



National Audit Office

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Dear Chris,

REVIEW OF MPS' EXPENSES: WRITTEN EVIDENCE FROM THE COMPTROLLER AND AUDITOR GENERAL TO THE COMMITTEE ON STANDARDS IN PUBLIC LIFE

1. It was a pleasure to meet you again on 5 May to learn more about your review of MPs' expenses. At our meeting I agreed to give you written evidence for your inquiry, in my capacity as the Comptroller and Auditor General and external auditor of the House of Commons, and I am pleased to provide this here.
2. Any revised system for MPs' expenses needs to be founded on principles of transparency, independence, accountability, value for money to the tax payer and probity, if it is to both support MPs adequately and command public respect. External audit has an important role to play in sustaining these principles and is the focus of my submission to you. Specifically, I have outlined the attributes the system will need to have if it is to be fully auditable.
3. To facilitate effective and efficient audit, a future expenses system must have clear rules; produce and preserve sufficient and appropriate evidence to provide reasonable assurance as to the legitimacy of the transactions; be vigorously and consistently administered; and be supported by a robust governance framework that promotes compliance with the rules.

Framework of rules

4. As well as providing an opinion on whether accounts are "true and fair", auditors of public sector accounts are required to form an audit opinion on the "regularity" of the transactions recorded in the accounts. If a transaction is "regular", it means that the sums involved have been applied to the purposes intended by Parliament and that they conform to the authorities and rules that govern them.
5. To obtain audit assurance over the regularity of paid expense claims, auditors need to test them against the rules that pertained at the time the claim was made. Indistinct rules, such as those that have been in place in relation to an MP's designation of his or her main and second home and the costs claimable as a result of this designation, are open to wide ranging interpretation. In such cases, the criteria as to where the boundaries of acceptability for reimbursement lie are blurred, both for the users and administrators of the system, and its auditors. In these cases many different and, perhaps unintended, types of expenditure can be said to fall "within the rules".



6. To address this difficulty, the new system for MPs' expenses needs to have clear, documented rules specifying how much and what may and may not be claimed. There must also be a facility for the authoritative resolution of the unavoidable ambiguities that will arise.

#### Audit evidence

7. So that they can form their opinion on a set of accounts, auditors need to obtain sufficient and appropriate audit evidence to confirm the amount and regularity of the reported transactions and balances.
8. Audit evidence takes many forms. At a simple level, a receipt, contract or travel ticket usually provides good evidence to support both the amount claimed as well as its stated purpose. But these forms of evidence may not always provide persuasive evidence that the amount claimed by an MP relates to costs actually and necessarily incurred by him or her in the performance of his or her Parliamentary duties. Some of the current and past evidential requirements of the MPs' expenses system, such as the need for a receipt for the purchase of furnishings for an MP's second home, a staff contract, a car mileage claim or taxi receipt, often provide limited and in some cases no proof, that the expense was incurred on Parliamentary or constituency business, rather than on private or party business. In the wider public sector or the private sector, obtaining proof of the purpose of a claim is more straightforward because any claims are routinely counter-signed or authorised in some other way, by a claimant's manager, providing good evidence in support of the business purpose of the expense claimed.
9. Where receipts or contracts do not in themselves provide sufficient and appropriate audit evidence, it may be possible to supplement this evidence, for example, using analytical techniques to predict expected cost ranges and compare claim values to an expected average. In some cases, however, including an MP's nomination of his or her main and second home, no other evidence beyond an MP's declaration may be realistically or readily available.
10. To facilitate effective and efficient future audit, the rules governing the MPs' expenses system should specify the evidence that MPs must supply to justify their claim before it is reimbursed. Crucially, this evidence must be sufficient and appropriate to provide reasonable assurance of the legitimacy of purpose of the claim, as well as its amount and nature. This evidence must be retained so that the auditor may review it.

#### Administration

11. The requirement for the C&AG to examine 100 per cent of transactions recorded in a set of accounts ceased under the Exchequer and Audit Departments Act 1921. The C&AG's audit approach has evolved since then and has, for many years now, been fully compliant with International Standards on Auditing. Effective and efficient audit is now risk based and, while part of the audit assurance needed must still come from substantive testing, such as auditing a sample of individual transactions, the auditor anticipates obtaining some of the audit assurance needed by confirming the effective operation of management's controls designed to promote and provide evidence of compliance with the rules and prevent or detect erroneous or irregular transactions. Where management's administration is not robust and effective management controls are not in operation, the audit is rendered less effective and less efficient.
12. The indistinct rules and scope for their inconsistent interpretation by administrative staff, the self-regulated / self-certifying basis of the current system for MPs' expenses, along with, until recently, fairly limited receipting requirements, has restricted management's ability to put in

place administrative systems supported by effective internal control systems. As a result, the scope of assurance which the auditor has been able to obtain from management's controls has been restricted.

13. If the future administrative and internal control systems for MPs expenses are to support effective and efficient audit there must be robust, cost effective and proportionate management controls and processes designed to ensure compliance with those rules.

#### Governance

14. Difficulties arise with the current governance framework because those who have determined the system of MPs' expenses and resolved disputed cases are also beneficiaries of that system. In addition, the House Services who establish and maintain the administrative and control framework around the processing of claims for payment, do not have the final say in the design of that system, nor the ultimate authority to adjudicate on the appropriateness of a claim submitted by a Member under the approved rules. This arrangement limits the ability of staff at the Department of Resources (the "Fees Office") to enforce the rules and challenge or reject claims.
15. An effective governance framework would develop and maintain an effective framework of rules, promote compliance with those rules and support management's development of robust administration and control systems that are able to enforce those rules. It would also provide for independent adjudication of disputed cases, while not undermining management's overall control framework. This Committee's independent Review and the recent proposal brought forward by the Leader of the House for the establishment of an independent Parliamentary Standards Authority (PSA), provide an opportunity to address these concerns and strengthen the overall governance and policing arrangements.

#### Audit arrangements

16. The shortcomings of the past and current systems have hampered effective audit of MPs' expense claims over the years, and, in particular, the availability of evidence to support the regularity of those claims. The scope of the audit engagement or remit for the Members Estimate Resource Account has therefore been limited. In forming an audit opinion in respect of MPs' claims I have been asked to consider only:

- whether payments were supported by a Member's claims form;
- whether the purpose of the expenditure stated on the claims met that of the relevant allowance; and
- whether the House of Commons' Service (i.e. Department of Resources - the "Fees Office") had properly accounted for these claims.

I set out details of this limitation in my audit certificate.

17. In recent years, incremental reforms to the system of MPs' expenses, including the reduction in the receipting threshold (£25 from 1 April 2008, recently reduced to £0), have resulted in improvements to the quantity and quality of audit evidence available. As a result, in April 2008, I proposed, in evidence to the Members Estimate Audit Committee, a sub group of the Members Estimate Committee, that the restriction on the scope of my audit engagement should be removed. The House accepted the Audit Committee's recommendations to that effect on 22 January 2009. The staff at the National Audit Office (NAO) are currently undertaking the audit of the 2008-09 Members Estimate Resource Account in line with the limited scope outlined above, but are already testing the reliance that can be placed on the newly available evidence

in support of claims, with a view to its use in the audit of the 2009-10 Members Estimate Resource Account. The NAO's audit work on the Members Estimate Resource Account will be on the same footing as its audit work on Central Government bodies. The NAO will seek independent evidence to confirm both the amount and legitimacy of claims paid.

18. I hope that you find this submission a useful aid to your deliberations and, if you would find it helpful, I, or my successor Amyas Morse, would be pleased to discuss further the points we have raised.
19. I wish you well in what is clearly a challenging review and look forward to learning of the recommendations for reform that you bring forward in due course.

*Yours sincerely*

TIM BURR