Annual report and accounts 2009/10

audit commission

Audit Commission

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Report and accounts of The Audit Commission for Local Authorities and the National Health Service in England, showing the Statement of comprehensive income for the year ended 31 March 2010 and Statement of financial position as at 31 March 2010, together with the Report of the Comptroller and Auditor General thereon.

Presented to Parliament pursuant to the Audit Commission Act 1998, Schedule 1, clause 14 (2)

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Foreword

The Commission's purpose is to promote maximum value for the public money spent by councils, police, fire and rescue authorities and NHS trusts. To fulfil our statutory duty of securing the audit of local public bodies – our core business – we appoint accountancy firms and auditors from our in-house practice. This mixed economy gives us the professional benefits of flexibility and diversity and ensures competitive pressure on both costs and quality.

We continuously review the share of work between private firms and our auditors, and are currently testing the market for audits in Cornwall and Cumbria.

Parliament approved updates to our Audit Codes that underpin public audit of councils and NHS trusts during 2009/10. Accounting requirements are changing and we have supported finance directors during the transition to International Financial Reporting Standards (IFRS), including financial support, by absorbing costs and returning £6.6 million from our reserves to help audited bodies.

As well as our audit duties, we have a statutory duty to combat fraud. In the National Fraud Initiative, we match data sets to identify anomalies that might point to fraud, error and overpayment of council tax, housing and other benefits. Our UK-wide antifraud programme helped trace £215 million in fraud, overpayments and error in 2008/09, against £140 million found in the previous report (2006/07). The public auditors in the devolved administrations have joined the NFI. We hope that our next round will include other government departments and the National Audit Office.

To spend well, those who spend and those who fund need the right information. We assure the quality of data used, for example, by NHS trust boards. During the past year we led the debate about how public bodies should share information, while guaranteeing its quality and comparability. The Oneplace website offered members of the public an independent, objective and evidence-rich perspective on public services where they live.

At the end of March 2010, Steve Bundred left after six and a half years' service as Chief Executive. We thank him for his leadership of the Commission. The Board appointed Eugene Sullivan, Managing Director for Finance and Corporate Services, as Acting Chief Executive from 1 April until the Commission appoints a permanent replacement for Steve Bundred.

The Commission, along with other public bodies, is adapting to the priorities of the new government. Public spending is under rigorous review and we are restructuring, planning for continuous improvement and cutting costs. We will publish details of supplier payments online. Here are highlights of the year past and pointers to what lies ahead.

Michael O'Higgins and Eugene Sullivan

Annual Report

Outline of the year

Our core business is to appoint auditors to give their professional opinion on the financial accounts presented by councils, police, fire and rescue authorities and NHS trusts. Audit complements and underpins democracy. We assure the reliability of financial information available to elected members and to the electorate that votes for them. We also consider timeliness – during 2009/10, we pointed out how indefensibly late some councils had been in presenting their accounts.

To audit councils, NHS trusts and other local spending bodies, the Commission appoints either a qualified individual employed by the Commission or one of the audit firms with which we have contracted: Deloitte, KPMG, PKF, PricewaterhouseCoopers and Grant Thornton. Our own in-house practice is the fifth largest audit practice in the UK.

We welcomed a second annual inspection of our auditors' work by the independent Audit Inspection Unit. Such external assessment supplements our own quality review and assures councils and other bodies to which we appoint auditors. We negotiated to extend the duration of existing contracts with the firms in return for lower prices.

We appoint to 900 principal councils, police, fire and rescue authorities and NHS trusts in England and to smaller organisations such as parish councils and drainage boards. During the year, we consulted on the five-yearly update of the audit Codes of Practice; the new Codes secured parliamentary approval in March 2010.

Auditors did not have to qualify any NHS trust accounts on grounds of truth or fairness. They worked to a speedier timetable than in previous years and, as a result, the Department of Health was able to lay its consolidated accounts before parliament before the July 2009 recess – a notable achievement.

In December 2009, we published an open letter to the then Communities Secretary, drawing attention to four councils that had still not published audited accounts eight months after the end of the financial year. We asked the government to amend statutory requirements for the approval of the accounts to allow timelier financial reporting.

The Commission supported the continuing transition of public bodies to International Financial Reporting Standards, which create new rules for how bodies treat transactions and value assets, and on disclosure. To help pay for audited bodies' extra work arising from IFRS, we agreed to return £6.6 million in fees to them. Auditors reported concerns but judged the NHS to be broadly on track to make the transition. NHS trusts' 2009/10 accounts will be the first audited under the new rules. We said that councils would need to step up the pace to meet IFRS, which applies to local authorities, police and fire and rescue authorities for the first time in 2010/11.

Outside the normal cycle of accounting, auditors may have to alert the public to problems. During 2009/10, for example, the appointed auditors of Cheltenham Borough Council issued a public interest report drawing attention to the way councillors had claimed damages against a former managing director.

In our value for money work, we rated how well local bodies commissioned services, took decisions and handled natural resources, assets and people. Auditors gave councils scores on how well they performed on their use of resources, as well as evaluating the value for money performance of primary care trusts (PCTs).

We recognised the financial pressures mounting in the public sector and advised public bodies of the need to prepare early. We supported this with timely studies that the local government sector welcomed. The series of reports included *Crunch Time* and *When it Comes to the Crunch*.

Comparison is the classic Commission way of discovering opportunities to learn and improve. We noted how some councils were anticipating the financial freeze and adjusting now to preserve their most valued services in the years ahead. For practical use, we offered PCTs an interactive tool to check their value for money profiles. To assess the financial performance of councils, we devised an online tool showing comparative financial ratios.

Under the National Fraud Initiative (NFI), we bring together public data sets to match entries, which flag anomalies for investigation. Councils and other bodies used the matches to detect fraud, error and overpayment of, for example, housing benefit, council tax discount, and applications for blue badges and travel passes. We froze NFI participation fees for the period 2010/12. Since 1996, the NFI has saved an estimated £664 million. During the year, the government offered to pay for larger housing associations to take part in a special NFI exercise to identify potential tenancy fraud. Our report on fraud, *Protecting the Public Purse*, said that council taxpayers could be losing almost £2 million a week to fraudsters claiming the 25 per cent single-person discount on their council tax.

Good data is crucial in getting better value for money. The Commission reviewed data assurance in the NHS, helping trusts to ensure the integrity of clinical performance assessment. A second annual review of Payment by Results (PbR) in the NHS found that clinical coding for diagnoses and procedures had improved. Trust performance varied, however: coding was too often wrong and errors blighted the accuracy of payments for treatment. The Commission's 'National Benchmarker' was joint overall winner in the Excellence in Healthcare Information Management awards in October 2009.

Specific work and studies

Six independent public service inspectorates pioneered joint, cross-cutting judgements of the public services provided to residents in local areas, assessed against local priorities and England-wide targets. Commission specialists led these Comprehensive Area Assessments. We conducted separate organisational assessments of councils and fire and rescue authorities. These assessments, and those for children's services, adult social care and the police, contributed to the overall assessment of public services in each local area.

We published the assessments in plain, accessible language on the Oneplace website http://oneplace.direct.gov.uk. The aim was to equip residents to hold to account councillors and others commissioning and providing services. Many people seized the chance and by mid-March unique visitors to the website exceeded 200,000. Councils welcomed the principle of assessing the public services provided in a local area and forming one judgement of how well the public bodies served their communities.

An independent evaluation of CAA found that inspectorates should work more closely to avoid duplicating or repeating calls on the time of councillors and managers. In May 2010, the coalition government announced the abolition of CAA and the Commission is moving quickly in response to this.

In response to serious and continuing problems, we undertook a corporate governance inspection of the Metropolitan Borough of Doncaster and referred the case to the Communities Secretary for action. The Secretary of State responded to this report with a package of measures for improvement, including a new Chief Executive, and a team of Commissioners to ensure the Borough gets the experienced leadership and support that it needs.

We published a study tracking how the recession and credit crunch were affecting council revenues and spending, providing the government with timely appraisals of their financial condition. Another study found little evidence that increased spending since 2000 had improved the health of children under five. At the other end of the age range, we found councils struggling to cope with the financial effects of ageing: they did not know enough about the cost implications for their areas of demographic change.

With HM Inspectors of Constabulary, the Commission assessed police authorities. The joint verdict on, for example, the Metropolitan Police Authority was two stars, based on a finding of 'adequate' performance. Another joint report showed that only a third of a sample of police authorities set long-term strategic plans for themselves or their police forces.

The Commission's Corporate Governance Framework requires a review of the Board's effectiveness at least every two years. In April 2009, the Board received an independent report on the latest review. The reviewers found a 'high performing Board that demonstrates many areas of good practice'. The report noted the Board provided helpful and robust challenge in holding the organisation to account; it addressed concerns quickly and made decisions effectively. The review also noted the Corporate Governance Framework represented best practice.

Looking forward

The new government formed after the May 2010 election promised to bring UK national accounts back towards balance principally by cutting spending. During 2009/10, the Commission had urged service providers to look ahead and plan. The coalition government is setting out its plans to cut the UK deficit within the next few years, and they include cuts to budgeted spending in 2010/11. The Commission looks forward to collaboration with the Efficiency Reform Group in the Cabinet Office and the Local Productivity Group set up by Communities and Local Government. We will publish online all external transactions worth £500 or more, in line with the government's wish to publish details of spending and anticipating a similar proposal for local authorities to run from 2011. The Commission sees a business and an accountability case for maximum transparency in all it does.

The Commission is reviewing its own structures as it seeks to cut overheads and administrative costs.

The new government is also setting out its plans to decentralise power and strengthen local accountability. The Commission is in talks with the Local Government Association and the other inspectorates about a new approach to inspection and public information. Our aim is to cuts costs, lessen the burden of inspection and improve productivity, support self-improvement and provide early warning of corporate or service failure.

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Commissioners during the period of review

All comments relating to the Commissioners reflect their activities during the year ended 31 March 2010.

Michael O'Higgins Chairman

Michael has been Chairman of the Audit Commission since October 2006, and became Chairman of Alexander Mann Solutions, the recruitment process outsourcing company, in August 2009. He is also a Non-Executive Director of HM Treasury and Chair of the Treasury Group Audit Committee. Michael is Chair of the charity Centrepoint and is a Trustee of the National Centre for Social Research (NatCen). He is a Visiting Professor of Economics at the University of Bath and a Non-Executive Director of Investec Structured Products Calculus VCT plc.

Previously, Michael was a Managing Partner with PA Consulting, leading its government and IT consulting groups, latterly as a director on its International Board. He was a Partner at Price Waterhouse and worked at the Organisation for Economic Co-operation and Development in Paris. He held academic posts at the University of Bath, the London School of Economics, Harvard University and the Australian National University.

Bharat Shah Deputy Chairman

Bharat has been providing business consultancy and executive mentoring since 2002. He is the Non-Executive Chairman of the Sure Group, a private equity-backed business. He has been a Non-Executive Director of the West Bromwich Building Society since July 2004 and from January 2010 he has been Non-Executive Director of the Places for People Group. He trained as a certified accountant and worked for Eastman Kodak for 27 years where he rose from 'shop floor' to become the Chief Executive of EAMER, Kodak Consumer Imaging and Vice-President, Eastman Kodak. He was also a Vice-President of Singer, responsible for Europe, Africa, Middle East and Asia. He was the Non-Executive Chairman of Picdar Group, a 3i-backed digital asset management company.

Steve Bundred Chief Executive
Steve was Chief Executive of the Commission from September 2003 until 31 March 2010. Before joining the Commission, he was Executive Director of the Improvement and Development Agency for local government. Before that he worked for the London Borough of Camden, joining as Director of Finance in 1992 and becoming Chief Executive in 1995. Steve has worked for the London Boroughs of Lewisham and Hackney councils and Birkbeck College. He was Deputy Pro Chancellor of City University, a Board member of the Higher Education Funding Council and Chair of the Higher Education Regulation Review Group. As Chief Executive, Steve was also part of the management team.

Lord Adebowale, CBE
Victor is Chief Executive of Turning Point, the social care charity working with people with complex needs involving substance misuse, mental health problems and learning disabilities. He began his career in local authority estate management before joining the housing association movement. He worked with Patchwork Community Housing Association and the Ujima Housing Association. He was Director of the Alcohol Recovery Project and Chief Executive of youth homelessness charity Centrepoint. In 2000, Victor was awarded a CBE for service to the unemployed and homeless young people and in 2001 became a cross-bench member of the House of Lords.

Councillor Merrick Cockell
Merrick was elected Chairman of London Councils in 2006. He has been Leader of the Royal Borough of Kensington and Chelsea since 2000, after having been Chairman of the Council's Education and Libraries Committee and Conservative Party Chief Whip. He founded and ran a business specialising in trade with China and Africa for 23 years until 2006. He was Chairman of the Portobello Business Centre, which provides training and professional advice to start-up and small businesses, and the Chelsea Theatre, a theatre and arts charity. Merrick was awarded a knighthood in the Queen's Birthday Honours in June 2010 for services to local government.

Jim Coulter

Jim was Chief Executive of the National Housing Federation for 17 years until retiring in June 2005 and before that, he had a similar role at Leeds Federated Housing Association. He is Chair of Bridging Newcastle Gateshead, the housing market renewal pathfinder, and a member of the North-East Regional Housing Board. He is also a Board member of the Tenant Services Authority. He has been a Board member of Shelter and Chair of Homeless Network and has served on Communities and Local Government project boards.

Dr Jennifer Dixon

Jennifer is Director of the Nuffield Trust. She was Director of Health Policy at the King's Fund and among previous posts she was Policy Adviser to the Chief Executive of the NHS. She has a background in clinical medicine and holds a PhD in health services research.

Councillor Stephen Houghton, CBE

Stephen has been Leader of Barnsley Metropolitan Borough Council for 11 years and a member for 20. He is also Chair of the Barnsley Local Strategic Partnership, Chair of the Special Interest Group of Municipal Authorities (SIGOMA) and Chair of Barnsley Miller Partnership Ltd. He was awarded the CBE for services to local government in 2004.

Councillor Peter Jones

Peter is a retired investment banker. He has been Conservative Leader of East Sussex County Council since 2001. Among other roles, he is a member of Sussex Police Authority and Deputy Chairman of the South East England Development Agency. Peter's appointment ended on 30 April 2009.

Sir Thomas Legg, KCB QC
Tom was Permanent Secretary of the Lord Chancellor's Department (now the Ministry of Justice) from 1989 to 1998. He is Non-Executive Director of the Imperial College Healthcare NHS Trust and a consultant to the law firm Clifford Chance.

Dame Denise Platt
Denise is Chair of the independent advisory panel for the Local Innovation Awards Scheme. She was previously Chair of the Commission for Social Care Inspection. Among her voluntary sector roles Denise is Chair of the National AIDS Trust, a trustee of the National Society for the Prevention of Cruelty to Children (NSPCC) and a member of the National Executive Council of the Family Planning Association. She is a Governor of the University of Bedfordshire and a member of the Independent Review Board of the Cheshire Fire and Rescue Service. She is a member of the Committee on Standards in Public Life.

Brian Pomeroy, CBE
Brian was Senior Partner of Deloitte Consulting until 1999. He is Chairman of the Treasury's Financial Inclusion Taskforce, the Payments Council and the Gambling Commission. He is a member of the Financial Reporting Review Panel, Director and Deputy Chairman of QBE Insurance Europe Ltd, a trustee of the Money Advice Trust, a board member of The Social Market Foundation and Chair of The Photographers' Gallery. He was formerly Chair of the National Lottery Commission, Centrepoint and Homeless Link and an independent member of the Council of Lloyd's. Brian's appointment ended on 30 April 2009.

Dr Raj Rajagopal
Raj was Chief Executive of BOC Edwards and Executive Director of the BOC Group plc from 2000 to 2006. From 1981 to 2000 he held various positions in the BOC Group plc including Managing Director of Edwards High Vacuum. He is a Non-Executive Director of Bodycote plc, WS Atkins plc and Spirax Sarco Engineering plc, a member of the Prime Minister's Council of Science and Technology and a Fellow of the Royal Academy of Engineering. He is also Chairman of HHV Pumps, an adviser to Bristlecone Ltd and Director of Dr Rajagopal Associates. He is Chairman of University of Manchester Intellectual Property Ltd.

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Professor Peter C Smith
Peter is Professor of Health Policy at Imperial College, London and former Director of the Centre for Health Economics at the University of York, having worked at Cambridge University and in local government. He has held posts advising governments and international agencies. He has published widely on economic aspects of public services. Peter's appointment ended on 30 April 2009.

Sheila Drew Smith, OBE
Sheila is an independent management consultant on business development and related management and governance issues. She is a Board member of the Tenant Services Authority and of the London Thames Gateway Development Corporation. She was Executive Chair of Tower Hamlets Housing Action Trust until 2004/05 and was a Board member of the Housing Corporation from 2002 to 2008. She became a Non-Executive Director of the Infrastructure Planning Commission in March 2010 where she chairs its Audit Committee.

Jenny Watson
Jenny is Chair of the Electoral Commission, a role she has held since January 2009. She is also a Non-Executive Director of Waste and Resources Action Programme (WRAP). She is a trustee of the Charities Aid Foundation and Money Advice Trust. Her past roles include Chair of the Equal Opportunities Commission and she was a founding Partner of Global Partners and Associates.

Councillor Chris White
Chris was elected to Hertfordshire County Council representing Central St Albans in 1993. He was Leader of the Liberal Democrat Group from 1994 to 2003, resuming the leadership in 2005. He was Deputy Leader of the Council and has also been a member of the Hertfordshire Police Authority. From 1998 to 2008 Chris was Leader of the Liberal Democrats on the East of England Regional Assembly. He also chairs the Local Government Association Culture, Tourism and Sport Board. He was elected to St Albans City and District Council in 2008.

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Members' appointment dates

	Appointment start date	Appointment end date
Michael O'Higgins, Chairman	01/10/06	30/09/12
Lord Adebowale, CBE	01/09/07	31/08/10
Steve Bundred[1]	01/11/03	31/03/10
Councillor Sir Merrick Cockell	13/07/09	12/07/12
Jim Coulter	01/04/05	31/03/11
Dr Jennifer Dixon	01/11/03	30/10/10
Sheila Drew Smith, OBE	01/05/04	31/12/10
Councillor Stephen Houghton, CBE	02/05/06	30/04/12
Councillor Peter Jones	01/11/03	30/04/09
Sir Thomas Legg, KCB QC	01/04/05	31/03/11
Dame Denise Platt	01/09/07	31/08/10
Brian Pomeroy, CBE	01/05/03	30/04/09
Dr Raj Rajagopal	01/09/07	31/08/10
Bharat Shah	01/09/07	31/08/10
Professor Peter C Smith	01/11/03	30/04/09
Jenny Watson	01/09/07	31/08/10
Councillor Chris White	01/06/05	31/05/11

Note 1: This ex-officio appointment was coterminous with his appointment as Chief Executive.

Board member interests

The following disclosures relate to Commissioners who were in post at 31 March 2010 and relate to the year ending March 2010. The disclosures arise where a Commissioner has been in a position of influence resulting from being elected to, receiving remuneration from, or being appointed to any organisation:

- where the Commission appoints the auditor or inspects the body
- where there are specific statutory responsibilities to cooperate, for example, with the Healthcare Commission;
- that is a central government body; and
- that is a provider or receiver of significant services to or from the Commission.

Michael O'Higgins Chairman

- Chair, Centrepoint (Registered Social Landlord)
- Non-Executive Director, HM Treasury and Chair, Treasury Group Audit Committee

Bharat Shah Deputy Chairman

- Non-Executive Director, Places for People Group (Registered Social Landlord)

Steve Bundred Chief Executive (left the Audit Commission 31 March 2010)

- During the year his wife worked on contracts with government departments.

Lord Adebowale, CBE

- Chief Executive, Turning Point (Registered Social Landlord)

Councillor Sir Merrick Cockell

- Member, Royal Borough of Kensington and Chelsea

Jim Coulter

- Chair, Bridging Newcastle Gateshead
- Board member, Tenant Services Authority

Jennifer Dixon

- Director of the Nuffield Trust

Councillor Stephen Houghton, CBE

- Member, Barnsley Metropolitan Borough Council
- Member, Barnsley/Miller Partnership
- Fees from Improvement and Development Agency for peer member duties

Sir Thomas Legg, KCB QC

- Non-Executive Director, Imperial College Healthcare NHS Trust

Dame Denise Platt

- Member, Committee on Standards in Public Life
- Chair, independent advisory panel, Local Innovation Awards Scheme
- Independent Review board member, Cheshire Fire and Rescue Service

Dr Raj Rajagopal

- None

Sheila Drew Smith, OBE

- Board Member, Tenant Services Authority
- Board Member, London Thames Gateway Development Corporation
- Fees from government departments for Office of the Commissioner for Public Appointment duties
- Non-Executive Director, Infrastructure Planning Commission (from 1 March 2010)

Jenny Watson

- Chair, Electoral Commission

Councillor Chris White

- Member Hertfordshire County Council
- Member St Albans City & District Council
- Family member an employee of Ernst & Young

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Senior managers during the period of review

Steve Bundred Chief Executive
Steve left the Commission on 31 March 2010, however he was the Commission's chief officer throughout the year and held the statutory title of Controller of Audit. The Board has delegated authority for the day-to-day management of the Commission to the Chief Executive. The Chief Executive therefore has responsibility for the overall organisation, management and staffing, and for its procedures in financial and other matters including conduct and discipline. He discharges this responsibility through his management team who meet on a regular basis throughout the year.

The Audit Commission's management team during the year to 31 March 2010 was as follows:

Eugene Sullivan Managing Director, Finance and Corporate Services
Eugene rejoined the Commission on 2 June 2008. Before joining the Commission, Eugene was a Partner in RSM Robson Rhodes LLP (now merged with Grant Thornton LLP) in charge of public sector services. He previously worked for the Commission for five years in the 1980s. Eugene was appointed Acting Chief Executive of the Commission on 1 April 2010.

Gareth Davies Managing Director, Local Government, Housing and Community Safety
Gareth was previously the Commission's Regional Director for the North of England. His professional background is in public audit, including appointments as district auditor to major local authorities and NHS bodies. Gareth is also a trustee and Honorary Treasurer of Oxfam GB.

Tracey Dennison Managing Director, Human Resources
Tracey was previously Assistant Chief Executive (Personnel) at Camden Council. She has a Diploma in Public Administration from Warwick University and is a fellow of the Chartered Institute of Personnel and Development. Tracey is a trustee of the Employers Forum on Age and the Employers Forum on Belief.

Martin Evans Managing Director, Audit
Martin trained as an accountant in local government, before holding a series of technical roles in the accountancy profession. He was Policy and Technical Director at CIPFA, from where he joined the Commission in 1998.

Andy McKeon Managing Director, Health
Andy was the Director of Policy and Planning at the Department of Health. During his time at the Department he was also Head of Primary Care and played a central role in the development of a number of white papers. He is also a non-executive director of the National Institute for Health and Clinical Excellence, and a trustee of the Nuffield Trust.

David Walker Managing Director, Communications and Public Reporting
David was appointed Managing Director of Communications and Public Reporting at the Audit Commission in October 2008. He was previously editor of the Guardian's Public magazine, chief leader writer for The Independent and a regular presenter of BBC Radio Four's Analysis programme. David is a council member at the Economic & Social Research Council and a trustee of the Franco-British Council.

Peter Wilkinson, CBE Managing Director, Policy Research and Studies
Peter has been at the Audit Commission since 1990, and a director since 1995. He has held a variety of appointments covering the Commission's strategy, policy and corporate management, as well as responsibility for external work in the local government, health and police sectors.

Auditor details

This financial statement is audited by the Comptroller and Auditor General and he has not provided any other service to the Commission during the period. The audit fee is disclosed in Note 7.

The Accounting Officer confirms that:

- there is no relevant audit information of which the auditors are unaware;
- he has taken all the steps he ought to ensure that he is aware of all relevant audit information; and
- he has taken all the steps he ought to establish that the auditors are aware of the information.

Annual accounts

Financial review

Financial strategy

The Commission's Board set a financial strategy in March 2010 covering the three financial years from 2010/11 to 2012/13. The strategy reflected what we knew then about future government spending plans. It preserved financial resilience, yet enabled investment in strategic objectives and the return of surpluses to AIBs. The strategy included efficiency savings of 15 per cent but warned that more may be necessary.

The Board knew it would need to review its financial strategy following the general election when the new government's public service and spending plans became clearer. The coalition government has already stopped Comprehensive Area Assessment (CAA) and other activity will reduce. The Board now knows it must manage an immediate cut in income from grants and fees in 2010/11, with more to follow in future years.

The government announced its emergency budget on 22 June 2010 and there will be a Spending Review (SR) that will conclude in the autumn. The review will set budgets for 2011/12 to 2014/15. In common with other public sector bodies, the Commission will need to make real-term cuts in its administrative costs of about 25 per cent. It will also need to review its draft strategic and management plans and its financial strategy, to reflect the implications of these government policy statements.

Income

Total operating income for 2009/10 reduced to £213.1 million (2008/09: £215.7 million). Most of the Commission's income (86 per cent) came from fees charged to AIBs for audit and assessment (£182.7 million). Just 13 per cent came from grants received from government departments (£28.0 million). Other income (£2.4 million) includes interest and rent.

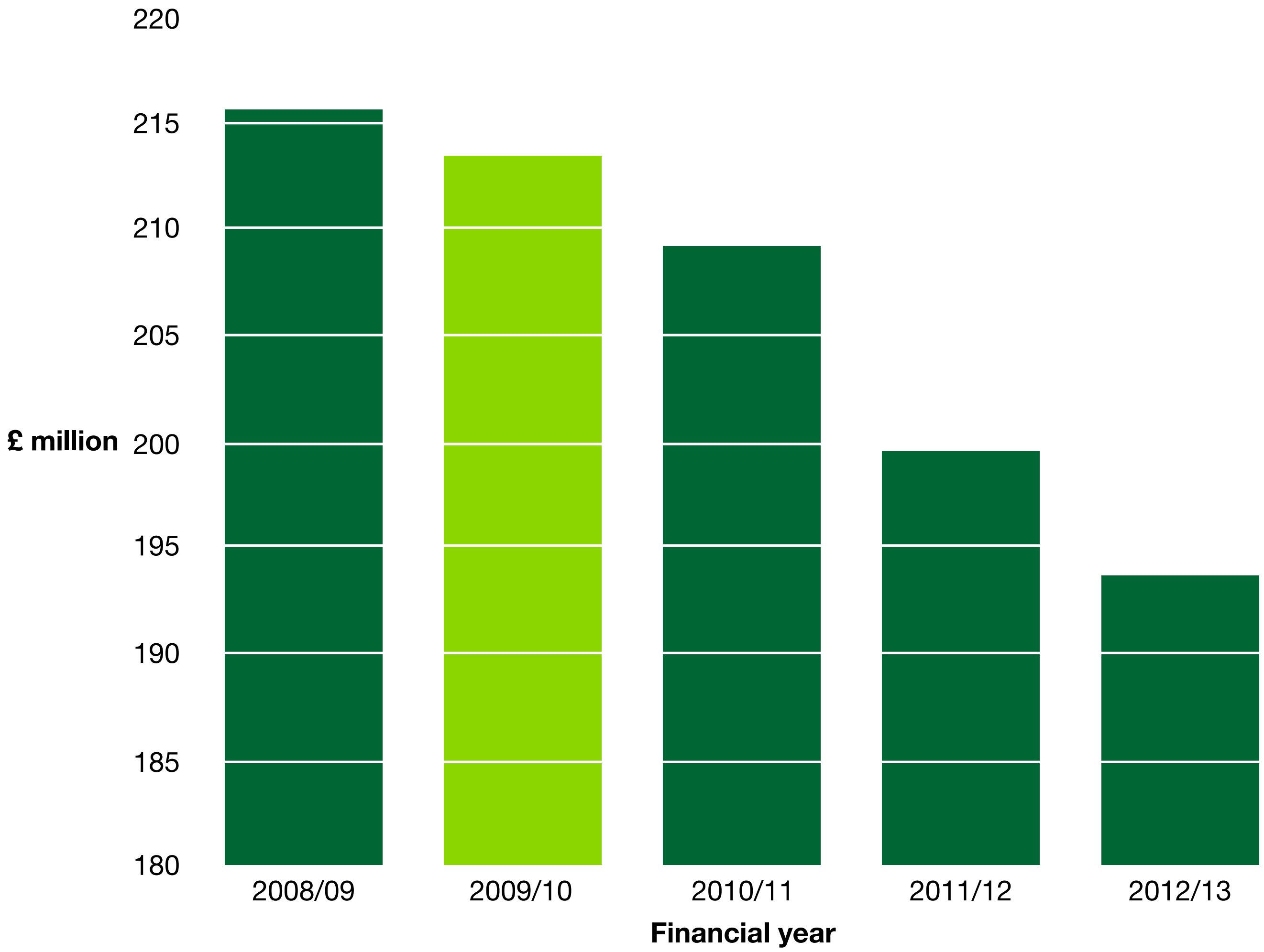
Introducing International Financial Reporting Standards (IFRS) has meant more work for the Commission and some AIBs in the last year. In recognition of this, the Commission passed back £1.5 million of fees to health and probation bodies. The Commission also passed back £5.1 million of fees to local government and police bodies.

Seventy per cent (£149.9 million) of the Commission's total operating income for 2009/10 came from the local government sector including police and fire and rescue authorities. The rest (£63.6 million) came from the health sector. Grants received from central government departments (the majority from Communities and Local Government) account for 18.7 per cent of the Commission's local government sector income.

Five private sector audit firms carry out 30 per cent of the Commission's audits. This work produces 23.5 per cent (£50.1 million) of the Commission's income. Having a mixed economy helps the Commission to ensure value for money and quality across all audits. The Commission renegotiated existing contracts with its main suppliers during 2009/10 to reduce costs in future years and started a procurement exercise for work in Cumbria and Cornwall. The Commission keeps the balance between internal and contracted delivery under review.

The medium-term financial plan, agreed before the demise of CAA, sets out the Commission's projections for the next three financial years. The Board had expected income to fall by £27.0 million over the next three years but now knows the reduction will be significantly higher. Chart 1 shows the projections before the announcement that CAA would stop. The Commission expects to lose some 50 per cent of planned income for CAA work in 2010/11 and more in future years.

Chart 1: **Total income (2008/09 – 2012/13) *before* CAA stopped in May 2010/11**



Costs

The Commission spends its income on the activities undertaken by its operational staff, the private accountancy firms it subcontracts work to and its corporate directorates. As income reduces, the Commission will necessarily reduce its costs.

The Commission's total costs were £220.3 million in 2009/10 (2008/09: £210.1 million). Increases in staff costs of £13.5 million were offset by cost reductions in other areas.

One of the main reasons for the increase in the salary bill for 2009/10 was the £5.3 million one-off cost of redundancies associated with the reduction in workload as AIB numbers fall and work programmes are cutback. Fifty-eight full-time equivalents (FTEs) took voluntary redundancy in 2009/10 and 18 FTEs were selected for compulsory redundancy. Thirty FTEs included in the year-end total of 1,985 FTEs left us at the end of March 2010. As the work programme decreases the Commission's bill for staff salaries will reduce.

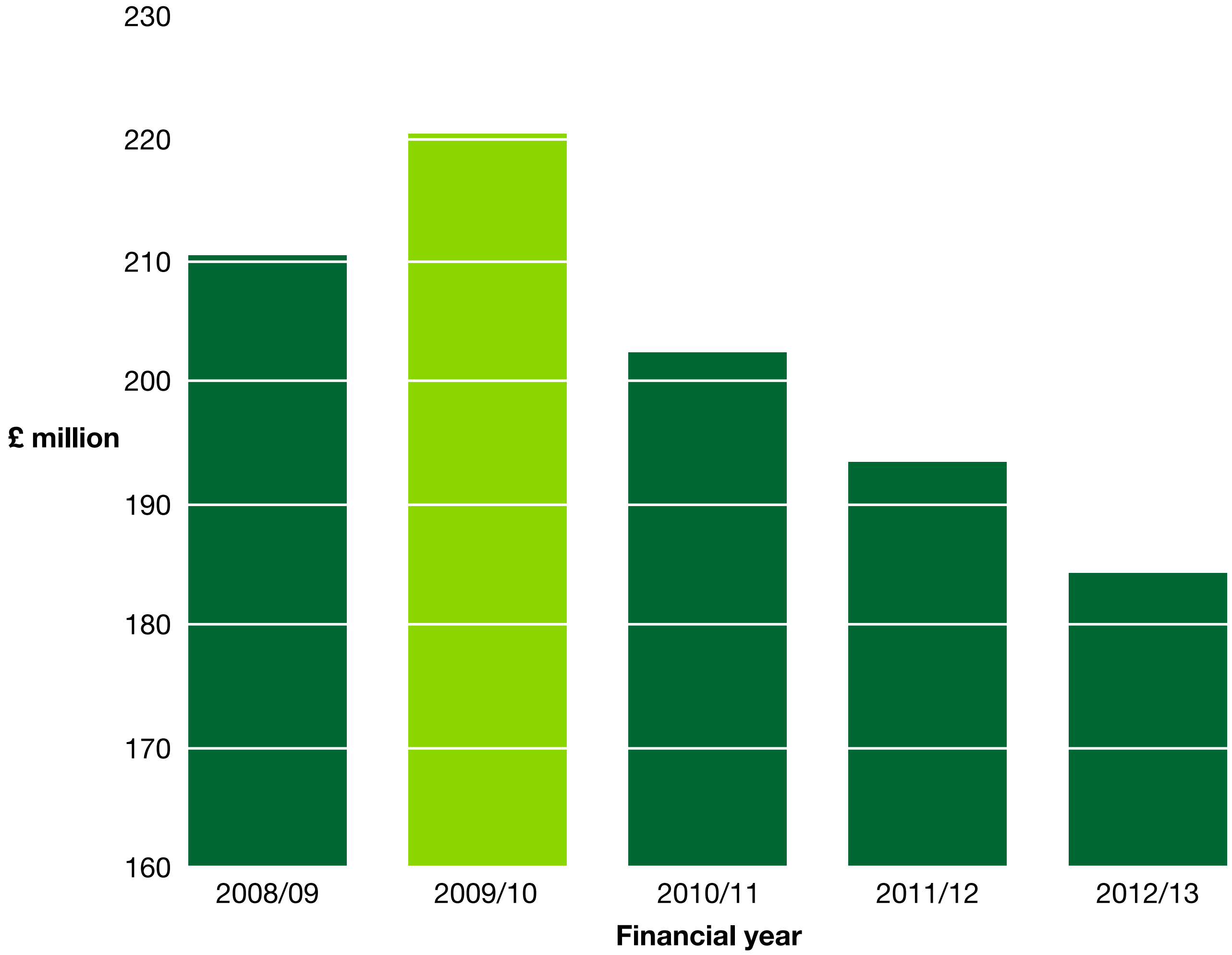
The increase in staff salaries in 2009/10 also reflects the cost of living pay award agreed under a three-year pay agreement. In 2010/11, the final year of the agreement, the Commission will pay a salary increase of 0.7 per cent to staff earning less than £100,000. The Commission will observe the two-year pay freeze for public sector staff announced in the Chancellor's emergency budget on 22 June 2010.

The cost of bought-in services (for example contractor and consultancy costs) reduced by £3.5 million. The Commission also reduced its spending on supplies and services, travel and subsistence, recruitment, and training in the last year. Costs in other areas will reduce in future years as the Commission delivers its planned efficiency savings.

Before the announcement that CAA would stop, the Commission's financial strategy was to reduce costs by £32.1 million by 31 March 2013. The Board will update this forecast to reflect recent developments. Chart 2 shows planned cost reductions before the announcement.

The Commission planned to review each of its business areas to deliver 15 per cent savings over the next three financial years. The Commission is now reviewing these plans to increase savings in line with expectations of 25 per cent real-term cuts across the public sector.

Chart 2: **Total costs (2008/09 – 2012/13) *before* CAA stopped in May 2010/1**



Staffing levels

Staff numbers had increased by 14 at the end of 2009/10 to 1,985 (2008/09: 1,971). This figure includes 30 FTEs who left the organisation on 31 March 2010 and reflects the expansion in the graduate trainee programme to 87 recruits last year.

In 2009/10, the Commission brought existing and new trainees together from within regions, to manage them as part of a centrally coordinated scheme. The four-year programme leads to the CIPFA professional qualification. Having more trainees enables us to reduce our reliance on contractors. These trainees are an investment in the senior managers of the future.

Staff numbers will reduce in 2010/11 because CAA has stopped, inspection will contract and we will reduce our administrative costs.

Pension scheme

The Commission's annual accounts show the pension scheme shortfall increased by £102.96 million at March 2010, following revaluation of the scheme's assets and liabilities in line with International Accounting Standard 19 (IAS19) for employee benefits. The Commission is already addressing this shortfall to ensure the financial resilience of the pension fund. The Commission's Board has agreed to increase employee contributions from 1 July 2010. The normal retirement age (NRA) will increase to 65 years from 1 July too.

Financial performance in 2009/10

The Commission forecast a published deficit for the year of £7.0 million in January 2010. The actual figure turned out to be £9.0 million, due mainly to a loss on pension scheme assets and liabilities of £1.5 million.

The Commission aims to follow the principles of HM Treasury's Better Payment Practice Code and pay undisputed invoices from its suppliers within 30 days. We paid 94.3 per cent of undisputed invoices within 30 days in 2009/10 (2008/09: 91 per cent).

Remuneration report

Remuneration policy

In determining the appropriate level of remuneration for members of the Audit Commission Management Team, the Commission has regard to:

- the need to attract and retain suitably qualified and experienced individuals to enable the Commission to fulfil its remit and responsibilities;
- market intelligence and specialist advice on national and regional labour markets; and
- official guidance, including the government's inflation target.

In March 2008 the Commission established a Remuneration Committee as a standing committee of the Board. It comprises three Commissioners and meets at least once a year. Its Terms of Reference are:

- to determine the remuneration and other terms and conditions of service of the Chief Executive;
- to receive reports from the Chairman of the Commission on his annual appraisals of the Chief Executive following consultation with Commissioners;
- to receive reports from the Chief Executive on his annual appraisals of members of the Management Team, and to determine their remuneration on receipt of recommendations from the Chief Executive;
- to determine or make recommendations on any issue referred to it by the Board; and
- to determine or, where matters are reserved to the Board, make recommendations on such other issues as may be proposed by the Chairman or Chief Executive, for example the strategy on staff pay awards.

All roles are subject to a competitive external recruitment process.

Chief Executive's and Managing Directors' remuneration

The remuneration and contract terms of the Chief Executive and Managing Directors are determined by the Audit Commission Board in accordance with Schedule 1 of the Audit Commission Act 1998.

Composition of remuneration

The main components of the Management Team members' remuneration are:

- **Salary** The basic salary for each Management Team member is determined by taking account of each person's responsibilities, record of achievement and experience, together with market analysis.
- **Other benefits** All Management Team members (with the exception of the Chief Executive) are eligible for a leased car. Individuals can opt for an alternative transport allowance. A travel card for travel within London is also available.
- **Performance-related pay** The Board agreed to stop annual performance-related bonuses for staff with a contractual entitlement to receive one. This was compensated for by a one-off 6 per cent increase in basic salary for these staff on 1 April 2009.

Chief Executive and Management Team appointments

	Date of joining	Date of appointment to post
Steve Bundred, Chief Executive[1]	01/09/03	01/09/03
Gareth Davies, Managing Director, Local Government, Housing and Community Safety	01/09/87	19/10/06
Tracey Dennison, Managing Director, Human Resources	17/11/03	17/11/03
Martin Evans, Managing Director, Audit	05/10/98	01/04/06
Andy McKeon, Managing Director, Health	08/09/03	08/09/03
Eugene Sullivan, Managing Director, Finance & Corporate Services[2]	02/06/08	02/06/08
David Walker, Managing Director, Communications and Public Reporting	06/10/08	06/10/08
Peter Wilkinson, Managing Director, Policy Research and Studies	21/05/90	01/11/06

Note 1: Steve Bundred left the Commission on 31 March 2010.
Note 2: Eugene Sullivan became Acting Chief Executive Officer with Accounting Officer responsibilities on 1 April 2010.

Pension arrangements

The Chief Executive and Managing Directors are all eligible to be members of the Audit Commission Pension Scheme. This is a stand-alone defined benefit scheme with the same level of benefit for all members. From 1 August 2008 contributions to the Audit Commission Pension Scheme are made via a “salary sacrifice” arrangement called SMART Pensions.

Other terms of employment

Notice periods and provisions for compensation for early retirement are based on those for staff. The Commission will appoint on a fixed-term or permanent contractual basis as appropriate, although all contracts currently in place are on a permanent basis.

Chief Executive and Management Team remuneration details (audited)

	Year to 31 March 2010 Salary £000	Other benefits £000	Total (excluding employer pension contribution) £000	Year to 31 March 2010 Pension contribution £000	Year to 31 March 2009 (excluding pension contribution) £000
Steve Bundred	217	0	**217**	53	**208**
Gareth Davies	163	3	**166**	43	**165**
Tracey Dennison	119	6	**125**	29	**121**
Martin Evans	142	6	**148**	53	**147**
Andy McKeon	167	5	**172**	41	**166**
Eugene Sullivan[1]	168	4	**172**	41	**149**
David Walker[2]	115	5	**120**	40	**59**
Peter Wilkinson	149	6	**155**	56	**153**

Note 1: The figures for 2008/09 relate to the period 02/06/08 to 31/03/09.
Note 2: The figures for 2008/09 relate to the period 06/10/08 to 31/03/09.

Chief Executive and Management Team pension entitlement details (audited)

	Real increase in pension at 60 £000	Total accrued pension at 31 March 2010 £000	Total accrued pension at 31 March 2009 £000	Increase in transfer value £000	Transfer value at 31 March 2010 £000	Transfer value at 31 March 2009 £000
Steve Bundred	6	**63**	57	223	**1,511**	1,288
Gareth Davies	6	**52**	46	136	**833**	697
Tracey Dennison	4	**50**	46	120	**957**	837
Martin Evans	5	**53**	48	147	**1,137**	990
Andy McKeon	5	**73**	68	203	**1,608**	1,405
Eugene Sullivan	2	**4**	2	58	**102**	44
David Walker[1]	2	**3**	1	44	**58**	14
Peter Wilkinson	4	**39**	35	151	**920**	769

Note 1: The normal retirement age for staff that joined the pension scheme before 1 August 2008 is 60 years. The normal retirement age for staff joining the pension scheme on or after 1 August 2008 is 65 years.

The pension entitlement calculation assumes a retirement age of 60, except for staff who joined after 1 August 2008. David Walker is the only member of the Management Team who joined after this date.

The transfer values above are calculated using a set of assumptions prescribed by the Cabinet Office and known as the Public Sector Transfer Club basis.

Commissioner remuneration policy

The remuneration paid to non-executive Commissioners is determined by the Secretary of State for Communities and Local Government and is based on the anticipated number of days worked. This is currently three days per month, with the exception of the Deputy Chairman who receives payment based on five days per month.

The Secretary of State also determines the Chairman's remuneration, which is based on an average weekly time commitment of two days per week.

The cost of living award paid to Commissioners each year is also determined by the Secretary of State and is usually linked to the award granted to senior civil servants. There was a 1.5% increase awarded in 2009/10.

With the exception of the Chief Executive, no other Commissioner receives remuneration benefits from the Audit Commission, nor are they members of the Audit Commission Pension Scheme.

The Commission has unfunded liabilities for the provision of a pension of £85,000 (2008/09: £66,000) in respect of one former Commissioner.

Commissioner remuneration details (audited)

	Year to 31 March 2010 £000	Year to 31 March 2009 £000
Commissioners in place at 31 March 2010		
Michael O'Higgins, (Chairman)	**90**	89
Lord Adebowale, CBE	**14**	14
Councillor Sir Merrick Cockell[1]	**10**	0
Jim Coulter	**14**	14
Dr Jennifer Dixon	**14**	14
Sheila Drew Smith, OBE	**14**	14
Councillor Stephen Houghton, CBE	**14**	14
Councillor Peter Jones[2]	**1**	14
Sir Thomas Legg, KCB QC	**14**	14
Dame Denise Platt	**14**	14
Brian Pomeroy, CBE[2]	**2**	19
Dr Raj Rajagopal	**14**	14
Bharat Shah (Deputy Chairman and Audit Committee Chairman)[3]	**24**	19
Professor Peter C Smith[2]	**1**	14
Jenny Watson	**14**	14
Councillor Chris White	**14**	14
Steve Bundred[2] (see above for remuneration details)		

Note 1: The appointment of Councillor Sir Merrick Cockell started on 13/07/09.
Note 2: The appointments of Councillor Peter Jones, Brian Pomeroy and Professor Peter C Smith ended on 30/04/09. Steve Bundred's appointment ended on 31/03/10.
Note 3: The appointment of Bharat Shah as Audit Committee Chairman started on 1/05/09.

Eugene Sullivan

Accounting Officer
12 July 2010

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Statement of responsibilities

Board members' responsibilities

The Board is responsible for:

- ensuring that high standards of corporate governance are observed at all times;
- ensuring that the Commission identifies and manages its risks effectively;
- subject to the requirement that the Commission maintains at all times its independence, ensuring that, in reaching decisions, the Board has taken into account directions issued by the Secretary of State and any relevant guidance issued by the sponsoring departments and had regard to any applicable government policy; and
- establishing and maintaining effective arrangements for the discharge of the Commission's functions, including delegating to staff within a clear framework of strategic control, and ensuring the Accounting Officer has sufficient resources to discharge his functions.

Statement of Accounting Officer's responsibilities

In accordance with paragraph 11 (1) of Schedule 1 to the Audit Commission Act 1998, the Secretaries of State for Communities and Local Government, and Health directed the Commission to prepare a Statement of Account. The accounts are prepared on an accruals basis and must show a true and fair view of the Commission's state of affairs at the period end and of its income and expenditure and cash flows for the accounting period.

In preparing the accounts the Accounting Officer is required to:

- observe the Accounts Direction issued by the Secretaries of State, including the relevant accounting and disclosure requirements, and apply suitable accounting policies on a consistent basis;
- make judgements and estimates on a reasonable basis;
- state whether applicable accounting standards have been followed, and disclose and explain any material departures in the accounts; and
- unless inappropriate, prepare the accounts on the going concern basis.

The Chief Executive has been appointed Accounting Officer for the Commission. His relevant responsibilities as Accounting Officer, including his responsibility for the propriety and regularity of the public finances for which he is answerable, for the keeping of proper records, and for safeguarding the Commission's assets, are set out by HM Treasury and published in Managing Public Money.

Statement on internal control

1. Scope of responsibility

1.1 As Accounting Officer, I am responsible for upholding sound internal controls that support the Commission's policies and objectives. The internal controls safeguard the public funds and assets for which I am personally responsible under Managing Public Money.

1.2 I took up the positions of Acting Chief Executive and Accounting Officer for the Audit Commission on 1 April 2010. Until 31 March 2010, Steve Bundred was the Commission's Chief Executive and Accounting Officer. On 31 March 2010 Steve Bundred wrote to me formally confirming:

- in the period from 1 April 2009 to 31 March 2010, sound internal controls were in place which accord with Treasury guidance; and
- to the best of his knowledge no significant internal control issues arose in the period 1 April 2009 and 31 March 2010.

2. The purpose and nature of the system of internal control

2.1 Internal controls aim to manage risk to a reasonable level rather than to remove all risk of failure to achieve policies and objectives. Internal controls can therefore only provide reasonable and not total assurance of effectiveness.

2.2 The principal features of the system of internal control and key high-level controls in place throughout the year are:

- an organisational structure that supports clear lines of communication, monitoring, reporting and accountability;
- business strategies that are approved by the Commission Board and are subject to consultation with Commission stakeholders;
- key performance indicators that are regularly measured against the strategic plan;
- detailed business plans produced at regional and Directorate level that include risk assessments of all their business activities; and
- a risk escalation process allowing risks identified within business plans to be brought to the attention of senior directors, the Audit Committee and the Commission Board if required.

2.3 The high-level controls enable the Commission to encourage innovative solutions that, while sometimes involving risk, can be carried out with an awareness and active management of the risks that they carry.

2.4 We evaluate the effectiveness of our system of internal control through:

- scrutiny of internal audit reports, internal controls and risks by our Audit Committee;
- a regular programme of internal audit;
- external audit by the National Audit Office;

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- review and external accreditation of our controls over information security;
- engagement of external reviewers as needed; and
- review and external accreditation of the quality of our audit work.

2.5 The system of internal control has been in place in the Commission for the year ended 31 March 2010 and up to the date of approval of the annual report and accounts, and accords with Treasury guidance.

3. Our principal internal controls

The Commission's structure and governance framework

3.1 The Commission subscribes to the seven principles of conduct underpinning public life as set out by Lord Nolan (selflessness, integrity, objectivity, accountability, openness, honesty and leadership).

3.2 On 23 April 2009, the Commission Board approved a new draft framework agreement between the Commission and its principal sponsoring department, Communities and Local Government. The Commission presented the draft agreement to Communities and Local Government and the Department of Health for discussion. The Commission awaits the response of the sponsoring departments.

3.3 The Commission consults ministers and others extensively when planning its activities, including on the risks associated with different courses of action. It also oversees progress against both the activities and the risks. The Commission Solicitor routinely attends Board meetings to advise on governance and legal risks.

3.4 Internally the Commission has produced, after both internal and external consultation, a comprehensive Corporate Governance Framework, which clearly sets out how the Board manages its affairs and which matters are delegated to the Chief Executive and which reserved to the Board. The Commission reviews the Framework yearly. The Framework sets out the role of the Commission's Board.

3.5 The Commission Board comprises Commissioners who are independent appointees of the Secretary of State for Communities and Local Government in consultation with the Secretary of State for Health. Commissioners usually serve for a three-year term which may be extended. The Board has the final responsibility for ensuring the Commission identifies and manages its risk effectively. Under a clear governance framework, it makes decisions in the most significant of the Commission's areas of responsibility. The Audit Committee reviews the major risks quarterly.

3.6 All reports to the Board include details of the risks arising from the issue under consideration.

3.7 The Commission's Corporate Governance Framework states the Board will review its performance every two years. The most recent review took place in March 2009, when the Board engaged Deloitte to conduct an independent review of the Board's performance in March 2009. Deloitte's report to the Board on 22 April 2009 said the Commission has a high-performing Board which displays robust and productive challenge and good governance, underpinned by a Corporate Governance Framework reflecting best practice. The next review will take place in 2011.

3.8 Also the Commission has drawn up a Scheme of Delegation which addresses delegations by the Chief Executive, as required by the Corporate Governance Framework. This Scheme, which the Commission also reviews yearly, covers all Directorates and enshrines a systematic and common approach to delegation within the organisation. The Scheme is backed by a comprehensive set of financial, IT and human resources policies. The Audit Committee and Board approve the prime financial policies yearly. As Accounting Officer, I approve the more detailed policies which support the prime financial policies.

3.9 The Scheme of Delegation sets out the role of the Commission's Management Team. The Management Team has the responsibility for overseeing risk management within the Commission.

3.10 The culture of risk management within the Commission is determined at a strategic level. The Management Team formally reviews all significant risks and ensures that they have been correctly stated. It also considers risk as part of its decision-making processes and satisfies itself that less significant risks are being actively managed by relevant departmental managers, with the proper controls in place, and that these controls are working effectively.

3.11 The Management Team considers all significant papers for both the Board and the Audit Committee, to ensure all relevant issues are considered.

Risk management

3.12 The key risks managed by the Commission during 2009/10 were:

- the risk that audit and inspection work is of poor quality, and vulnerable to legal challenge;
- the risk that inspection and assessment work is not effective and does not deliver value to audited and inspected bodies;
- the risk that our assessment regime does not respond promptly and effectively to changes in government policy;
- the risk of failure to achieve targets for savings and efficiencies;
- the risk of political criticism or adverse media coverage of the Commission;
- the risk that we do not comply with Data Protection and Freedom of Information

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legislation, or government data security requirements, resulting in loss or inappropriate disclosure of data;
- the risk of difficulties in getting data for audit and inspection work because of data security controls;
- the risk that current banks fail to honour their commitments;
- the risk of disruption to business continuity because of major incident, systems failure or supplier failure;
- the risk of poor management of staff performance and employment-related legal proceedings; and
- the risk that we fail to embed sustainable development in assessment work or internal practices.

3.13 Proper consideration of mitigating risk is important to the effectiveness of internal control. Risks are identified at an operational level and consolidated to identify themes arising across the organisation. All management teams have managing their own risks as a regular agenda item, and local risk registers are kept. The corporate-level risks arising from this process are reviewed for completeness by the Management Team and the Audit Committee.

3.14 The Commission has identified risk areas which it is actively managing:
- strategic risks;
- risks to the Commission's reputation and credibility;
- operational risks;
- risks associated with financial and regime stability;
- financial risks;
- legal risks; and
- information risks.

3.15 To uphold a proper profile within the organisation, the Audit Committee receives regular presentations from the responsible executives on emerging or changing risks. These presentations detail the risk, how the risk is changing, and the steps being taken to limit or remove it.

3.16 The Commission has designed its risk processes to:
- set up a policy framework approved by the Commission Board and the Management Team, within which strategic risks are identified, managed and kept under review. The Commission reviews its risk management policy yearly to ensure the policy reflects best practice and clarifies the Commission's risk appetite;
- embed risk management and compliance by making it part of day-to-day management processes;
- adopt a consistent approach to risk management throughout the organisation; and
- encourage staff to identify and manage risk.

3.17 The Head of Assurance commissioned an independent internal audit of risk management in 2009/10. RSM Tenon undertook the review and the Head of Assurance presented their report to the Audit Committee on 18 February 2010. RSM Tenon gave substantial assurance the Commission's risk management policies and processes reflected best practice, and that we were applying them properly and consistently.

3.18 The Commission's risk processes properly consider information risks and the controls in place to protect the Commission's information assets. These processes recognise that personal and other sensitive information, including employee information, requires extra safeguards. Auditors and inspectors will have access to personal data routinely as part of their work. Security and confidentiality are key requirements in holding this data.

Financial Management

3.19 The Commission has established the Improving Financial Management Programme to strengthen its financial management, processing and reporting. During 2009/10 the programme has made significant progress by:

- improving the efficiency of the financial system (Agresso) by cleansing and archiving data;
- establishing a Management Information project to develop web-based financial reporting; and
- introducing an online staff expenses system, which went live on 1 April 2010.

3.20 In 2010/11 the Improving Financial Management team will upgrade the Commission's financial system, introduce improved financial planning tools, improve the efficiency of payment processes and complete its work on improved financial monitoring and reporting.

4. How we evaluate internal controls

The Audit Committee

4.1 The Audit Committee comprises no fewer than four Commissioners. It meets at least three times a year and in the year under review, met five times. Its Terms of Reference are:

- to oversee the production of the Commission's annual accounts and to recommend them to the Board for approval;
- to examine and review:
  - the Commission's financial, accounting and tax policies, practices and processes, including IT;
  - the Commission's internal controls including policies for addressing fraud and arrangements for internal audit; in particular to appoint the internal auditors, approve their workplan and review their reports and the responses of management;

- the Commission's assessment and management of risk, including risk associated with implementation of significant new systems and failure to comply with laws and regulation; and
- the results of the external audit by the National Audit Office, including their management letter and the response by management;

- to carry out recommendations from audit reports, hold the executive to account where they have not acted on, or have disagreed with, significant agreed recommendations;
- to examine any work of the organisation against the criteria of best practice and to report to the Board as fitting;
- to oversee the Quality Review Process for assessing the performance of auditors and inspectors appointed by the Commission, whether from its own staff or from external suppliers; and
- to report yearly to the Board on its views of the Commission's governance and the Audit Committee's own effectiveness.

4.2 The members of the Audit Committee for the period under review were:

Audit Committee Member	Period of Office
Bharat Shah (The chair from 1 May 2009)	Whole year
Brian Pomeroy (The chair until 30 April 2009)	Until 30 April 2009
Sheila Drew Smith, OBE	Whole year
Sir Thomas Legg, KCB QC	Whole year
Councillor Chris White	Whole year

4.3 As Accounting Officer, I normally attend meetings of the Audit Committee.

4.4 The Audit Committee will review its effectiveness every year. In 2009/10 the Head of Assurance undertook the assessment of the Audit Committee's effectiveness. The National Audit Office reviewed the results of her assessment and she reported the results of the assessment to the Audit Committee on 18 February 2010. The self-assessment decided the Audit Committee complied in all material respects with the National Audit Office's best-practice guidance for Audit Committees.

Internal audit

4.5 The Commission's Head of Assurance is responsible for internal audit and reports to the Audit Committee and Accounting Officer regularly to standards defined in the government's Internal Audit Standards. Those reports include the Head of Assurance's independent opinion on the adequacy and effectiveness of the Commission's system of internal control with the recommendations for improvement. The Commission also encourages and supports liaison between internal and external audit to achieve a more effective audit, based on a clear understanding of respective roles and requirements.

4.6 The Head of Assurance attends all Audit Committee meetings and has direct access to me and to the chair of the Audit Committee.

External audit

4.7 The external auditor, the Comptroller and Auditor General, is appointed by statute, and the National Audit Office regularly comments on governance.

4.8 The external auditor is invited to attend all Audit Committee meetings and has direct access to me and to the Chair of the Audit Committee.

Information assurance

4.9 We aim to avoid collecting and holding large volumes of personal data, unless required for a specific purpose, and have put in place suitable measures to ensure that we manage information risks. These measures include the secure encryption of all laptops to the FIPS 140 standard, and controls to prevent unauthorised access to our network systems. We require all staff to undertake annual information assurance training. In 2009/10, all staff completed the National School of Government training module on data security.

4.10 We have embedded our Information Assurance Framework during 2009/10, which included information risk controls.

- We have appointed Information Asset Owners (IAOs) for all data held by the Commission.
- IAOs have undertaken an information assurance audit during the year, assessing the risks associated with their data and ensuring that they take suitable mitigating action.
- The Information Asset Register has been updated to reflect the findings of the Information Assurance Audits.
- IAOs have provided a signed declaration to the Commission's Senior Information Risk Owner (SIRO) to confirm they have identified, evaluated and addressed the risks associated with the information they held during 2009/10.

4.11 The Commission had processes and systems in place during 2009/10 that ensure compliance with Data Protection Act and Freedom of Information Act requirements, and that information held by the Commission is held securely and accurately processed.

4.12 It is a requirement to report protected personal data-related incidents to the Information Commissioner's Office. The Commission had no protected personal data security breaches during the year to 31 March 2010 that needed reporting to the Information

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Commissioner or to its sponsoring department, Communities and Local Government. During the year the following small, localised incidents occurred:

Items lost or stolen 2009/10	Number
Laptops	10
Personal digital assistants	8
Mobile phones	16
Memory sticks	38
CDs / DVDs	2

Devices containing personal or confidential data were fully encrypted to the government-required standard of FIPS 140, which provides proper security. None of these losses put personal data at significant risk.

4.13 The National Fraud Initiative collects large volumes of personal data but has comprehensive security and risk management procedures in place. In 2009/10 the Commission secured independent accreditation through a Risk Management Accreditation Document Set (RMADS) endorsed by CESG (the National Technical Authority for Information Assurance) to demonstrate that the NFI system complies with HMG Information Assurance Standard No.1 and Standard No.2.

4.14 We comply with the statutory Code of Data Matching Practice as a key means of ensuring that our data matching exercises comply with the Data Protection Act 1998. We have established a Data Matching Strategy Board, chaired by a commissioner and including independent members, to ensure proper governance of data matching.

4.15 In 2009/10 the Commission itself took part in NFI matching for payrolls and pensions data. The Head of Assurance has followed up the matches identified and found no evidence of fraud.

Quality review of audit and inspection work

4.16 The Commission has a well-developed, rigorous approach to reviewing the quality of the work of appointed auditors. Our quality review process places reliance on the published results of the annual quality review of the firms' work by the Audit Inspection Unit (AIU – part of the Financial Reporting Council) and on the AIU's inspection of the Commission's Audit Practice. We also commission the AIU to carry out cyclical reviews of the firms' work for us. A separate programme of quality reviews focuses on those aspects of audit work that are specific to the Commission's audit regime and compliance with the Commission's regulatory requirements. These reviews are carried out by the

Commission's Director of Audit Policy and Regulation, who reports her findings to the Commission's Audit Committee. The results of the annual quality review programme are published.

4.17 The Commission's in-house Audit Practice has put in place a comprehensive quality framework that meets the standards set out in the International Standard on Quality Control (ISQC) (UK and Ireland) 1, issued by the Auditing Practices Board. ISQC (UK and Ireland) 1 sets out standards and provides guidance about a firm's responsibilities for its system of quality control for audits and reviews of historical financial information, and for other assurance and related services engagements. However, our arrangements go beyond this standard to meet certain added requirements of the Commission's audit regime. The Commission's Audit Practice is subject to independent inspection by the AIU, which reports its findings to the Commission Board. The findings of the AIU's inspection are reported, together with the results of the annual internal quality monitoring programme, in the Audit Practice's annual quality report.

4.18 The Commission also applies a rigorous quality assurance framework to its Comprehensive Area Assessment judgements. Trained staff undertake independent quality reviews both before and during on-site work. This review ensures the assessment process is consistent with guidance, and the work programme and evidence gathered are enough to ensure robust scored judgements.

5. Review of effectiveness

5.1 As Accounting Officer, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the Commission who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. I have received assurances from the Audit Committee and from the Management Team that feed into my assessment of the effectiveness of the system of internal control.

5.2 During 2009/10, no significant internal control issues arose, which require reporting in the Statement on Internal Control. The National Audit Office have not raised any issues of significance in their interim management letter for 2009/10.

5.3 The process the Commission has upheld to ensure internal control during the period includes both risk management and other sources of assurance, including internal audit. The Commission's Head of Assurance has regular access to me and to the chair of the Audit Committee, and attends every Audit Committee meeting.

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5.4 I believe there are satisfactory processes in place to identify and manage the significant risks faced by the Commission.

Eugene Sullivan

Accounting Officer
12 July 2010

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The certificate and report of the Comptroller and Auditor General to the Houses of Parliament

I certify that I have audited the financial statements of The Audit Commission for Local Authorities and the National Health Service in England (the Commission) for the year ended 31 March 2010 under the Audit Commission Act 1998. These comprise the Statement of Comprehensive Income, the Statement of Changes in Taxpayers' Equity, the Statement of Financial Position, the Statement of Cash Flows, and the related notes. These financial statements have been prepared under the accounting policies set out within them. I have also audited the information in the Remuneration Report that is described in that report as having been audited.

Respective responsibilities of the Accounting Officer and auditor
As explained more fully in the Statement of Accounting Officer's Responsibilities, the Accounting Officer is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me and my staff to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Commission's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Commission; and the overall presentation of the financial statements.

In addition, I am required to obtain evidence sufficient to give reasonable assurance that the expenditure and income reported in the financial statements have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Opinion on regularity
In my opinion, in all material respects the expenditure and income have been applied to the purposes intended by Parliament and the financial transactions conform to the authorities which govern them.

Opinion on financial statements
In my opinion:

- the financial statements give a true and fair view of the state of the Commission's affairs as at 31 March 2010 and of its deficit, changes in taxpayers' equity and cash flows for the year then ended; and
- the financial statements have been properly prepared in accordance with the Audit Commission Act 1998 and the Secretary of States' Accounts Directions issued thereunder.

Opinion on other matters

In my opinion:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with Secretary of States' Accounts Directions issued under the Audit Commission Act 1998; and
- the information given in the section on Commissioners and senior managers during the period of review and the Financial Review for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

I have nothing to report in respect of the following matters which I report to you if, in my opinion:

- adequate accounting records have not been kept; or
- the financial statements are not in agreement with the accounting records or returns; or
- I have not received all of the information and explanations I require for my audit; or
- the Statement on Internal Control does not reflect compliance with HM Treasury's guidance.

Report

I have no observations to make on these financial statements.

Amyas C E Morse
Comptroller and Auditor General
National Audit Office
157-197 Buckingham Palace Road
Victoria, London SW1W 9SP

14 July 2010

Statement of comprehensive income for the year ended 31 March 2010

	Note	Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000
Operating income			
Audit fee income		**175,526**	176,125
Inspection income	3	**35,213**	37,485
Other operating income	4	**2,359**	2,076
Total operating income	2	**213,098**	215,686
Operating costs			
Staff and members' costs	5	**131,531**	117,994
Bought-in services	6	**54,460**	57,928
Other operating costs	7	**35,046**	33,316
Notional capital costs	1(x)	**(739)**	873
Total operating costs including notional capital costs		**220,298**	210,111
Operating surplus/ (deficit) including notional capital costs	25	**(7,200)**	5,575
Financing income			
Add back notional capital costs	1(x)	**(739)**	873
Net investment return	8	**384**	519
Net return on pension scheme assets	24(x)	**(1,483)**	4,704
Surplus/ (deficit) for the financial year		**(9,038)**	11,671

The comprehensive income statement brings together the income (expressed as the value of work done) and the costs incurred (valued on an accruals basis) in running the business.

Statement of changes in taxpayer's equity for the year ended 31 March 2010

	Note	Capital Reserve £000	Pension Reserve £000	Retained Earnings £000	Total £000
Restated balance at March 2008		3,734	(16,705)	28,413	15,442
Restated surplus for the year		0	5,121	6,550	11,671
Transfer		(3,734)	0	3,734	0
Actuarial movements in the year		0	8,118	0	8,118
Restated balance at 31 March 2009	21-23	**0**	**(3,466)**	**38,697**	**35,231**
Surplus/ (deficit) for the year		0	549	(9,587)	(9,038)
Transfer		0	0	0	0
Actuarial movements in the year	24(xi)	0	(103,504)	0	(103,504)
Net movement this year		**0**	**(102,955)**	**(9,587)**	**(112,542)**
Balance at 31 March 2010	21-23	**0**	**(106,421)**	**29,110**	**(77,311)**

The statement of changes in taxpayer's equity analyses the change in the Commission's net worth. It shows operational changes that feed through to the statement of financial position and changes resulting from the revaluation of assets and liabilities that have affected its position.

The total net movement in this period of £112.542 million equals the difference between the opening and closing statement of financial position for this financial year (£35.231 million – (£77.311) million).

Statement of financial position as at 31 March 2010

	Note	As At 31 March 2010 £000	As At 31 March 2009 Restated £000	As At 1 April 2008 Restated £000
Non-current assets				
Intangible assets	10	**1,180**	527	261
Plant and equipment	11	**6,903**	7,429	6,858
Long-term receivables	12	**4,828**	6,870	0
Total non-current assets		**12,911**	14,826	7,119
Current assets				
Trade receivables and work in progress	13	**23,358**	30,342	27,025
Other receivables	14	**8,793**	7,730	8,740
Short-term investments	15	**47,000**	57,000	63,000
Cash and cash equivalents	15	**306**	0	0
Total current assets		**79,457**	95,072	98,765
Total assets		**92,368**	109,898	105,884
Current liabilities				
Trade and other payables	16	**19,304**	12,115	12,153
Deferred income	17	**38,926**	57,037	58,969
Current provisions	18	**3,592**	736	1,026
Total current liabilities		**61,822**	69,888	72,148
Total assets less current liabilities		**30,546**	40,010	33,736

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Statement of financial position as at 31 March 2010

	Note	As At 31 March 2010 £000	As At 31 March 2009 Restated £000	As At 1 April 2008 Restated £000
Non-current liabilities				
Non-current provisions	19	**1,436**	1,313	1,590
Pension	24(vi)	**106,421**	3,466	16,705
Total non-current liabilities		**107,857**	4,779	18,295
Assets less liabilities		**(77,311)**	35,231	15,442
Financed by				
Capital reserves	20	**0**	0	3,734
Retained earnings:				
Local Government	21	**26,800**	32,705	24,554
Health	22	**2,310**	5,992	3,859
		29,110	38,697	28,413
Pension reserve	23	**(106,421)**	(3,466)	(16,705)
Total taxpayer's equity		**(77,311)**	35,231	15,442

The statement of financial position summarises the Commission's assets and liabilities and how these are held across the retained earnings and the pension reserve.

The notes that follow form part of these financial statements.

Eugene Sullivan

Accounting Officer
12 July 2010

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Statement of cash flows for the year ended 31 March 2010

	Note	Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000
Operating surplus/ (deficit)		**(7,200)**	5,575
Adjustments for:			
Notional costs/ (credits)		**(739)**	873
Pension (credit)/ charge		**(2,032)**	(417)
Depreciation and amortisation	10, 11	**2,422**	1,859
Loss on disposal of fixed assets		**1,027**	64
(Increase)/ decrease in trade receivables and work in progress	12-14	**7,963**	(9,177)
Increase/ (decrease) in payables and provisions	16-19	**(7,581)**	(2,683)
Net cash from operating activities		**(6,140)**	(3,906)
Cash flows from investing activities			
Payments to acquire short-term investments	15	**(47,000)**	(57,000)
Repayments on maturity of short-term investments	15	**57,000**	63,000
Interest received	8	**384**	519
Purchase of non-current assets	10, 11	**(3,576)**	(2,760)
Net cash from investing activities		**6,808**	3,759
Net increase/ (decrease) in cash and cash equivalents		**668**	(145)
Cash and cash equivalents at the beginning of the year		**(362)**	(217)
Cash and cash equivalents at the end of the year	15	**306**	(362)

The cash flows statement shows how changes in the comprehensive income statement and the statement of financial position affect cash and cash equivalents. It analyses the changes by operating, investing and financing activities.

The notes that follow form part of these financial statements.

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Notes to the financial statements

Introduction

The notes that follow form part of the financial statements.

Note 1 describes the accounting conventions and policies used to prepare these financial statements.

Notes 2 – 24 provide supporting information to the primary financial statements.

Notes 25 – 31 provide additional information showing the operating results for the previous four accounting periods, future financial commitments, contingent liabilities and post statement of financial position events.

Note 1: Accounting conventions and policies

(i) The accounts are prepared under the historical cost convention, modified to account for the:
- revaluation of fixed assets to their value to the business by reference to their current costs, in a form directed by the Secretary of State, with the approval of HM Treasury, under paragraph 11 (1) of Schedule 1 to the Act; and
- the valuation of the pension scheme assets is at fair value and liabilities is at present value as per IAS19.

(ii) The accounts meet the requirements of the Companies Acts 2006, without limiting the information given, and applicable accounting standards so far as those requirements are appropriate.

(iii) Income and expenditure is directly attributed where possible to either Local Government or Health activities (Note 2 refers). Where this is not possible, income and expenditure has been attributed to each activity on an hours-worked or other appropriate basis.

(iv) Operating lease rentals are charged on a straight-line basis over the lease term.

(v) Gross fee income and other operating income are recognised on the value of chargeable work exclusive of VAT.

(vi) Operating income, whether generated by direct government grant, fees to authorities or otherwise, is credited to the year of account in which the work is done.

(vii) The net costs arising from litigation, if any, are not treated as part of the Commission's operating result, but shown separately on the statement of comprehensive income.

(viii) Depreciation is provided on all plant and equipment, and intangible assets calculated to write off the cost, less estimated residual value, of each asset in equal annual instalments over its expected useful life as follows:

Furniture and fittings	10 years
Computer equipment	3 years
Office equipment	5 years
Intangible assets – software	3 years

Under the Commission's capitalisation policy, individual computer equipment in excess of £5,000, other equipment in excess of £1,000 and office refurbishments are capitalised.

New software or software upgrades with improved features bought separately from hardware, to include any licences that cover the life of the software with a value over £5,000 are also capitalised.

(ix) The Commission provides a defined benefit pension scheme for its employees, the costs of which are shown in these accounts in accordance with IAS19.

(x) Our Accounts Direction as issued by the Secretary of State for Communities and Local Government and the Secretary of State for Health, requires us to calculate the notional capital cost at 3.5 per cent (2008/09: 3.5 per cent), based on net assets/ liabilities. As the Commission is a fee-earning body, the Commission is allowed to credit this cost back to the statement of comprehensive income.

(xi) Any government grant received in respect of the purchase of specific assets is accounted for through the Government Grant Reserve. It is released into the income statement to match the charge incurred when the underlying assets are depreciated.

(xii) The Commission provides for dilapidation costs under its property leases, discounted to current value. The provision for future dilapidations for leased property is discounted to current value. The real rate used is 2.2 per cent (2008/09: 2.2 per cent).

(xiii) The estimated fair values of the financial instruments of the Commission approximate to their book values at 31 March 2009 and 2010. The following criteria have been used to assess the fair values of the Commission financial instruments:
- trade and other receivables along with deferred income are based upon discounted cash flows at prevailing interest rates or at their nominal amount less impairment losses if due in less than 12 months;
- trade and other payables are based on their nominal amount; and
- short-term investments, cash and cash equivalents are approximate to their book values due to their short maturity period. Cash equivalents are defined as investments of up to one month's duration.

(xiv) Work in progress is valued at estimated realisable value.

(xv) The Commission actively pursues all debt, and provides only for that element where recovery is in doubt. Any debt written off that is subsequently collected is netted against the additional provision made in the period.

(xvi) The Commission recognises as a reduction of income, rebates of where it has a constructive obligation to make payments stemming from a decision of the Board communicated to audited bodies.

(xvii) We have reviewed International Financial Reporting Standards and the Government Financial Reporting Manual (FReM) requirements which have recently been issued or amended, but are not yet effective. The only requirement applicable to the Commission is Chapter 11 of the FReM, relating to Cost of Capital Charging which came into effect on 1 April 2010. This will be applied in next year's financial statements.

(xviii) As a result of a revaluation of pension scheme assets during the year, the Commission's balance sheet at 31 March 2010 shows net liabilities of £77.3 million. This reflects the inclusion of liabilities falling due in future years which, in so far as the Commission is unable to meet them from its other sources of income, would fall, in the last resort, to be met by grants from central government. Under the normal conventions applying to parliamentary control over income and expenditure, such grants may not be issued in advance of need, but there is no reason to believe that, if required, grant funding and parliamentary approval will not be forthcoming. It has accordingly been considered appropriate to adopt a going-concern basis for the preparation of these financial statements.

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Note 2: Segmental analysis

i) Analysis by sector
The Commission is sponsored by two main government departments – Communities & Local Government and Health. The Commission is required to keep a separate account of its health and local government activities.

Table 1 summarises the total income and surpluses arising in the year as shown in the statement of comprehensive income.

	Year to 31 March 2010 £000	Year to 31 March 2009 £000
Operating income	**213,098**	215,686
Net investment return	**384**	519
Net gain on pension scheme assets	**0**	4,704
Total income for the year	**213,482**	220,909

Table 2 analyses the total income for the year shown in Table 1 between the Local Government and Health sectors.

	Year to 31 March 2010 £000	Year to 31 March 2009 £000
Local Government sector income	**149,848**	154,302
Health sector income	**63,634**	66,607
Total income for the year (as in Table 1)	**213,482**	220,909

Table 3 below analyses the total expenditure for the year shown in the statement of comprehensive income.

	Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000
Operating costs	**220,298**	210,111
Remove notional capital costs / credits	**739**	(873)
Loss on pension scheme assets	**1,483**	0
Total expenditure for the year	**222,520**	209,238

Table 4 analyses the expenditure for the year shown in Table 3 between the Local Government and Health sectors.

	Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000
Local Government sector expenditure	**155,395**	144,402
Health sector expenditure	**67,125**	64,836
Total expenditure for the year (as in Table 3)	**222,520**	209,238

The analysis in Tables 2 and 4 above are brought together in Table 5 to show the surplus/ (deficit) for the Local Government sector.

Table 5		Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000
Local Government, Community Safety and Housing Sector			
Income	Audit income	**112,675**	111,710
	Inspection income	**7,197**	11,810
	Grant income	**28,016**	25,675
	Other income	**1,960**	5,107
	Total income (Table 2)	**149,848**	154,302
Expenditure	**Total expenditure** (Table 4)	**155,395**	144,402
Surplus/ (deficit) for the year		**(5,547)**	9,900

During the year the Commission passed back £5.1 million in fees rebates to local government and police bodies.

The analyses in Tables 2 and 4 above are similarly brought together in Table 6 to show the surplus/ (deficit) for the Health sector.

Table 6		Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000
Health Sector			
Income	Audit income	**62,851**	64,414
	Other income	**783**	2,193
	Total income (Table 2)	**63,634**	66,607
Expenditure	**Total expenditure** (Table 4)	**67,125**	64,836
Surplus/ (deficit) for the year		**(3,491)**	1,771

During the year the Commission passed back £1.5 million in fees rebates to health and probation bodies.

ii) Analysis of income between work undertaken by the Commission directly, and work outsourced

The table below provides an analysis of the income for each sector to show the fees earned in respect of work carried out by the private accountancy firms.

Local Government, Community Safety and Housing	**Year to 31 March 2010 £000**	Year to 31 March 2009 £000
Audits undertaken by the Commission	**113,744**	115,798
Audits undertaken by private accountancy firms	**34,144**	33,397
Other income	**1,960**	5,107
Total income (Table 5)	**149,848**	154,302

Health	**Year to 31 March 2010 £000**	Year to 31 March 2009 £000
Audits undertaken by the Commission	**46,891**	45,639
Audits undertaken by private accountancy firms	**15,960**	18,775
Other income	**783**	2,193
Total income (Table 6)	**63,634**	66,607

iii) Analysis of disclosable activity

The Commission has the statutory power to carry out certain other types of work provided it recovers the full cost of doing that work. The relevant sections from the Audit Commission Act 1998 are as follows:

Section 28: Certifying claims or returns made by an authority. Income received from this work was £20,966,000 (2008/09: £19,463,000).

Section 29: Additional audits undertaken with the consent of the Secretary of State. There was no work of this type carried out in 2009/10 or 2008/09.

Section 36: Studies designed to improve economy, efficiency and effectiveness, undertaken at the request of specified educational bodies. There was no work of this type carried out in 2009/10 or 2008/09.

The powers granted under section 35 of the Audit Commission Act 1998 have been extended by the following section of the Local Government and Public Involvement in Health Act 2007.

Paragraph 9 of Schedule 2A: income from advice and assistance work. Income received for this work was £1,750,000 (2008/09: £1,492,000).

(iv) Analysis of assets and liabilities
Current assets and liabilities are separated out into central government, NHS, local government, public corporations and external government analysis, shown in notes 14 and 17.

Under this disclosure, there is a realignment of some NHS and LG balances into the external to government category due to work carried out by external parties, for example, firms.

Note 3: Inspection income

Under the Local Government Act 1999 the Commission is responsible for the inspection of local authorities' compliance with the requirements of the Act.

Grants are available to the Commission for statutory inspection work, and in the period a number of grants were received, principally from Communities and Local Government (CLG).

	Year to 31 March 2010 £000	Year to 31 March 2009 £000
Fee income	**7,197**	11,810
Grant income		
CLG	**21,020**	19,212
CLG – Fire	**1,915**	2,094
CLG – Housing	**2,961**	3,617
Other departments	**2,120**	752
Total inspection income	**35,213**	37,485

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Note 4: Other operating income

This note provides a detailed analysis of the other operating income line in the statement of comprehensive income.

	Year to 31 March 2010 £000	Year to 31 March 2009 £000
Staff seconded out to other organisations	**495**	737
Rebates due under contractual agreements	**227**	300
Accommodation rental received	**803**	413
Costs recharged to the Commission pension scheme	**260**	228
Sundry income	**574**	398
Total other operating income	**2,359**	2,076

Note 5: Staff and commission members' costs

This note provides a detailed analysis of the staff and members' costs included in the statement of comprehensive income.

Staff and commission members' costs	**Year to 31 March 2010 £000**	Year to 31 March 2009 £000
Staff salaries[1]	**96,721**	86,080
Commissioners' remuneration	**270**	297
Social Security costs	**8,697**	8,113
Pension costs[2]	**19,243**	17,421
Cost of lease cars	**5,720**	5,222
Subscriptions and other benefits	**880**	861
Total staff and commission members' costs	**131,531**	117,994

Note 1: The staff salaries figure includes redundancy costs of £5,320,000 (2008/09: £625,000), and an increase in the cost of holiday entitlement not yet taken of £1,500,000. It also includes the costs of staff seconded to other organisations of £580,000 (2008/09: £751,000). Staff costs increased during the year due to the full year effect of cost of living awards calculated as a result of the three-year pay deal. The pay award on 1 April 2010 under the final year of the pay deal was 0.7% for staff earning less than £100,000.
Note 2: Pension cost figure includes a credit of £2,032,000 resulting from the application of IAS19 (2008/09: £417,000). This reduces the overall cost of staff salaries in both years. Employer's pension costs increased in line with salary costs.

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The average number of full-time-equivalent staff employed during the year, compared to last year, is set out in the table below.

Staff employed	**Year to 31 March 2010**	Year to 31 March 2009
Operational	**1,302**	1,290
Central Directorates	**681**	653
Secondees	**8**	11
Average number of staff employed in the year	**1,991**	1,954
In post at year end[1]	**1,985**	1,971

Note 1: 30 members of staff made redundant on 31 March 2010 are included in these figures. A further 45 will leave the Commission on 30 September 2010. Staff numbers increased mainly due to the expansion of the Commission's graduate auditor trainee scheme designed to reduce spending on contractors in future years.

Note 6: Bought-in services

This note analyses the bought-in services line in the statement of comprehensive income. These are services procured by the Commission to support the delivery of its audit, inspection and research functions. The expenditure in the year is summarised in the following table.

Cost of bought-in services	**Year to 31 March 2010 £000**	Year to 31 March 2009 £000
Payments to private accounting firms	**40,153**	43,914
Research and other consultancy costs	**3,336**	4,312
Audit and inspection contractors	**10,971**	9,702
Total cost of bought-in services	**54,460**	57,928

Contractors employed	**Year to 31 March 2010**	Year to 31 March 2009
Contractors – Average number in the year	**197**	190
Contractors – Number in post at year end	**187**	192

Note 7: Other operating costs

This note provides further analysis of the other operating costs line in the statement of comprehensive income, as set out in the table below.

Other operating costs		**Year to 31 March 2010 £000**	Year to 31 March 2009 Restated £000
Accommodation[1]	rent and lease costs	**4,558**	3,839
	other costs	**3,389**	2,984
Supplies and services		**9,592**	10,144
Depreciation and amortisation		**2,422**	1,860
Travel and subsistence	staff	**3,979**	4,595
	Commissioners	**20**	28
Recruitment and relocations		**915**	1,096
Training		**3,422**	3,627
Support contractor costs[2]		**5,265**	3,698
Audit fee[3]		**72**	78
Professional fees[4]		**1,006**	990
Publications[5]		**400**	368
Debts provided for		**6**	9
Total operating costs		**35,046**	33,316

Note 1: The main reason for the increase in rent and lease costs was rent reviews. Other accommodation costs increased due to asset disposal losses at a property vacated in Leeds and flood damage at Gateshead. The Commission is currently undertaking a strategic review of its property estate to make efficiency savings and plans to reduce significantly the estate overall.
Note 2: Support contractor costs increased mainly due to contractors working on several specialist projects during the year.
Note 3: The audit fee of £78,000 for 2008/09 includes £2,500 for non-audit services in respect of a review of restated IFRS-compliant financial statements. No non-audit services were provided in 2009/10.
Note 4: Professional fees relate mainly to property, legal and pensions advice.
Note 5: This is the printing cost of publications produced by the Commission. These costs are dependent on the number of reports produced.

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Note 8: Net investment return

This note provides information on interest received and paid in the year.

Net investment return	Year to 31 March 2010 £000	Year to 31 March 2009 £000
Interest receivable[1]	**416**	3,125
Impairment of cash deposits	**(32)**	(2,606)
Net investment return	**384**	519

Note 1: There is a significant reduction in interest receivable during 2009/10 due to a drop in interest rates between the financial years. The Commission's investment strategy is to minimise risk. With the exception of the two Icelandic bank deposits, all cash surplus to working capital requirements is deposited with HM Treasury's Debt Management Office.

Note 9: Financial instruments

Financial instruments held by the Commission comprise borrowings, cash and liquid resources, trade receivables and trade payables, all of which arise directly from its operations. Reserves and pension liabilities are also treated as financial instruments.

The main risks arising from these financial instruments are liquidity, interest rate and credit risks. The Board reviews and agrees policies for managing these risks and they are summarised below:

- Interest Rate Risk: to maintain a mixture of fixed and variable-rate deposits. Fixed-rate deposits are maintained to maximise interest receivable; variable-rate deposits for working capital requirements.
- Liquidity Risk: to ensure that current working capital requirements are immediately available, and to limit fixed-rate deposits to mature in no more than 6 months from the date of deposit. At the period end, the longest-dated deposit matures in May 2010. Short-term flexibility is achieved by overnight deposits and overdraft facilities.
- Credit Risk: cash investments are permitted with the HM Treasury's Debt Management Office or if unavailable, with named counterparties that have a short-term credit rating equal to P-1 (Moody) and A-1+ (Standard & Poor).

The Commission's policy and management of credit risk has been continually reviewed during 2009/10 in response to the ongoing unstable financial environment.

Heritable Bank

We have completed an impairment review on our Heritable asset in line with CIPFA's guidance, LAAP 82 Update 2. This has resulted in a write-back of £533,000 to the statement of comprehensive income. We expected this, as Heritable Bank have paid more than original estimates suggested.

Landsbanki

The Commission has also carried out an impairment review of its Landsbanki investment. We have decided to use a recovery rate of 89% in line with advice from the Commission's legal and technical accounting teams. This has resulted in an impairment of £477,000 to the statement of comprehensive income.

The following table shows three different scenarios based on three potential recovery rates – the recovery rate provided by CIPFA, the rate provided through internal advice as described above, and the rate which would apply should the Commission lose its priority status for payment by Landsbanki.

Recovery Rate	**94.85%**	**89.00%**	**38.21 %**
	(LAAP advice with a priority status)	(Internal advice based on priority status)	(LAAP advice based on non-priority status)
Recoverable amount	£3.7 million	£3.5 million	£1.5 million

The amount owed by Landsbanki was converted from British Sterling (GBP) into Icelandic Krona (ISK) on 22 April 2009 at a rate of 190.62 ISK/GBP following a change in Icelandic law. In line with accounting standards, the Commission has revalued the asset at 31 March 2010 at an exchange rate of 193.87 ISK/GBP. This has resulted in an uncrystallised exchange loss of £88,200 charged to the statement of comprehensive income.

The following table shows the sensitivity of changes to exchange rates if they were to increase or decrease.

Exchange Rate (ISK to GBP)	**195.00**	**193.87**	**192.00**
Impact on amount chargeable	£118,300	£88,200	£37,800

At the end of March 2010 the Commission held four deposits with the DMO in addition to those held with Landsbanki and Heritable.

With the exception of Landsbanki deposit, the Commission's policy is that no trading in financial instruments will be undertaken and that all deposits will be made in Sterling.

Less than 0.5% of the trade receivables balances (£16.692 million) are over 6 months old.

Note 10: Intangible assets

This note provides an analysis of the movements in the Commission's intangible assets as shown in the statement of financial position.

Cost	**Software £000**
At 1 April 2008	384
Purchases	507
Disposals	0
At 31 March 2009	**891**
Purchases	1,318
Disposals	0
At 31 March 2010	**2,209**
Amortisation	**0**
At 1 April 2008	123
Provided in period	241
Disposals	0
At 31 March 2009	**364**
Provided in year	665
Disposals	0
At 31 March 2010	**1,029**
Net book value	
At 31 March 2010	**1,180**
At 31 March 2009	527
At 31 March 2008	261

The net book value of assets using current value is not materially different from the net book value at historic cost. All assets are owned and none subject to lease agreements.

The Commission has reviewed its financial policies on software and as a result is now capitalising any software items valued over £5,000. We have restated our 2008/09 accounts in line with the new policy. This led to a reduction in revenue costs of £242,877.

Note 11: Plant and equipment

This note provides an analysis of the movements in the Commission's plant and equipment as shown in the statement of financial position.

	Furniture and fittings £000	Computer equipment £000	Office equipment £000	Total £000
Cost				
At 1 April 2008	10,729	1,774	509	13,012
Purchases	2,000	244	9	2,253
Disposals	(145)	(991)	(366)	(1,502)
At 31 March 2009	**12,584**	**1,027**	**152**	**13,763**
Purchases	1,392	859	7	2,258
Disposals	(2,424)	(355)	(106)	(2,885)
At 31 March 2010	**11,552**	**1,531**	**53**	**13,136**
Depreciation				
At 1 April 2008	4,670	1,082	402	6,154
Provided in period	1,167	384	67	1,618
Disposals	(92)	(991)	(355)	(1,438)
At 31 March 2009	**5,745**	**475**	**114**	**6,334**
Provided in year	1,312	427	18	1,757
Disposals	(1,397)	(355)	(106)	(1,858)
At 31 March 2010	**5,660**	**547**	**26**	**6,233**
Net book value				
At 31 March 2010	**5,892**	**984**	**27**	**6,903**
At 31 March 2009	6,839	552	38	7,429
At 31 March 2008	6,059	692	107	6,858

The net book value of assets using current value is not materially different from the net book value at historic cost. All assets are owned and none subject to lease agreements.

Note 12: Long-term receivables

This note shows the impaired value of deposit and accrued interest for two deposits made with Icelandic banks that are due for repayment after March 2011. During the current financial year Heritable Bank repaid a total of £1,779,232.

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Heritable Bank	**1,351**	2,828	0
Landsbanki Islands hf	**3,477**	4,042	0
Total long-term receivables	**4,828**	6,870	0

Note 13: Trade receivables and work in progress

This note provides an analysis of the trade receivables and work in progress line shown in the Commission's statement of financial position.

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Trade receivables			
– Local Government	**12,962**	19,358	16,303
– Health	**3,730**	4,813	3,063
Total receivables[1]	**16,692**	24,171	19,366
Work in progress			
– Local Government	**5,335**	4,017	5,647
– Health	**1,331**	2,154	2,012
Total work in progress	**6,666**	6,171	7,659
Total trade receivables and work in progress	**23,358**	30,342	27,025

Note 1: Trade receivables decreased significantly because of changes in billing arrangements for 2009/10.

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The following table shows the movement in the year on the irrecoverable and doubtful debt provision (netted against appropriate debtor).

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Opening provision	**9**	0	62
Released in the year	**(9)**	0	(62)
Provision made in the year	**15**	9	0
Closing provision	**15**	9	0

Note 14: Other receivables

This note provides an analysis of the other receivables line in the statement of financial position.

	31 March 2010 £000	31 March 2009 Restated £000	1 April 2008 Restated £000
Accommodation prepayments	**1,457**	2,406	2,429
Leased car prepayments	**1,566**	2,422	2,207
Other debtors and prepayments	**4,793**	2,156	4,104
Icelandic banks current debtors	**977**	746	0
Total other receivables	**8,793**	7,730	8,740

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The long-term receivables balances in note 12 and the current receivables and work in progress balances in notes 13 and 14, have been reanalysed as follows in line with the Whole of Government Accounts regulations:

Whole of Government Accounts receivable category	**31 March 2010** **£000**	31 March 2009 Restated £000	1 April 2008 Restated £000
Central government bodies	**8,270**	9,900	8,171
Local government bodies	**11,194**	11,907	12,671
NHS trusts	**3,284**	4,495	2,175
Balances with bodies external to government	**14,231**	18,640	12,748
Total WGA receivables	**36,979**	44,942	35,765

Note 15: Short-term investments, cash and cash equivalents

This note provides an analysis of the short-term investments, cash and cash equivalents line in the statement of financial position.

	31 March 2010 **£000**	31 March 2009 £000	1 April 2008 £000
Short-term investments	**47,000**	57,000	63,000
Cash and cash equivalents	**306**	(362)	(217)
Total short-term investments, cash and cash equivalents	**47,306**	56,638	62,783
Short-term investments (1 month and above)			
– maturing 3 months and above	**0**	10,000	13,000
– maturing in 1 – 3 months	**7,000**	31,000	10,000
– maturing within 1 month	**40,000**	16,000	40,000
Total short-term investments	**47,000**	57,000	63,000

Note 16: Trade and other payables

This note analyses the trade and other payables line in the statement of financial position.

	31 March 2010	31 March 2009 Restated	1 April 2008 Restated
	£000	£000	£000
Trade payables	**1,758**	2,516	2,659
Taxation and Social Security[1]	**3,801**	1,202	623
Accrual for holiday entitlement not yet taken[2]	**5,400**	3,892	3,219
Accruals[3]	**8,345**	4,143	5,435
Bank overdraft	**0**	362	217
Total trade and other payables	**19,304**	12,115	12,153

Note 1: Taxation and Social Security creditors are higher at 31 March 2010 because of timing differences.
Note 2: Accrual for holiday entitlement not yet taken has increased at 31 March 2010 due to a review of annual leave data as part of a human resources systems implementation during the year.
Note 3: Accruals at 31 March 2010 increased mainly because of an accrual for refunds to local government and police audited and inspected bodies approved by Board.

Note 17: Deferred income

Deferred income represents the invoices raised in advance for audit and inspection work.

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Deferred income	**38,926**	57,037	58,969

The payable and deferred income balances in notes 16 and 17 have been reanalysed as follows in line with the Whole of Government Accounts regulations.

	31 March 2010 £000	31 March 2009 Restated £000	1 April 2008 Restated £000
Central government bodies	12,491	17,814	9,045
Local government bodies	28,011	29,248	40,622
NHS trusts	8,017	6,373	9,437
Public Corporations	116	0	0
Balances with bodies external to government	9,595	15,717	12,018
Total WGA creditors and deferred income	**58,230**	69,152	71,122

Note 18: Current provisions

This note provides an analysis of the movement in the current provisions shown in the statement of financial position. These current provisions are for redundancy costs where individuals were notified before the year end and for dilapidations costs that are due to be released within the next 12 months.

	31 March 2010 £000	31 March 2009 £000	31 March 2008 £000
Opening balance	**736**	1,026	184
Reclassification of provisions	**(4)**	419	115
Utilised in the year	**(367)**	(1,026)	(184)
Provision in the year	**3,227**	317	911
Total current provisions	**3,592**	736	1,026

Note 19: Non-current provisions

This note provides an analysis of the movement in the non-current provisions shown in the statement of financial position. These non-current provisions are for future dilapidations costs which are released when the lease ends.

	31 March 2010 £000	31 March 2009 £000	31 March 2008 £000
Opening balance	**1,313**	1,590	1,193
Reclassification of provisions	**4**	(419)	(115)
Utilised in the year	**0**	(17)	0
Provision in year	**119**	159	512
Total non-current provisions	**1,436**	1,313	1,590

Note 20: Capital reserves

The Commission reclassified its capital reserves as general reserves during 2008/09.

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Local Government	**0**	0	1,580
Health	**0**	0	2,154
Total capital reserves	**0**	0	3,734

Note 21: Retained earnings: Local Government

Retained earnings show the net deficit or surplus for the year together with the cumulative amount brought forward from prior accounting periods. The following table shows the movements on the Local Government sector's share of the retained earnings during the year.

		Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000	Year to 31 March 2008 Restated £000
Brought forward		**32,705**	24,554	19,329
Reclassified from capital		**0**	1,580	0
Surplus/ (deficit) for year	2.5	**(5,547)**	9,900	14,767
Net movement to the pension scheme reserve		**(358)**	(3,329)	(9,542)
Local Government retained earnings		**26,800**	32,705	24,554

Note 22: Retained earnings: Health

Retained earnings show the net deficit or surplus for the year together with the cumulative amount brought forward from prior accounting periods. The following table shows the movements on the Health sector's share of the retained earnings during the year.

		Year to 31 March 2010 £000	Year to 31 March 2009 Restated £000	Year to 31 March 2008 Restated £000
Brought forward		**5,992**	3,859	3,046
Reclassified from capital		**0**	2,154	0
Surplus/ (deficit) for year	2.6	**(3,491)**	1,771	5,811
Net movement to the pension scheme reserve		**(191)**	(1,792)	(4,998)
Health retained earnings		**2,310**	5,992	3,859

Note 23: Pension reserve

The pension reserve shows the additional surplus or deficit experienced during the year resulting from the application of IAS19 together with the balance brought forward from prior accounting periods.

	31 March 2010 £000	31 March 2009 £000	31 March 2008 £000
Brought forward	**(3,466)**	(16,705)	(14,696)
Movement in the year from statement of comprehensive income	**(21,276)**	(12,684)	779
Cash payments to the scheme	**21,825**	17,805	13,762
Movement in the year from statement of changes in taxpayer's equity	**(103,504)**	8,118	(16,550)
Pension reserve	**(106,421)**	(3,466)	(16,705)

Note 24: Pension scheme

The following notes show that the net pension liability for the Commission increased from £3.4 million to £106.4 million over the year, despite positive asset returns. This is a position common across many companies in the UK and comes as a result of falling corporate bond yields and increases in expectations of future price inflation.

IAS19 requires the Commission to discount future benefits to current day values. The discount rate used is based on the yield available on high-quality corporate bonds. These yields increased in 2008/09 as a result of uncertainty around the credit crunch. However, they fell in 2009/10 to more historically normal levels as a result of returning market confidence. This means that future benefits are now discounted at a lower rate, resulting in a higher value of the scheme's liabilities.

Market expectations for future price inflation also increased in 2009/10 resulting in higher salary projections. This leads to a higher valuation of future benefits and a higher value for scheme liabilities.

These two factors are partly offset by a positive return on the scheme's assets. For example, the FTSE all-share price index increased by 50% over the year.

(i) Relationship between the reporting entity and the trustees
The Commission has a self-administered occupational pension scheme (the Audit Commission Pension Scheme) open to all permanent employees and employees who are on a fixed-term contract of two years or more. It is a defined benefit scheme partly funded by contributions from members

based on 6 per cent of pensionable salaries unless they participate in the salary sacrifice scheme (SMART pensions). No contributions are paid by those members who participate in the SMART pensions scheme, but the Commission pays an additional 6 per cent of those members' pensionable salaries into the scheme on their behalf. There is a reduction in notional salaries of 6% for staff participating in this scheme, so there is no additional cost to the Commission for these contributions. The Commission contributes the balance of the cost.

The pension assets are held in a separate trustee-administered fund to meet long-term pension liabilities to past and present employees. The trustees of the scheme are required to act in the best interest of the scheme's beneficiaries. The appointment of trustees to the scheme is determined by the scheme's trust documentation and legislation. Currently the scheme has nine trustees: four management nominated, four Member Nominated Trustees and an independent chair.

(ii) Future funding obligations in relation to defined benefit schemes
The most recently completed actuarial valuation of the scheme was performed by an independent actuary for the trustees of the scheme and was carried out as at 31 March 2008. Following the valuation the Commission's contributions remained at 17% of pensionable salaries (23% for members participating in SMART pensions).

The Commission's contributions amounted to £21.8 million in the 12 month period to 31 March 2010 (2008/09: £17.8 million). The levels of contributions are based on the current service costs and the expected future cash flows of the defined benefit scheme. The Commission estimates the duration of the scheme's liabilities is approximately 22 years.

(iii) How the liabilities arising from defined schemes are measured
The Commission provides retirement benefits to some of its former and approximately 97.5% of current employees through a defined benefit scheme. The level of retirement benefit is principally based on salary earned in the last year of employment.

The liabilities of the scheme are measured by discounting the best estimate of future cash flows to be paid out by the scheme using the projected unit method. This amount is reflected as a deficit in the statement of financial position. The projected unit method is an accrued benefits valuation method in which the scheme liabilities make allowance for projected earnings.

An alternative method of valuation to the projected unit method is a solvency basis, often estimated using the cost of buying out benefits at the statement of financial position date with a suitable insurer. This amount represents the amount that would be required to settle the scheme liabilities at the statement of financial position date rather than the Commission continuing to fund ongoing liabilities of the scheme. The Commission estimates the amount required to settle the scheme's liabilities at the statement of financial position date is £357 million.

(iv) Disclosure of principal assumptions

a) The Trustees' principal assumptions

Full actuarial valuations are conducted biennially (annually prior to 2006) and the last one finalised was carried out using the projected unit method as at 31 March 2008.

The market value of the net assets of the scheme at 31 March 2008 was £477 million which on the actuarially assessed value provided cover for 96 per cent of the benefits that had accrued to members after allowing for expected future increases in earnings. The principal financial assumptions used by the actuary and quoted in real terms relative to price inflation were:

	2008 % pa	**2006 % pa**
Rate of interest	Term dependent 4.0% at 5 years duration 3.2% at 20 years duration 2.8% at 40 years duration	2.1
Rate of salary increase	**0.75**	0.75

b) The Commission's principal assumptions

Under the accounting standard IAS19 (Employee Benefits), the principal financial assumptions used by the actuary will be as follows:

	2010 % pa	2009 % pa	2008 % pa	2007 % pa
Rate of inflation	**3.8**	3.3	3.4	3.1
Rate of salary increase[1]	**4.45**	3.95	4.05	3.75
Discount rate for liabilities	**5.6**	6.6	6.3	5.3
Rate of increase of pensions in payment	**3.8**	3.3	3.4	3.1
Rate of increase of deferred pensions	**3.8**	3.3	3.4	3.1

Note 1: The salary escalation includes an additional age-related promotional salary scale.

The post-retirement mortality tables used in 2010 are PA00 Year of Birth tables. The table also includes an allowance for improvements to anticipated life expectancy. This is expected to continue to rise in line with the higher rates observed over the last 30 years for the longer term (up to 2040) with future improvements then tailing off. The assumed life expectancies on retirement at age 60 are as follows:

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	2010	2009	2008
Retiring today			
Males	**28**	28	28
Females	**31**	31	31
Retiring in 20 years			
Males	**30**	29	29
Females	**32**	32	32

The expected return on the scheme assets is calculated from assumptions of long-term expected returns by asset class, as follows:

	2010	2009	2008
Equities and diversified growth funds	**7.65%**	7.15%	7.65%
Property	**5.55%**	5.05%	5.55%
Corporate bonds	**5.6%**	6.6%	n/a
Gilts and liability-driven investment funds	**4.55%**	4.05%	n/a
Cash	**0.5%**	0.5%	5.25%
Assets taken at	**bid value**	bid value	bid value

Sensitivity analysis of the principal assumptions used to measure scheme liabilities
The sensitivities regarding the principal assumptions used to measure the scheme liabilities are set out below.

Assumption	Change in assumption	Impact on scheme liabilities
Discount rate	Decrease by 0.5%	Increase by 11%
Rate of inflation	Increase by 0.5%	Increase by 8%
Rate of salary growth	Increase by 0.5%	Increase by 3%
Rate of mortality	Mortality table rated down by one year	Increase by 2%

(v) Nature and extent of the risks arising from financial instruments held by the defined benefit scheme

At 31 March 2010, the scheme assets were invested in a portfolio that consisted primarily of diversified growth and property securities. The fair value of the scheme assets as a percentage of total scheme assets is detailed below.

	2010	2009	2008
UK equities	**0%**	2%	52%
Overseas equities	**0%**	2%	41%
Diversified growth funds	**84%**	67%	0%
Property	**4%**	4%	6%
Corporate Bonds	**0%**	8%	0%
Liability-driven investment funds	**9%**	12%	0%
Cash	**3%**	5%	1%

Following an asset liability review carried out in 2007 and subsequent discussions between the Commission and the trustees, the current investment strategy is detailed below.
Portfolios of growth assets and cash assets are as follows:

- growth assets are held in diversified growth funds (investing in UK and overseas equities together with a range of alternative asset classes) and pooled property funds. The majority of the growth portfolio is held in diversified growth funds (in order to reduce funding level volatility without compromising on expected returns). The scheme also holds (for historical reasons) some pooled property funds; and
- cash assets are held within a liability-driven investment portfolio backing the hedge of around 80 per cent of the interest rate and inflation risk within the scheme's liabilities.

Assuming the scheme is fully funded, the long-term aim is to invest around 10 per cent of assets within the liability-driven investment portfolio (to meet collateral requirements) with the remaining 90 per cent invested in growth assets. The actual proportions vary from time to time depending on short-term collateral requirements and the extent to which the scheme's assets may vary in relation to the liabilities. Growth assets are liquidated as necessary to provide a prudent level of liquidity necessary for the liability-driven investment manager to maintain the Swap Fund investments.

(vi) Net pension assets

This note provides a high-level summary of the net pension liability for the year.

		31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Fair values of scheme assets	viii	**607,138**	473,872	476,866
Present value of scheme liabilities	vii	**(713,559)**	(477,338)	(493,571)
Net pension liability		**(106,421)**	(3,466)	(16,705)

(vii) Reconciliation of present value of liabilities

This note provides an analysis of the change in the year of the present value of scheme liabilities summarised in the table in Note 24 (vi).

		Year to 31 March 2010 £000	Year to 31 March 2009 £000	Year to 31 March 2008 £000
Opening present value of defined benefit liability		**477,338**	493,571	531,388
Net operating charge to the Commission	ix	**19,227**	17,388	17,424
Interest cost	x	**31,700**	31,202	27,247
Employee contributions[1]		**99**	1,782	5,562
Actuarial losses	xi	**197,923**	(50,841)	(52,134)
Benefits paid		**(13,294)**	(15,764)	(10,453)
Past service cost	viii/ ix	**566**	0	(25,463)
Closing defined benefit liability	vi	**713,559**	477,338	493,571

Note 1: The reduction in employee contributions is due to the full year effect of employees making contributions under SMART pension arrangement from 1 August 2008. Under this arrangement employees agree to give up an agreed percentage of their pay and an equivalent amount is paid into the pension scheme as an employer contribution.

(viii) Reconciliation of fair value of scheme assets

This note provides an analysis of the change in the year in the fair value of the schemes assets summarised in Note 24 (vi).

		Year to 31 March 2010 £000	Year to 31 March 2009 £000	Year to 31 March 2008 £000
Opening fair value of scheme assets		**473,872**	476,866	516,692
Expected return on scheme assets	x	**30,217**	35,906	39,687
Actuarial gains/ (losses)	xi	**94,419**	(42,723)	(68,684)
Contributions by employer		**21,825**	17,805	13,762
Contributions by employees		**99**	1,782	5,562
Benefits paid		**(13,294)**	(15,764)	(10,453)
Settlements		**0**	0	(19,700)
Closing fair value of scheme assets	vi	**607,138**	473,872	476,866

Based on the current contribution rate of 23 per cent of pensionable salaries for SMART pension members and 17 per cent of pensionable salaries for non-SMART pension members, the Commission expects to contribute £21.5 million in cash contributions to the scheme in 2010/11.

(ix) Analysis of the operating charge for the year

This note provides an analysis of the operating charge for the pension scheme for the year as calculated by using IAS19.

		Year to 31 March 2010 £000	Year to 31 March 2009 £000	Year to 31 March 2008 £000
Current service costs	vii	**19,227**	17,388	17,424
Gains on settlements	vii	**566**	0	(5,763)
Total operating charge		**19,793**	17,388	11,661

The contribution due from the Commission as calculated above is shown in the staff and members' costs line in the statement of comprehensive income. This operating charge includes a credit of £2,032,000 (2008/09 £417,000) as a result of the application of IAS19.

(x) Analysis of amount credited to other finance income

This note analyses the surplus/ (deficit) arising from the IAS19 calculation of the value of pension assets. The surplus/ (deficit) is taken into the statement of comprehensive income.

	Year to 31 March 2010 £000	Year to 31 March 2009 £000	Year to 31 March 2008 £000
Expected return on pension scheme assets	**30,217**	35,906	39,687
Interest cost	**(31,700)**	(31,202)	(27,247)
Net return	**(1,483)**	4,704	12,440

(xi) Analysis of amount recognised in statement of taxpayers equity

This note provides an analysis of the net gain in the pension scheme assets and liabilities due to the IAS19 revaluation shown in the statement of taxpayer's equity. The table below includes the total of recognised gains from previous financial years and the gain in the current financial year.

		Year to 31 March 2010 £000	Year to 31 March 2009 £000	Year to 31 March 2008 £000
Opening amount recognised		**18,372**	10,254	26,804
Gains and losses in the year				
Actual return less expected return on scheme assets	viii	**94,419**	(42,723)	(68,684)
Experience gains/ (losses) arising on the scheme liabilities	vii	**(27,995)**	14,454	(6,496)
Changes in demographic and financial assumptions underlying scheme liabilities	vii	**(169,928)**	36,387	58,630
Net gain/ (loss) in the year		**(103,504)**	8,118	(16,550)
Closing amount recognised		**(85,132)**	18,372	10,254

(xii) Pension scheme performance information

Key financial data for the pension scheme for the year and the previous four financial years is shown below. The deficit in the current year is larger than in previous years due to market performance.

	31 March 2010 £000	31 March 2009 £000	31 March 2008 £000	31 March 2007 £000
Scheme liabilities note (vi)	**(713,559)**	(477,338)	(493,571)	(531,388)
Scheme assets note (vi)	**607,138**	473,872	476,866	516,692
Deficit	**(106,421)**	(3,466)	(16,705)	(14,696)
Actual returns less expected returns on assets	**94,419**	(42,723)	(68,684)	8,741
As a percentage of scheme assets	**15.6%**	(9.0%)	(14.4%)	1.7%

Note 25: Operating results for the last four periods

This note provides a high-level overview of the Commission's financial performance. The Commission's operating costs increased by £11.8 million or 5.6 per cent compared to 2008/09 at a time when operating income reduced by £2.6 million or 1.2 per cent.

	Year to 31 March 2010 £m	Year to 31 March 2009 Restated £m	Year to 31 March 2008 £m	Year to 31 March 2007 £m
Operating income	**213.1**	215.7	219.7	223.6
Operating costs	**(221.0)**	(209.2)	(215.3)	(228.3)
Notional capital (costs)/ credits	**0.7**	(0.9)	(0.5)	0.1
Operating surplus/ (deficit)	**(7.2)**	5.6	3.9	(4.6)
% of operating surplus/ (deficit) to operating income	**(3.4%)**	2.6%	1.8%	(2.1%)

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Note 26: Commitments under leases

i) As at 31 March 2010 there are annual commitments to pay property rentals under lease agreements during the following year, within two to five years, and after five years as follows:

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Within 1 year	**3,899**	3,852	3,542
Within 2 to 5 years	**13,100**	13,691	12,544
Over 5 years	**12,637**	14,519	19,121
Total buildings	**29,636**	32,062	35,207

Actual property lease expenditure for the year up to March 2010 amounted to £3,697,611.

ii) As at 31 March 2010 there were annual commitments to pay rentals in respect of non-cancellable car and photocopier leases during the following year and within two to five years as follows:

	31 March 2010 £000	31 March 2009 £000	1 April 2008 £000
Within 1 year	**2,750**	2,749	2,931
Within 2 to 5 years	**3,571**	3,674	3,076
Total cars and photocopiers	**6,321**	6,423	6,007

Actual car and photocopier lease expenditure for the year up to 31 March 2010 amounted to £3,382,669.

iii) All building leases are taken out in the name of the Audit Commission. Office accommodation with spare capacity is sublet, with the majority of building leases subject to rent reviews. Commitments under non-cancellable operating leases to receive rentals during the year and, within two to five years following the year of these accounts, are shown in the table below.

Lease Receipts	**31 March 2010 £000**	31 March 2009 £000	1 April 2008 £000
Obligations to receive rentals under operating subleases comprise:			
Within 1 year	**974**	668	390
Within 2 to 5 years	**3,505**	3,200	34
Over 5 years	**2,921**	3,200	0
Total lease rental receipts	**7,400**	7,068	424

Actual lease receipts for the year up to 31 March 2010 amounted to £802,804.

Note 27: Contingent liabilities

The Commission indemnifies appointed auditors against costs incurred by them in connection with Court proceedings arising through their exercise of special legal functions. In addition, costs may be awarded against auditors in such proceedings which fall to be borne by the Commission under the terms of the indemnity. Amounts incurred in any one year, as a result of this indemnity, depend upon the progress of individual cases and cannot, therefore, be predicted or quantified until they crystallise.

The Commission received an initial ruling from HM Revenue and Customs (HMRC) that its best value inspections are not business activities for VAT purposes. If this changes it would create a liability estimated to be £1.3 million. The Commission actively continues to seek a final ruling from HMRC.

Counsel's advice is the Commission should not charge VAT on data matching work, nor recover VAT on costs incurred in relation to this work. If this were to take effect, the annual additional cost is estimated to be less than £0.1 million, although this could be applied retrospectively for work carried out since July 2008. We have asked HMRC to confirm the correct VAT treatment for this work.

The Commission continues to discuss its liability for Corporation Tax with HMRC. Consultation with the Commission's legal Counsel has highlighted that HMRC considers interest received on cash deposits and investments subject to Corporation Tax. Assuming other current arrangements for Corporation Tax remain unchanged, we estimate the liability at 31 March 2010 to be £0.4 million. HMRC has confirmed that any liability will be calculated from 1 January 2009.

The Commission awaits the findings of an external review of its employment taxation arrangements. Although the initial draft of the report did not highlight any new risks, it has highlighted areas where policies and procedures could be improved to reduce potential challenge by HMRC. This information will help us to review the level of provision we will need to make in the future, but we estimate a liability of £180,000 as at 31 March 2010.

The Commission has one £5.0 million deposit with Landsbanki Islands hf. Although the deposit and accrued interest have been impaired (see notes 8 and 9), there remains some uncertainty as to the final amount that will be repayable. Heritable bank has started to repay the Commission's £5.0 million deposit in line with the schedule.

The Commission currently has three ongoing litigation cases. In the event that we are required to pay costs, the total estimate is £378,000.

The continuing restructure of the Commission may lead to further redundancy costs estimated on 31 March 2010 at £298,000. These have not been provided for in the year.

Note 28: Related party transactions

The related party disclosures given below meet the requirements of International Accounting Standard 24. Disclosure relates to key management personnel of the Commission, or their close family members, who are in a position of significant influence resulting from being elected to, receiving remuneration from, or being appointed to any organisation:

- where the Commission appoints the auditor or inspects the body;
- where there are specific statutory responsibilities to cooperate, for example, the Care Quality Commission;
- that is a central government department; and
- that is a provider or receiver of significant services to or from the Commission.

Related party relationships for Commissioners are disclosed on page 12. Details of material transactions with these related parties, and any relating to other key management personnel of the Commission, are provided below.

Transactions with related parties
Such transactions are all carried out on an arm's-length basis and are conducted on normal commercial terms. No amounts were written off or forgiven during the year and outstanding balances were settled under normal trading terms.

Commissioners

- **Michael O'Higgins** is a Non-Executive Director of HM Treasury and Chair of the Treasury Audit Group Committee. During the year transactions for services provided by HM Treasury to the Commission amounted to £6,090 (2008/09: £45,035). There was no balance due to HM Treasury at 31 March 2010.

- **Merrick Cockell** is a Member of the Royal Borough of Kensington and Chelsea. He was appointed as a Commissioner on 13 July 2009, and from that date until the year end, transactions for services provided by the Commission to the Borough amounted to £353,183 (2008/09: n/a). The balance due to the Commission at 31 March 2010 was £75,251.
- **Jim Coulter and Sheila Drew Smith** are Board Members of the Tenant Services Authority. During the year transactions for services provided by the Commission to the Authority amounted to £79,818 (2008/09: nil). There was no balance due to the Commission at 31 March 2010.
- **Stephen Houghton** is a Member of Barnsley Metropolitan Borough Council. During the year transactions for services provided by the Commission to the Council amounted to £473,395 (2008/09: £563,901). The balance due to the Commission at 31 March 2010 was £92,018. Stephen is also a Peer Member of the Improvement and Development Agency, and during the year transactions for services provided by the Agency to the Commission amounted to £138,870 (2008/09: £108,863).There was no balance due to the Agency at 31 March 2010.
- **Denise Platt** is an Independent Review Board Member of Cheshire Fire and Rescue Service. During the year transactions for services provided by the Commission to the Service amounted to £59,598 (2008/09: £92,471). The balance due to the Commission at 31 March 2010 was £6,525.
- **Chris White** is a Member of Hertfordshire County Council. During the year transactions for services provided by the Commission to the Council amounted to £514,058 (2008/09: £398,159). The balance due to the Commission at 31 March 2010 was £35,674. Chris White is also a Member of St Albans City and District Council, to which transactions for services provided by the Commission amounted to £125,432 (2008/09: £217,421). The balance due to the Commission at 31 March 2010 from this Council was £22,417.

Management Team

- **Eugene Sullivan** was a Non-Executive Director on CIPFA Commercial Services Board during the year until 30 September 2009. During this period transactions for services provided by the Commission to the CIPFA amounted to £51,262 (2008/09 year: £122,296). There was no balance due to the Commission at 31 March 2010. Transactions for services provided by CIPFA to the Commission during the period amounted to £645,185 (2008/09 year: £985,520). The balance due to CIPFA at 31 March 2010 was £174,805.
- **Martin Evans** is a member of the Audit and Risk Committee of the Department for Communities and Local Government (CLG). Details of transactions with the CLG are given below.
- **David Walker's** brother is the Chief Executive of Broxbourne Borough Council. During the year transactions for services provided by the Commission to the Council amounted to £166,642 (2008/09 from date of appointment, 6 October 2008: £107,529). The balance due to the Commission at 31 March 2010 was £2,372.

Regional Director

- **Jo Whitehead's** husband is a member of the Professional Executive Committee of Bristol Primary Care Trust. During the year transactions for services provided by the Commission to the Trust amounted to £43,845 (2008/09: £38,537). There was no balance due to the Commission at 31 March 2010.

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Other related parties
The Commission is a public corporation sponsored in the year by the CLG. During the year, amounts invoiced to CLG for services provided by the Commission to, or on behalf of CLG, amounted to £26.3 million (2008/09: £18.6 million). The balance due to the Commission at 31 March 2010 was £3.7 million. Amounts invoiced to the Commission by CLG during the year amounted to £7,518 (2008/09: £10,540). There was no balance due to CLG at 31 March 2010.

Compensation of key management personnel
IAS24 also requires the disclosure, in aggregate, of the compensation of key management personnel and these details are set out below. These positions have influence over decision making within the Commission.

	Short-term benefits (salary and taxable benefits) £000	Post-employment benefits (pension contributions) £000	Total year to 31 March 2010 £000	Total year to 31 March 2009 £000
Commissioners	270	0	270	297
Management Team	1,275	356	1,631	1,515
Regional Directors	541	126	667	611
Total compensation	**2,086**	**482**	**2,568**	**2,423**

Note 29: Losses and special payments

There were no cases of losses or special payments made in the year.

Note 30: First-time adoption of IFRS

The first-time adoption of IFRS has not changed total equity or net expenditure as previously reported under UK GAAP.

Note 31: Post-statement of financial position events

The new government published "The Coalition: our programme for government" on 20 May 2010. Comprehensive Area Assessment (CAA) will end and inspection will reduce further. While waiting for more detail following discussion with CLG officials, the Commission decided to cease CAA work with immediate effect on 21 May 2010. The Commission continues to work with the government and other inspectorates on a plan to meet the government's objectives of increasing accountability for local public services through more transparency and less inspection. The Commission has started to review its strategic, management and financial plans in response to the government's changing policy agenda.

The Commission's financial statements are laid before the Houses of Parliament by the Secretary of State for Communities and Local Government. International Accounting Standard 10 requires the Commission to disclose the date on which the accounts are authorised for issue. This is the date on which the certified accounts are dispatched by the Commission to the Secretary of State for Communities and Local Government.

The authorised date for issue is 14 July 2010.

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Appendix 1

The Audit Commission for Local Authorities and the National Health Service in England

Accounts direction given by the Secretary of State for Communities and Local Government and the Secretary of State for Health with the consent of the Treasury, in accordance with paragraph 11(1) of Schedule 1 to the Audit Commission Act 1998.

1 The annual financial statements of the Audit Commission for Local Authorities and the National Health Service in England (hereafter in this accounts direction referred to as “the Commission”) shall give a true and fair view of the income and expenditure and cash flows for the financial year and the state of affairs at the year end. Subject to this requirement, the financial statements for 2009/10 and for subsequent years shall be prepared in accordance with:

a. the accounting and disclosure requirements of the Companies Act;
b. International Financial Reporting Standards;
c. any guidance that the Treasury may issue from time to time in respect of the financial statements of public corporations; and
d. any other specific disclosure requirements of the Secretaries of State;

insofar as these requirements are appropriate to the Commission and are in force for the year for which the financial statements are prepared, and except where agreed otherwise with the Secretaries of State and the Treasury, in which case the exception shall be described in the notes to the financial statements.

2 Schedule 1 to this direction gives additional disclosure requirements of the Secretaries of State.

3 This direction shall be reproduced as an appendix to the financial statements.

4 This direction replaces all previously issued directions.

Signed by authority of the Secretary of State for Communities and Local Government

Paul Rowsell

A Senior Civil Servant in the Department For Communities and Local Government
24 June 2010

Signed by authority of the Secretary of State for Health

Stephen Mitchell

A Senior Civil Servant in the Department of Health
2 July 2010

Schedule 1

Additional disclosure requirements

The following information shall be disclosed in the financial statements, as a minimum, and in addition to the information required to be disclosed by paragraph 1 of this direction.

1 The income and expenditure account or the notes thereto

a. The following income:
   (i) fees; and
   (ii) other income.

b. The following expenditure:
   (i) audit fees to private firms;
   (ii) contract audit assistance for the Commission's regional operations;
   (iii) other amounts payable to private accountancy firms; and
   (iv) debts written off and movements in provisions for bad and doubtful debts.

2 The notes to the financial statements

a. For each of the following categories of business, an analysis of income between that generated from work carried out by the Commission and that generated from work carried out by private accountancy firms:
   (i) local government audits;
   (ii) local government inspections;
   (iii) National Health Service audits; and
   (iv) National Health Service inspections.

b. For work carried out under each of the following sections in the Audit Commission Act 1998 (items i to iii) and Local Government and Public Involvement in Health Act 2007 (item iv), a statement showing the income and expenditure for the year:
   (i) section 28 (certification of claims, returns etc.);
   (ii) section 29 (agreed audit of accounts);
   (iii) section 36 (studies at request of educational bodies); and
   (iv) paragraph 9 of Schedule 2A (advice and assistance work).

c. For each of the following categories of business, a statement showing the opening income and expenditure reserve, income and expenditure for the year and the closing income and expenditure reserve.
   (i) Local Government authorities; and
   (ii) Health Service authorities.

d. Details of employees, other than Commission members, showing:
   (i) the average number of persons employed during the year, including part-time employees and secondees, analysed between appropriate categories;
   (ii) the total amount of loans to employees;
   (iii) employee costs during the year, showing separately:
      a wages and salaries;
      b early retirement costs;
      c social security costs;
      d contributions to pension schemes;
      e payments for unfunded pensions; and
      f other pension costs.

e. In the note on receivables, prepayments and payments on account shall each be identified separately.

f. Particulars, as required by the accounting standard on related party disclosures, of material transactions during the year and outstanding balances at the year end (other than those arising from a contract of service or of employment with the Commission), between the Commission and a party that, at any time during the year, was a related party. For this purpose, notwithstanding anything in the accounting standard, the following assumptions shall be made:
   (i) transactions and balances of £5,000 and below are not material;
   (ii) parties related to board members and key managers are as notified to the Commission by each individual board member or key manager;
   (iii) the following are related parties:
      a subsidiary and associate companies of the Commission;
      b pensions funds for the benefit of employees of the Commission or its subsidiary companies (although there is no requirement to disclose details of contributions to such funds);
      c board members and key managers of the Commission;
      d members of the close family of board members and key managers;
      e companies in which a board member or a key manager is a director;
      f partnerships and joint ventures in which a board member or a key manager is a partner or venturer;
      g trusts, friendly societies and industrial and provident societies in which a board member or a key manager is a trustee or committee member;
      h companies, and subsidiaries of companies, in which a board member or a key manager has a controlling interest;
      i settlements in which a board member or a key manager is a settlor or beneficiary;
      j companies, and subsidiaries of companies, in which a member of the close family of a board member or of a key manager has a controlling interest;

k partnerships and joint ventures in which a member of the close family of a board member or of a key manager is a partner or venturer;

l settlements in which a member of the close family of a board member or of a key manager is a settlor or beneficiary; and

m the Department for Communities and Local Government, as the sponsor department for the Commission.

For the purposes of this sub-paragraph:

(i) A key manager means a member of the Commission's management board.

(ii) The close family of an individual is the individual's spouse, the individual's relatives and their spouses, and relatives of the individual's spouse. For the purposes of this definition, "spouse" includes personal partners, and "relatives" means brothers, sisters, ancestors, lineal descendants and adopted children.

(iii) A controlling shareholder of a company is an individual (or an individual acting jointly with other persons by agreement) who is entitled to exercise (or control the exercise of) 30% or more of the rights to vote at general meetings of the company, or who is able to control the appointment of directors who are then able to exercise a majority of votes at board meetings of the company.

g. A statement of losses and special payments during the year, being transactions of a type which Parliament cannot be supposed to have contemplated. Disclosure shall be made of the total of losses and special payments if this exceeds £250,000, with separate disclosure and particulars of any individual amounts in excess of £250,000. Disclosure shall also be made of any loss or special payment of £250,000 and below if it is considered material in the context of the Commission's operations.

Note to paragraph 2(f) of Schedule 1: under the Data Protection Act 1998 individuals need to give their consent for some of the information in these sub-paragraphs to be disclosed. If consent is withheld, this should be stated next to the name of the individual.

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Our history and statutory background

The Audit Commission for Local Authorities in England and Wales (the Commission) was established on 21 January 1983 by the Local Government Finance Act 1982. The Commission is a public corporation and began operations on 1 April 1983.

On 1 October 1990 the Commission assumed responsibility for the external audit of the National Health Service and its name was changed to the Audit Commission for Local Authorities and the National Health Service in England and Wales. A consolidating Act, the Audit Commission Act 1998, was given Royal Assent in June 1998 bringing the earlier statutory provisions together into one document.

Since 1998, a number of important amendments to the Commission's functions have been made by various statutes.

The Commission's powers were extended by the Local Government Act 1999 to include inspection of best value authorities, and by the Local Government Act 2003 to include inspection of registered social landlords. The Local Government Act 2003 also conferred on the Commission express powers to undertake comprehensive performance assessment of local authorities. The Health and Social Care (Community Health and Standards) Act 2003 provided that a foundation trust may appoint an officer of the Commission as its auditor with the agreement of the Commission. This provision is now to be found in the National Health Service Act 2006. In 2005 the Commission's remit was extended to the appointment of auditors to English National Health Service charities by a new provision inserted into the Charities Act 1993.

The Commission's inspection functions were extended by the Fire and Rescue Services Act 2004 to cover fire and rescue authorities' compliance with the Fire and Rescue National Framework. The remit of the Commission in respect of Wales was transferred to the Auditor General for Wales by virtue of the Public Audit (Wales) Act 2004. The words 'and Wales' were removed from the Commission's name in 2008.

The Commission was given an express statutory power to conduct data matching exercises by the Serious Crime Act 2007. The Local Government and Public Involvement in Health Act 2007 transferred the Benefit Fraud Inspectorate to the Commission, and gave the Commission a new power to provide advice and assistance to other public bodies. The 2007 Act also conferred on the Commission a power to report on the performance of English local authorities in support of its programme of comprehensive area assessment. The Housing and Regeneration Act 2008 replaced registered social landlords with registered providers of social housing, and conferred on the Commission power to inspect them at the request of the Tenant Services Authority.

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