excluding accommodation which was paid directly by ITW. There were occasions when meals were also provided using the ITW credit card.

2. ***"Many of these Councillors are also claiming additionally a full range of Council allowances".***

The Review Team investigated payments made to Councillors and found no evidence of subsistence being paid by Councils, other than the daily attendance allowance.

3. ***"The vast majority of public money given to this project has been used in expensive business class air travel, trip subsistence and hotel accommodation all over the world".***

The Review Team confirmed that a high percentage of the public funds granted to ITW had been used for overseas business visits. They commented that this was the nature of ITW's business.

4. ***"The company's card has been used extensively as a non-visible means of enhancing personal payments".***

The Review Team confirmed that the credit card had been used extensively and identified cash withdrawals totalling some £5,600 that had not been properly accounted for. Also, a significant percentage of the Visa Card expenditure (25% by value and 87% by transaction volume) was not supported by invoices/receipts.

5. ***"In September 2000 [the then LEDU Western Regional Office manager] went on an all expenses paid trip to Boston to attend a course not related to ITW work and incurred credit card charges of over £3,000. He was accompanied by his wife who was not an authorised participant".***

The Review Team noted that a substantial cash withdrawal (£1,097) was in evidence (although it was contended by the former LEDU manager that this was attributable to daily allowances). In addition, hospitality (of some £750) had been afforded to course delegates and significant telecommunication costs (£1,453) were evident. There was no evidence that any of this expenditure had been necessary or sanctioned by ITW prior to the visit or that the visit itself had been approved.

The Review Team found nothing to substantiate the claim that the former LEDU manager's wife was involved in the visit.

6. ***"Large groups of councillors/officials embarked on 5-14 day worldwide trips costing £40-£50,000.00"***

The Review Team confirmed that a high percentage of the public funds granted to ITW had been used for overseas business visits, as this was the nature of ITW's business. The groups had included Directors, Officials, Councillors and delegates. The Review Team stated that it was not in a position to comment on the appropriateness or make-up and size of the groups.

7. ***"The business creation of these trips over many years has been virtually nil - although big and deliberately false claims have been made".***

The Review Team noted that its focus was on propriety and probity issues - a separate VFM study into ITW activities had been commissioned by the funding bodies.

Note: The consultants who undertook the value for money review examined the employment generation, turnover and business interactions resulting from ITW's overseas activities. Based on a review of the information available and discussions with participating companies, they reported that, in each of the areas examined, there was evidence of positive outcomes. This included examples of additional employment, increased turnover and improved productivity in companies which had been involved in overseas visits. The consultants did comment, however, that ITW's reporting of anticipated outcomes had been unduly optimistic.

National Museums and Galleries of Northern Ireland Financial Statements 2000-01

Introduction

1. The National Museums and Galleries of Northern Ireland (the Museum) is a Non-Departmental Public Body administered by a board of trustees under the provisions of the Museums and Galleries (Northern Ireland) Order 1998. Article 9 of the 1998 Order enables the Department of Culture, Arts and Leisure to make grants to the Board of Trustees in respect of each financial year, with such sums and conditions of grant as it considers appropriate. During 2000-01, £10,566,628 was made available from the Department to the Trustees of the Museum to carry out its activities.

Qualified Opinion on fixed Assets Arising from Limitation in Audit Scope

2. These financial statements continue the process of improvement in financial reporting which has been evident in recent years. However, I have qualified my opinion on the financial statements of the Museum for 2000-01 as the evidence available to me was limited at the Ulster Folk and Transport Museum and the Ulster American Folk Park, because of inadequate accounting records which have been reported on in previous years.

3. The qualification relates to the completeness and valuation of fixed assets at the Ulster Folk and Transport Museum and the Ulster American Folk Park. The total value of fixed assets for all three sites of the Museum at 31 March 2001 is £42,565,933 and includes £1,015,077 of Land, Buildings and other fixed assets which are subject to qualification.

4. My audit of the accounting records maintained by the Museum in support of the values recorded in previous years for fixed assets at the Ulster Folk and Transport Museum and Ulster American Folk Park found that the recording of fixed assets in place at the Museum was incomplete. In place of a fixed assets register the Museum maintained an inventory of assets. My review during 2000-01 continued to find the inventory to be incomplete and there was no identified audit trail. Fixed assets were not subjected to management checks for existence, for continuing use, remaining life or obsolescence. This loss of audit trail prevented my staff from verifying the accuracy and completeness of the value of the fixed assets.

5. The 2000-2001 financial statements include £1,015,077 of fixed assets which in my view have not been reliably valued, and there is not a complete audit trail to support the completeness of these fixed assets. However, this is an improvement over the original position as a significant proportion of the value of fixed assets was the subject of a professional valuation at 31 March 2000 and a revaluation at 31 March 2001 by the Valuation and Lands Agency. These exercises reliably established the value of land and buildings for the financial statements, except for one building (included in the financial statements at a value of £688,154), a residential centre at Ulster Folk and Transport Museum. This building was not included in the professional valuation due to ongoing discussions about its heritage status. It is however included on the list for the next full valuation.

6. All fixed asset additions at the Ulster Folk and Transport Museum and Ulster American Folk Park from the date of the merger (1998-99 onwards) have been transferred to a detailed fixed asset register, together with any detailed records which exist for previous years. In relation to the weaknesses identified in the historic records at both the Ulster Folk and Transport Museum and Ulster American Folk Park, I asked the Museum what steps are being taken to carry out full inventories and valuations of the remaining fixed assets. The Museum told me that they are pleased that they were able to resolve the issues in relation to the Land and Buildings, resolving a significant proportion of the issues relating to fixed assets. The task of carrying out full inventories of fixed assets at the Ulster Folk and Transport Museum and Ulster American Folk Park was completed by September 2003. The task of valuing these assets and estimating their useful life has now commenced. MAGNI has told me that some external assistance will be required in relation to this and has confirmed that if necessary a bid will be submitted to DCAL to seek funding in this respect.

Other Report Issues

7. In addition to the report on the qualification of fixed assets above I have kept the developments made by Museums on other matters under review and have reported on the progress made below.

Income from Admissions:

Ulster Folk and Transport Museum (£203,673)

8. During my audit of the Ulster Folk and Transport Museum's 1995-96 financial statements I noted weaknesses in the system of control over income from admissions. My review of controls operating during the 1996-97 to 1999-2000 financial years found that the weaknesses in the system had not been fully rectified. While new procedures were implemented during 1999-2000 to provide additional control over the completeness of income from admissions their operation was not fully documented until December 2002. However the introduction of the new procedures has ensured that there is a satisfactory audit trail for the purposes of verifying the value of income from admissions at Ulster Folk and Transport Museum and has significantly reduced the risk of loss of income. The accounts are therefore no longer qualified on this issue. I also expect that the collection of admissions income will be further secured by the new visitor ticketing system which was installed during 2001-02.

Other Operating Expenditure

9. My report last year raised concerns over the Museums procedures for tendering in support of ordering and purchasing of goods. My review of these procedures during 2000-01 noted that the documentation in support of ordering and purchasing of goods had improved significantly and procedures for all aspects of tendering have been formally documented since November 2001. During my audit I noted that, the full implementation of these procedures was being established in each of the Museum sites.

10. I will review the Museum's progress in dealing with these issues during my audit of the 2001-2002 financial statements and will report further if necessary.

Conclusion

11. On the basis of the limits imposed on my work due to the limited evidence available to me for fixed assets (£1,015,077) at both the Ulster Folk and Transport Museum and the Ulster American Folk Park due to inadequate accounting records (paragraphs 2 to 6), I have not obtained all the information and explanations that I consider necessary for the purposes of our audit and I have qualified my opinion on the financial statements on the basis of limitation in audit scope.

National Museums and Galleries of Northern Ireland Financial Statements 2001-02

Introduction

1. The National Museums and Galleries of Northern Ireland (the Museum) is a Non-Departmental Public Body administered by a board of trustees under the provisions of the Museums and Galleries (Northern Ireland) Order 1998. Article 9 of the 1998 Order enables the Department of Culture, Arts and Leisure to make grants to the Board of Trustees in respect of each financial year, with such sums and conditions of grant as it considers appropriate. During 2001-02, £11.7m was made available from the Department to the Trustees of the Museum to carry out its activities.

Qualified Opinion Arising From Limitation in Audit Scope

2. These financial statements continue the process of improvement in financial reporting which has been evident in recent years. However, I have qualified my opinion on the financial statements of the Museum for 2001-02 as the evidence available to me was limited at the Ulster Folk and Transport Museum and the Ulster American Folk Park, because of inadequate accounting records which have been reported on in previous years.

3. The qualification relates to the completeness and valuation of fixed assets at the Ulster Folk and Transport Museum and the Ulster American Folk Park.

Fixed Asset Qualification

4. Land and buildings were subject to a professional valuation by the Valuation and Lands Agency at 31 March 2002 which resolved a significant proportion of the issues relating to fixed assets in previous years. This exercise reliably established the total value of land and buildings for the financial statements at £41.3 million, except for one building (included in the financial statements at a value of £688,154), a residential centre at Ulster Folk and Transport Museum. This building was not included in the professional valuation due to ongoing discussions about its heritage status. The Museum told me that it is how-

ever included on the list for the next full valuation.

5. My audit of the accounting records maintained by the Museum in support of the values recorded in the 2001-02 Balance Sheet for fixed assets at the Ulster Folk and Transport Museum and Ulster American Folk Park found that the recording of fixed assets in place at the Museum was satisfactory for those assets purchased since the merger in 1998-99. However details of earlier assets were incomplete and were not subjected to management checks for existence, for continuing use, remaining life or obsolescence. This loss of audit trail prevented my staff from verifying the accuracy and completeness of the value of the fixed assets.

6. The 2001-2002 Museum financial statements disclose a total value of other fixed assets of £2.1 million. These include £418,935 of fixed assets for which there was not a complete audit trail to support the completeness and valuation of these fixed assets. However the Museum told me that a full inventory was completed by September 2003, and the task of valuing these assets and estimating their useful life has now commenced.

Other Report Issue

7. In addition to the report on the qualification of fixed assets above I have kept the developments made by Museums on other non qualification matters under review and have reported on the progress made below.

Income From Admissions:

Ulster Folk and Transport Museum (£211,326)

8. New procedures were implemented during 1999-2000 to provide additional control over the completeness of income from admissions and their operation has been fully documented since December 2002. In addition a new visitor ticketing system was installed during February 2002 however this required further controls over refunds. The Museum told me that revised cash handling procedures were implemented at the Ulster Folk and Transport Museum in December 2002 which included detailed guidance on the refunds procedures. The Ulster Folk and Transport Museum has therefore significantly reduced the risk of loss of income and the accounts are therefore no longer qualified on this issue.

9. I will review the Museum's progress in dealing with this issue during my audit of the 2002-2003 financial statements and will report further if necessary.

Conclusion

10. On the basis of the limits imposed on my work due to the limited evidence available to me for fixed assets (£1,107,089) at both the Ulster Folk and Transport Museum and the Ulster American Folk Park due to inadequate accounting records (paragraphs 4 to 6), I have not obtained all the information and explanations that I consider necessary for the purposes of our audit and I have qualified my opinion on the financial statements on the basis of limitation in audit scope.

Department of Education - Accounting to Parliament by Education and Library Boards

Introduction

1. The Department of Education (the Department) grant aids the majority of services provided by the five Education and Library Boards (the Boards) in Northern Ireland. The Boards are the local education and library authorities for their respective areas, namely, Belfast, North Eastern, South Eastern, Southern and Western. In 2002-03 the Department paid £1,152 million to the Boards.

Statutory Arrangements for Boards' Accounts

2. The Education & Libraries (Northern Ireland) Order 1986 requires each Board to prepare and submit annually to me a statement of accounts before such date, in such form and containing such information as the Department, with the approval of the Department of Finance and Personnel, may direct. The Order requires me to examine and certify those statements of accounts.

3. The Department is required to lay before the Assembly (and to Parliament, while devolution is suspended) a copy of each certified statement of account with a copy of any report I make on them.

4. These arrangements will change for the Boards' 2003-04 accounts which will be prepared under the Education and Libraries (Northern Ireland) Order 2003.

Move from Cash Accounting to Accrual Accounting

5. Until 1998-99 the Department required the Boards to prepare their accounts on a cash basis. On 28 November 1999 the Department directed each Board to prepare accrual accounts for the 1999-2000 and subsequent financial years. The Boards were further directed by the Department, amongst other matters, to submit accounts to me by 30 June immediately following the end of the financial year.

Delays in Finalising Accounts

6. While the Boards have submitted their accounts to me by the due date, all of these required material adjustments. The main areas requiring adjustment are described at paragraphs 8 to 16. The adjustments have taken a considerable time to process. In consequence, I am concerned by the delays in finalising these accounts. The table below shows the dates on which I certified each Board's accounts since the introduction of accrual accounts. At present, three of the five Boards' accounts for 2001-02 remain to be finalised along with all five 2002-03 accounts.

Table: Date of Certification of Boards' Accounts

Year of account	Belfast	North Eastern	South Eastern	Southern	Western
1999-2000	20.6.02	16.5.02	5.6.02	26.9.02	13.3.02
2000-2001	4.3.03	27.3.03	27.1.03	14.10.03	17.6.02
2001-2002	*	*	22.4.04	*	3.3.04
2002-2003	*	*	*	*	*

* indicates that the Board's finalised accounts for that year of account have not yet been submitted for certification

7. The Department laid the Boards' 1999-2000 accounts before the Assembly on 7 May 2003. The Department told me it expects to lay the 2000-01 accounts in early July 2004. Accounts for later years remain to be laid.

Principal Adjustments to Boards' Accounts Submitted for Audit

1999 - 2000 Accounts

8. For the 1999-2000 year of account, each of the five Boards had to produce several drafts of their accounts and (in some cases) opening balance sheets. Considerable additional audit time was spent identifying and discussing accounting issues and reconciling the revised versions of the accounts to what had gone before. This delayed completion of the audits well beyond what I regarded as reasonable or desirable. However, in light of the move to accrual accounting, and the complexity of the Boards' affairs, I gave the Boards every opportunity to present accounts which would attract an unqualified opinion.

9. In July 2002 I drew this to the attention of the Department and was told it expected the Boards' subsequent accounts to be produced in full compliance with the Accounts Direction and relevant accounting standards.

10. The Department told me it acknowledged the flexibility allowed to the Boards to enable them to address the difficulties encountered in moving from cash accounting to an accrual accounting regime. The Department told me this involved resolution of a range of issues including the consistent capture of opening balances, supported by rigorous verification and validation exercises, and the treatment of the Department as a net debtor in Boards' opening accrual accounts. In addition, the Boards had to manage the migration from the previous financial accounting system to a new one.

2000 - 2001 Accounts

11. I noted an improvement in the quality of 2000-01 draft accounts produced by the Boards. However, it still took more than two years for all of them to produce accounts which I was able to certify without qualification. The Department told me that the delay in finalising the Boards' 2000-01 accounts was a consequence of the knock-on effect of the problems and delays encountered in finalising the accounts for the previous year.

2001 - 02 Accounts

12. In March 2002, the Department introduced new accounting and funding arrangements to avoid the need for disbursement of large sums of cash from the Department to Boards at the end of financial years. The Department told me that these new arrangements were designed to maintain the important principle that cash should issue in line with need and that bank balances of funded bodies should be maintained at an operational minimum. The Department instructed the Boards to apply these new arrangements in respect of the 2001-02 financial year. The quantification and consistent application of these arrangements across all five Boards has proved to be difficult. This has been the chief reason for the delays in finalising the Boards' 2001-02 accounts.

13. The Department told me it accepts that difficulties arose in determining the amount of "end of year flexibility" under these new arrangements in the 2001-02 transition year. Further delays arose from the need to liaise with the other funding Departments (the Department of Employment and Learning and the Department of Culture, Arts and Leisure) and to obtain the approval of the Northern Ireland Executive to the new arrangements. The Department told me that, to help address these problems, it issued a model format and guidance in March 2002 and provided ongoing support to Boards. In the following year, the Department commissioned consultants to identify the end of year flexibility in respect of all Boards and agree the figures with the Department of Finance and Personnel to avoid a recurrence of these difficulties in the 2002-03 accounts.

2002 - 2003 Accounts

14. The Boards' land and buildings were subject to revaluation for the purpose of the 2002-03 accounts. Delays in obtaining certified valuations, and subsequent difficulties in accounting for valuation movements, have meant that I have not received final 2002-03 accounts from any of the Boards.

15. The Department told me that numerous representations were made about this issue to the Valuation and Lands Agency and to the Department of Finance and Personnel. It told me it also raised the matter at Accountability Review meetings with Boards and that Boards raised it at meetings of their audit committees. Despite this, the final certified Valuation Certificate was not received by the Boards until early in 2004.

16. The Department also told me that further significant delays have been caused by the need for substantial bespoke work to the supporting fixed asset software system, arising from the accounting treatment of depreciation and, in particular, impairments in valuations.

Accountability to Parliament

17. The Department has a responsibility to ensure the Boards are able to provide accounts and supporting information for audit on time and that they have been professionally prepared, subjected to comprehensive management review and that management has full confidence in them. This is a central requirement of accountability to Parliament.

18. I asked the Department what steps it has taken to ensure that outstanding Board accounts are finalised and that in future the accounts which are submitted to me on the directed date are to the necessary standard. The Department told me it took its responsibilities for the Boards' accounts very seriously and, in order to be more proactive in this

area, had enhanced the professional expertise in the Boards' sponsoring Branch through recruitment of a professional accountant. Regular advice is now provided to the Boards and monitoring and control procedures are being tightened to ensure that accounts are produced on time and to the expected standard. Progress in producing accounts has been included as a standing item on the agenda of the six-monthly Accountability Review meetings held by the Department with each Board.

19. In addition, in my view, there is considerable scope and merit in a thorough review of the accounts to reflect experience from the first four years of accrual accounting and the alignment of the Boards' accounting policies, practices and counter party balances with the Department's resource accounting regime. This is particularly the case as Boards will be included in Central Government Accounts for the first time in 2003-04. I asked the Department if this was under consideration. I was told that the Department has made good progress in working with the Boards to prepare for the requirements of Central Government Accounts. The Department's staff have carried out a dry run for Boards for 2002-03 and will be explaining the processes to Boards' staff in preparation for completion by Boards of the returns for the 2003-04 live year. The Department told me it does not consider that there will be any indebtedness between the Boards and the Department so counter party balances will not occur. The Department considers that many of the problems associated with the move to accrual accounting have been or are being addressed but would welcome the opportunity to consider with the Boards what steps could be taken to improve further the quality and timeliness of their accounts. It is important that improvement is achieved and I will keep progress under review.

Part 3

Northern Ireland Consolidated Fund

Northern Ireland Consolidated Fund

Revenue Accounts

1. The total revenue paid into the Northern Ireland Consolidated Fund in 2002-03 amounted to £8,793 million analysed as follows:

	2002 -2003 £ million	2001- 2002 £million
Receipts from the United Kingdom Government:		
Block Grant	7,799	7,999
Other revenues:		
Rates	609	568
Interest on loans and advances	161	169
Surplus Accruing Resources	31	27
Share of receipts from petroleum licenses	16	17
Other Receipts and transfers	177	191
Totals:	**8,793**	**8,971**

2. In fulfilment of my statutory duty I examined the departmental accounts of the receipts of revenue, and I confirmed that adequate regulations and procedures had been framed to secure an effective check on the assessment, collection and proper allocation of revenue. I also test-checked the correctness of the sums brought to account and I have no comment to make thereon.

3. A summary of the outturn in the year of rate levy and collection is:

	2002-2003 £ million	2001- 2002 £ million
Arrears at 1 April	22	17
Assessment during the year	687	648
Credit carried forward to next period	2	2
	711	667
Discharged during the year by:		
Credits brought forward from last period	2	2
Net receipts	606	568
Vacancies	54	48
Rebates	16	14
Allowances/Disabled Person's Allowance	5	4
Discounts	3	2
Written ñ off as irrecoverable	1	1
Residential Home Relief and other Reliefs	(1)	6
Arrears at 31 March	25	22
Totals	**711**	**667**

4. Assessments rose by £39 million and net receipts by £38 million during the year. Arrears at 31 March 2003 represented 3.5 per cent of the collectable rates for the year, compared with 3.3 per cent in the previous year.

5. The difference of £3 million between the net receipts of rates of £606 million shown in paragraph 3 above and the rates paid into the consolidated fund of £609 million shown in paragraph 1 represents funds transferred in advance to the consolidated fund . This will be adjusted in the next financial year.

Consolidated Fund Issues

6. Issues from the Consolidated Fund fall into two categories:

- Those to meet expenditure on services for which financial provision is voted annually by the Assembly/Parliament (Supply Services); and
- Those to meet expenditure on services for which the Assembly/Parliament, by statute, has authorised a continuing charge not subject to annual vote procedure (Consolidated Fund Services).

Issues for Supply Services are accounted for in the Resource Accounts and issues for Consolidated Fund Services are accounted for in the Public Income and Expenditure Account which is certified by me under Section 2 of the Exchequer and financial Provisions Act (Northern Ireland) 1950.

Consolidated Fund Services

7. The Public Income and Expenditure Account has been published separately as a White paper Account. (HC 1123). The account broadly distinguishes:

(i) issues for payments deemed to have been made out of public income for the year which includes interest on borrowings, district councils' share of revenue from rates, statutory charges on the Consolidated Fund for certain salaries and expenses and advances to funds and bodies;

(ii) issues for payments of a capital nature made out of borrowings which include: public debt repayments; advances to funds and bodies to meet capital expenditure; and

(iii) investments of surplus monies in the short-term money market and temporary advances for Contingencies to fund urgent services on which spending by departments cannot await approval in a Supply Estimate.

8. Total issues in 2002-2003 amounted to £12,005 million compared with £9,227 million in 2001-2002.

	2002-2003 £ million	2001- 2002 £ million
Redemption of Public Debt	114	118
Interest on Borrowings	139	145
Loans for capital Expenditure	20	24
District Councils' share of Rate Revenue	269	248
Miscellaneous Services	1	1
Advances for Contingencies	5	1
Temporary Investments	11,457	8,690
	12,005	9,227

9. Issues for the redemption of public debt were £4 million less than in 2001-2002 due to decreases of £3 million in the redemption of Ulster Savings Certificates and £2 million in the repayment of borrowings from internal funds and an increase of £1 million in payments to the National Loans Fund.

10. Interest on borrowings decreased by £6 million due to decreases of £8 million on payments to the National Loans Fund and an increase of £2 million in Ulster Savings Certificates.

11. Surplus monies held in the Consolidated Fund are invested in the short-term money market. In 2002-2003 these investments totalled £11,457 million compared with £8,690 million in 2001-2002. The sums available are subject to fluctuation depending upon the daily cash flow needs of individual departments.

Part 4

Private Finance Initiative: Reporting of Financial Commitments

Private Finance Initiative: Reporting of Financial Commitments

1. Since its launch in November 1992, the Private Finance Initiative (PFI)[1] has become one of the main methods by which the public sector procures services from the private sector. Its underlying objective is to use the best of both public and private sector skills to improve public services. In particular, this means the use by the public sector of capital assets owned and managed by the private sector.

2. Where PFI is used, the public sector becomes a purchaser of services from the private sector rather than being an owner and operator of assets. Similarly, the private sector becomes a long-term provider of services rather than an upfront asset builder, often combining the responsibilities of designing, building, financing and operating the assets in order to deliver the services required. As a result, the public sector avoids the need for capital expenditure at the beginning of a project in exchange for making payments for services as and when they are delivered, often over a period of up to thirty years.

3. As of July 2003, 29 projects, with a total capital value of £416m, had been procured through PFI in Northern Ireland. However, it is assuming greater significance through the Reinvestment and Reform Initiative and its Strategic Investment Programme with 16 projects, capital value approximately £785 million, in the process of procurement and at various stages of planning.

Northern Ireland Assembly Inquiry

4. During 2001, the Northern Ireland Assembly's Committee for Finance and Personnel examined the use of Public Private Partnerships (PPP)[2], including PFI; with a view to identifying:

- ways of financing Northern Ireland's public sector infrastructure deficit;
- the performance of PPPs to date;
- the degree to which PPPs have achieved Value for Money and the effects of committing money on a long term basis; and
- the patterns and trends emerging which would indicate the suitability, or otherwise, of certain types of projects for PPP.

5. The Committee's report, which was published in July 2001, concluded that HM Treasury was unlikely to meet the outstanding financial needs of Northern Ireland through public expenditure, and other sources, including PPP, would be likely to play a significant role in addressing the infrastructure deficit. The report also recognized that PPP could be a valuable tool and means of investment when used in the right circumstances and that the acceleration of investment in infrastructure through PPP had the potential to improve the quality of services and the economic development of the skills base in Northern Ireland.

[1] PFI is an arrangement wherby a consortium of private sector partners come together to provide and asset-based public service under contract to a public body.

[2] PPP is generally a medium to long-term relationship between the public and private sectors (including the voluntary and community sector), involving the sharing of risks and rewards and utilization of multi-sectoral skills, expertise and finance to deliver desired policy outcomes that are in the public interest.

6. However, the report identified the need for a Northern Ireland investment strategy that established a sustained programme and 'deal flow'. To achieve this, the report recommended the establishment of a unified cross-departmental investment strategy which would address the deficit in infrastructure assets and how it could be best managed and financed. In addition it recommended that the strategy should have the support of all key players, including the private and voluntary sectors and local communities, using a 'social partnership' approach.

7. The report also recognized the need to establish the value for money of the projects over their lifespan and to ensure greater openness and public accountability of the decision making process. To achieve this, it concluded that the full long-term spending implications must be taken into account by the Executive and made visible to the Northern Ireland Assembly.

Impact of the Reinvestment and Reform Initiative on Capital Investment

8. The Reinvestment and Reform Initiative (RRI) was announced by the First Minister and Deputy First Minister in May 2002. It provides for a package which includes:

- an extra £200m[3] for immediate use, including £125m as a result of new borrowing arrangements with HM Treasury which would be re-payable from existing regional rate income, and £75m[4] from the Executive's own resources;
- the transfer of a number of security bases for the use of the Northern Ireland Executive; and
- the formation of the Strategic Investment Board (SIB)[5].

The announcement also gave details of a new borrowing powers for the Executive, effective from 2004-05, which could be used to accelerate the replacement and upgrading of Northern Ireland's infrastructure.

The Strategic Investment Programme

9. The £2.0 bn Strategic Investment Programme (SIP) was launched in December 2002 as the next phase of RRI. At its launch it was confirmed that finance for SIP projects would be provided from the Northern Ireland Departmental Expenditure Limits[6], low cost borrowing (as introduced under RRI) and investment from the private sector in PFI schemes. Further details of the programme were announced in February 2003:

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[3] Subsequently increased to £270m in July 2002.

[4] Subsequently increased to £145m in July 2002.

[5] Established by the Strategic Investment and Regeneration of Sites (NI) Order 2003, SIB's remit is to ensure that the Reinvestment and Reform Initiative is planned and delivered in a way that makes the most of all the means and resources available. SIB will also work in partnership with bodies carrying out major investment projects. It is empowered to advise the Executive and public bodies. Legislation places a duty on these bodies to have regard to its advice.

6. Applies to school Projects which had already been announced.

- for Category 1 projects, value £800 million, covering health, emergency services, water and sewerage, transport and roads, SIB would advise on how best to proceed i.e. by conventional procurement or by public private partnership. The underlying assumption was that these projects could be fully covered within a five-year financial horizon;
- Category 2 projects, value £785 million, covering libraries, schools infrastructure, hospitals, community health services, accommodation projects, waste water treatment works, roads and a pilot rapid transit scheme for greater Belfast, would proceed by Public Private Partnerships for which provisions for the service payments would be required; and
- Category 3 projects, which were already well advanced, value £550 million, would proceed by conventional procurement. These were primarily in the education field but also included water and sewerage, transport and roads and actions to alleviate fuel poverty and provide special accommodation to alleviate homelessness.

10. For the period up to and including 2003-04, finance for the schemes will be provided for within departmental expenditure limits. Commencing in 2004-05, it is intended that the rating of vacant property and the phased introduction of industrial de-rating will contribute to the additional funding required for SIP Projects up to 2005-06, the final year of the current three-year spending plan. Provision for 2006-07 and 2007-08 will be considered in future budget rounds.

Reporting Requirements

11. It is evident that PFI activity will increase significantly under SIP. This in turn will increase the proportion of ongoing resource budgets being committed to meet service payments. The effect of this, in certain circumstances, can be reduced flexibility as regards future expenditure.

12. Due to the growing commitments made by departments in GB, HM Treasury issued Policy Statement No. 5, Provision of Information to Parliament. This requires HM Treasury to report to Parliament on a biannual basis, providing, at departmental level, the Estimated Capital Spending by the Private Sector, Estimated Payments by Departments on signed deals and advance warning of significant forthcoming PFI commitments. The Statement was formally adopted in Northern Ireland by the Department of Finance and Personnel (DFP) in 2000 and departments advised through Dear Accounting Officer letter (DFP) 4/00, 'Reporting PFI Contracts to Parliament."[7] The letter, in addition to requiring departments to provide information for onward transmission to HM Treasury for inclusion in its biannual reports to Parliament, also made clear that similar reports would be made by DFP to the Northern Ireland Assembly.

7. Dear Accounting Officer letters supplement guidance contained in the Northern Ireland Government Accounting Manual.

Reporting to Date

13. Since the formal adoption of Policy Statement No.5, we found that DFP has, as required, reported to Treasury via the Office of Government Commerce (OGC). However, no similar reports had been made to the Northern Ireland Assembly. During the period of the Northern Ireland Assembly, up to its dissolution in October 2002, four returns were made to OGC. DFP told us that, while the Assembly's Finance and Personnel Committee had commissioned a separate report on PFI in 2001 and had discussed it, formal procedures for reporting PFI cases to the Assembly had not been established prior to dissolution.

14. As part of our familiarisation with the process, we reviewed the November 2002 return made to OGC, reconciling the information provided back to individual project returns from departments. This highlighted an understatement in the return to OGC of some £47 million. This was rectified in the subsequent return made in March 2003 (Figure1); Appendix 1 provides the departmental analysis. Details of Departmental Estimates of Capital Spending by the Private Sector, March 2003 (Signed Deals) is provided at Appendix 2.

Figure 1 - Estimated Departmental Payments Under PFI Contracts at March 2003 (Signed Deals)

	£m		£m
2002-03	59.9	2015-16	21.7
2003-04	63.9	2016-17	17.5
2004-05	59.5	2017-18	18.5
2005-06	36.6	2018-19	15.6
2006-07	36.5	2019-20	15.7
2007-08	34.4	2020-21	15.8
2008-09	29.1	2021-22	17.0
2009-10	28.2	2022-23	17.0
2010-11	27.4	2023-24	17.1
2011-12	26.1	2024-25	14.5
2012-13	23.0	2025-26	12.5
2013-14	23.0	2026-27	10.5
2014-15	22.2	2027-28	2.5
Total			**665.7**

Source: Department of Finance and Personnel
Note: Figure 1 shows forecast estimated payments for services flowing from new private investment over the next 25 years. Actual expenditure will depend on the details of the payment mechanism for each project. Variances may occur due to changes in the service requirements agreed during the course of the contracts. They may also vary as a result of the early termination of the contract or through the failure of the supplier to meet required performance targets.

15. Since April 2003, responsibility for the collation, maintenance, production and provision of PFI statistics, has transferred from DFP to the Public Private Investment Unit (PPIU) within the Office of the First Minister and Deputy First Minister (OFMDFM). PPIU, in addition to developing relevant policy and collating information on PPP/PFI in Northern Ireland, has responsibility for overseeing the operation of the Strategic Investment Board. It also works in close conjunction with the Central Finance Group of DFP and carries certain responsibilities on its behalf, though reporting to Parliament/Assembly on PFI will be formally channelled through DFP.

16. Payments under PFI unitary charges currently make up a very small proportion, less than one per cent, of Northern Ireland's total annual Departmental Expenditure Limit of £6,526 million for 2002-03. However, the planned increased use of PFI in delivering the strategic investment programme will see a marked increase in commitments. DFP recognises that the cost of service payments needs to be kept under review and is likely to represent a major cost from 2006-07 onwards. It is therefore important, in our view, that the financial information provided to Parliament/Assembly is complete and accurate. In this respect, in addition to the information that is currently provided, we recommend that budget papers and subsequent request for resources presented to the Assembly should show, for each department, the element of expenditure that is already committed to meeting PFI service payments.

17. We have also noted HM Treasury's commitment[8] to increase transparency in monitoring and reporting on the progress of the PFI investment programme in England. In particular, its plans to build on the information currently provided by publishing, on an annual basis, a comprehensive statement on the progress of the PFI programme. This will include:

- a complete record of transactions committed to in the previous year;
- a record of projects that have been completed in the year in question and their performance against expectations; and
- a statement on potential future transactions by sector.

18. As PFI policy is devolved in Scotland, Wales and Northern Ireland, this commitment relates to England only. However, given the significance of the potential flow of PFI projects from the Strategic Investment Programme, we would encourage the adoption of a similar approach in Northern Ireland.

8 HM Treasury paper "PFI: Meeting the Investment Challenge", published July 2003.

Appendix 1

Estimated Payments Under PFI Contracts - March 2003

	DEL £m	DCAL £m	DFP £m	DOE £m	DE £m	DRD £m	DSD £m	DHSSPS £m	Total £m
2002-03	10.0	6.6	3.7	4.1	25.0	2.5	2.2	5.8	59.9
2003-04	10.0	3.6	3.6	6.3	27.0	2.5	5.1	5.8	63.9
2004-05	10.0	3.1	3.5	4.9	27.0	2.5	2.7	5.8	59.5
2005-06	10.0	3.1	3.4	3.0	6.0	2.6	2.7	5.8	36.6
2006-07	10.0	3.2	3.4	3.0	6.0	2.7	2.6	5.6	36.5
2007-08	10.0	3.3	3.3	3.0	6.0	2.3	0.9	5.6	34.4
2008-09	6.0	3.3	3.3	3.0	6.0	2.4	0.9	4.2	29.1
2009-10	6.0	3.4	3.3	3.0	5.0	2.4	0.9	4.2	28.2
2010-11	6.0	3.5	3.3	3.0	4.0	2.5	0.9	4.2	27.4
2011-12	6.0	3.3	3.1	3.0	4.0	2.5	0	4.2	26.1
2012-13	6.0	0	3.2	3.0	4.0	2.6	0	4.2	23.0
2013-14	6.0	0	3.2	3.0	4.0	2.6	0	4.2	23.0
2014-15	6.0	0	3.3	3.0	4.0	2.8	0	3.1	22.2
2015-16	6.0	0	3.4	3.0	4.0	2.8	0	2.5	21.7
2016-17	6.0	0	0	3.0	4.0	2.0	0	2.5	17.5
2017-18	6.0	0	0	3.0	4.0	3.0	0	2.5	18.5
2018-19	6.0	0	0	0	4.0	3.1	0	2.5	15.6
2019-20	6.0	0	0	0	4.0	3.2	0	2.5	15.7
2020-21	6.0	0	0	0	4.0	3.3	0	2.5	15.8
2021-22	8.0	0	0	0	4.0	2.5	0	2.5	17.0
2022-23	8.0	0	0	0	4.0	2.5	0	2.5	17.0
2023-24	8.0	0	0	0	4.0	2.6	0	2.5	17.1
2024-25	8.0	0	0	0	4.0	0	0	2.5	14.5
2025-26	5.0	0	0	0	5.0	0	0	2.5	12.5
2026-27	5.0	0	0	0	3.0	0	0	2.5	10.5
2027-28	0	0	0	0	0	0	0	2.5	2.5
Total	**180.0**	**36.4**	**47.0**	**54.3**	**176.0**	**57.9**	**18.9**	**95.2**	**665.7**

Source: Department of Finance and Personnel

Appendix 2

Departmental Estimate of Capital Spending by the Private Sector March 2003 (Signed Deals)

Department	2002-03 £m	2003-04 £m	2004-05 £m
DEL	4.0	-	-
DFP	1.4	1.3	2.2
DE	52.0	6	-
DOE	7.3	5.6	0.5
DSD	-	-	0.3
Total	**64.7**	**12.9**	**3.0**

Source: Department of Finance and Personnel

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