



WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU

Wales Audit Office / Swyddfa Archwilio Cymru

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Mr Darren Millar AM
Chair, Public Accounts Committee
National Assembly for Wales
Cardiff Bay
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Dear Darren

**PAC INQUIRY INTO THE GENERAL PRINCIPLES OF THE PUBLIC AUDIT (WALES) BILL:
ESTIMATE OF COST**

Further to my letter of 9 October 2012, please find enclosed a supplementary note regarding the financial implications of the Bill as requested by the Committee at its session on 24 September 2012.

I should emphasise that my estimates are based on trying to work out the practical implications of the Bill as it stands. As I have not had sight of the Welsh Government's instructions on the drafting of the Bill, I have not been in a position to allow for the Welsh Government's intended effect of the Bill and so do not have all the information that the Welsh Government may have taken into account in producing its estimates. The Committee may therefore wish to consider whether it would be helpful to probe the Welsh Government further on its estimates, particularly regarding the detail of the assumptions it has made.

I should also mention that I have not included in my note the potential loss of savings that may arise from changes to the data matching legislation brought about by the Bill. As mentioned in my submission of 5 September 2012, the last data matching exercise identified fraud and overpayments of some £6 million.

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FURTHER INFORMATION REGARDING THE AGW'S ESTIMATE OF THE FINANCIAL IMPLICATIONS OF THE BILL

1. In my submission to the Committee of 5 September 2012, I set out a range of estimates of the cost of the Bill. Even the lower end of that range is higher than the Government's estimate. In our oral evidence to the Committee on 24 September 2012, we set out the broad reasons for our higher estimates but also offered to provide a note so as to give more specific details. This note provides that further specific detail.
2. First, however, it is perhaps worth re-iterating that the underlying reason for the differences in estimate probably lies in the way that I have considered the Bill in some detail in the context of our operations and sought to identify the financial implications of its practical implementation. In relation to that, I should also mention that differences were perhaps inevitable because the Welsh Government has not requested any comment on its cost estimates, and, as far as I can tell, has not asked for any information on such matters as the extent of work likely to be needed to produce a new, more extensive code of audit practice or in revising technical and HR policies.
3. As with the summary of cost estimates that I supplied in my submission of 5 September 2012, I will distinguish between one-off set up cost items and ongoing recurring costs of the arrangements that would be put in place by the Bill. For ease of reference, I have reproduced the summary table of costs from my 5 September submission, with the addition of references to the paragraphs below.

SUMMARY OF COST ESTIMATES

ONE-OFF ITEMS

Item	Lower Estimated Amount £000	Upper Estimated Amount £000	Para Ref
Cost of legislative process (WAO only)	30	40	6
Implementation	150	250	4, 5
Disputes	0	60	7
Total	180	350	

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RECURRING ITEMS

Item	Lower Estimated Amount £000	Upper Estimated Amount £000	Para Ref
Board members' fees, expenses and NI	155	185	8
Co-opted members fees, expenses and NI	5	15	9
Board secretariat	40	70	10
Travel and subsistence taxation	0	380	11
Total	200	650	

ONE-OFF SET UP COSTS

4. I have identified that the largest likely additional expense is the cost of implementation in terms staff time needed for the following items:
- i. producing a new **code of audit practice**, which, as the Bill requires this to be more detailed and extensive in coverage, is not simply a matter of updating the existing code of audit practice (35 days drafting @ £400 a day plus 10 to 18 days review and redrafting @ £600 a day = £20,000 to £25,000). Following on from this, and in order to reflect certain other features of the Bill, there is also a need to review and revise the organisation's **technical policies** and **delivery manuals**, such as sections that concern how management arrangements work to ensure audit quality (40 items with each taking on average 2 days @ £400 a day = £32,000);
 - ii. producing **new schemes of delegation** for approval by the Board. Depending on the extent of change required by the Board, I estimate the cost to lie between £5,000 and £25,000 (on the basis of £400 a day for drafting and £600 a day for senior staff review). There will also be a need to create new **standing orders** and **operating guidance**, and revise existing business processes to support the new board (20 days @ £400 a day and 5 days @ £600 a day = £11,000 + legal checks of £2,000 = £13,000—again if the board wishes to revise the standing orders and guidance extensively, or experiment with various versions, this could be much more, eg £50,000);

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- iii. **changes in employee roles** following the new schemes of delegation. At the very least some job descriptions will need to be revised to reflect changed responsibilities (say 3 days of HR time @ £350 a day = £1,050), but if the new schemes of delegation lead to significant changes in roles, competitions along with redeployments and possibly redundancies may be necessary. For example, if the new schemes of delegation led to more middle-management staff being directly responsible for matters (ie a de-layering), then promotion/recruitment competitions would need to be held in respect of the posts with enhanced responsibilities, while senior staff with reduced responsibility would need to be subject to redeployment or redundancy procedures. If such a development involved four enhanced middle management posts and the deletion of two senior management posts, I estimate the overall cost in terms of competitions and redeployments would be in the region of £36,000 (£6,000 per post). For simplicity, I have assumed that any redundancies would be cost neutral, ie the cost of paying higher remuneration for the enhanced responsibilities would be matched by the savings arising from redeployment or redundancy. In other words, the cost identified is purely the cost of change. Clearly, the figure could be even higher if the new schemes of delegation led to more extensive employee role changes or if the changes triggered the redundancy entitlements of senior staff with extensive service. As redundancy entitlements vary considerably in accordance with personal circumstances, such as length of service, it is not appropriate to set out estimates for the costs of such entitlements;
- iv. ensuring that employment terms are “broadly in line” with those of the Welsh Government. This will require review of **employee contracts**, **HR policies** and other HR materials alongside their Welsh Government equivalents, and where necessary revision of the relevant items. Such revisions will require liaison or consultation with the trades unions. While this will be an ongoing task, it will be most extensive on initial implementation. There will also need to be revisions of HR materials, such as sections of the staff handbook, disciplinary policy and grievance policy, in order to set out the management structure and the role of non-executive members (altogether, 7 major items such as T&S policy at 8 days @ £400 and 2 days @ £600 each for initial review and comparison, revision drafting, trade union liaison and board presentation and approval, plus 25 items at 2 days each @ £400 a day = £50,800 + legal advice @ £10,000 in total = £60,000);
- v. setting a **Strategic Equality Plan for the WAO**, including engagement with persons representing interests of persons with protected characteristics, and revising the AGW’s SEP to take account of loss of functions (30 days @ £400 a day and 5 days @ £600 a day = £15,000). It should be noted that simply taking portions of the AGW’s Strategic Equality Plan and designating them as the WAO’s would not meet the

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requirements of the Equality Act 2010 (Statutory Duties) (Wales) Regulations 2011, as in setting equality objectives and drafting a Plan, a person covered by the regulations is required to involve persons representing interests of persons with protected characteristics;

- vi. producing a **publication scheme for the WAO** in accordance with the Information Commissioner's requirements and revising the AGW's publication scheme to take account of loss of functions (10 days @ £400 a day and 2 days @ £600 a day = £5,200). As material such as the new operating guidance in relation to the WAO Board would need to be reflected in the WAO's publication scheme, a simple division of the AGW's scheme would not be an option that would meet the Information Commissioner's requirements.
5. All of these tasks require substantial technical expertise. Many of the items need to be reviewed and revised by qualified accountants and lawyers. The following table summarises the one-off implementation costs identified in paragraph 4 above.

INDIVIDUAL ONE-OFF IMPLEMENTATION COSTS

Item	Lower estimate £000	Upper Estimate £000
New more extensive code of audit practice	20	25
Review and revision of technical guidance and manuals	32	32
Schemes of delegation	5	25
Standing orders and operating guidance	13	50
Changes in employee roles	1	36
Ensuring terms are broadly in line with Welsh Government	60	60
WAO Strategic Equality Plan and revision of AGW's	15	15
WAO publication scheme and revision of AGW's	5	5
Total	151	248

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6. As shown in Annex B of my submission to the Committee of 5 September 2012, I have also recognised that responding to the legislative process itself is a call on public resources. Current WAO staff time and some external legal advice has been needed, and is likely to continue to be needed, to consider the Bill and its likely effects. For example, WAO staff have had to consider the likely effects of the transfer provisions and spend time on dealing with queries from staff concerned about the effect of the Bill. We estimate WAO staff time will be in the region of 60 to 90 days (@ £400 a day = £24,000 to 36,000) plus cost of external legal advice of some £5,000. We have not attempted to estimate the Welsh Government's costs of producing the Bill.
7. My submission to the Committee of 5 September 2012 also includes an upper estimated amount of £60,000 for disputes. This on the basis of three disputes each taking up 30 days of staff time and costing £8,000 in legal fees. Potential flash points include claims in the context of the Bill's requirement for terms to be broadly in line with those of the Welsh Government in respect of working hours, professional qualification allowances and redeployment and redundancy policy.

RECURRING COSTS

8. As mentioned in my submission, I think that the Welsh Government has underestimated the remuneration that good quality board members will require. There does not seem to be a body in the UK with the unusual requirement for non-executive members to take executive decisions without sharing those decisions with an adequate number of executive members, so there is no benchmark with which to identify the risk premium that good candidates are likely to require. But given that they will be undertaking a more than usually risky role, it may not be unreasonable for fees rates to be some 50 per cent higher. Nevertheless, for my lower estimate I have assumed that the Welsh Government fee is sufficient. In addition, however, the Welsh Government does not seem to have included any amount for National Insurance contributions (up to 13.8 per cent) and T&S for members (some £10,000 including PAYE settlement). Taken together, these are likely to increase the cost of payments to Board members by some 20 per cent, and I have applied that uplift to the fees.
9. It is good governance practice for bodies to have independent external members on their audit committees. In particular, this is required by HM Treasury's Audit Committee Handbook where there are insufficient non-executive Board members. The Board is therefore also likely to need to co-opt two independent members for its audit committee. Co-opted members will require remuneration, and I estimate that this will amount to some £10,000 including National Insurance and travel and subsistence (ie some £4,000 each plus oncosts).

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10. The Welsh Government's estimate of the cost of support for the board of a corporate body (£29,000) is also likely to be too low. Such a board will need not only a secretariat providing administrative support, but it is also likely to require a substantial level of ongoing expert legal and technical advice on the proper exercise of its functions. I estimate that the secretariat employment costs will be in the region of £60,000, including National Insurance etc (this is based on the Board secretary being recruited or transferred in on a salary at the Welsh Government's Executive Band 2, ie £44,000 plus pension contributions of 21 per cent and NI of 13 per cent). It should be noted that in 2010, the NAO recruited a Head of Governance to support its Board, with an advertised starting salary of £62,000.
11. I am hopeful that HMRC will follow the example of its treatment of NAO staff and will not require staff T&S to be taxed on account of them being employed by one body yet working for another. I have therefore given a lower estimated amount of £ zero. But given the salutary experience that we have had in inheriting uncertainties about VAT, I think it is important to highlight the risk of the WAO having to settle employee's tax and National Insurance liabilities so as to ensure employees are not out of pocket. This would be necessary for fairness, but it also appears to be necessary in order to ensure that working conditions are in line with those of the staff of the Welsh Government. I have estimated potential additional liability at £380,000 based on current T&S payments of just over £400,000. For £400,000 to be reimbursed so that employees are not out of pocket, the WAO would need to pay £690,000, of which some £290,000 would need to be paid to HMRC in income tax and employee's National Insurance—the average combined WAO income tax and employee NI rate is 42 per cent. On top of this additional £290,000, the WAO would need to pay employer's NI on the whole payment, ie some 13 per cent on £690,000 = £90,000. Altogether, the additional cost would be £380,000 (£290,000 + £90,000).

THE TIME FRAME FOR ADDITIONAL COSTS

12. I understand from the explanatory memorandum that there is an intention to make commencement arrangements so that there is time to undertake preparatory work in advance of April 2014, such as running the WAO Board in shadow form. While it is difficult to predict what preparatory tasks the WAO Board will want to undertake, it seems likely and sensible that some implementation work, such as considering draft standing orders, will be done before April 2014. The expense of such work would fall in the financial year 2013-14. Similarly, it seems likely that some ongoing costs, such as members' fees, will fall in that financial year. Altogether, despite the considerable level of uncertainty, I consider that it is prudent to expect that some £250,000 of cost attributable to the Bill will be incurred in 2013-14 and a further £350,000 will be incurred in 2014-15.