

Report of:	Head of Governance
Contact Officer:	Stephen Baddeley
Telephone No:	4411
Portfolio Leader:	
Key Decision:	No
Report Track:	Audit & Governance only

Audit & Governance Committee
24th June 2014
Review of the Effectiveness of Internal Audit

1 Purpose of Report

- 1.1 For members of the Audit & Governance Committee to consider the findings of the annual review of the effectiveness of internal audit.

2 Recommendations

- 2.1 That Members
- (i) note the findings of the annual review of the effectiveness of internal audit for 2013-14;
 - (ii) note that Internal Audit is operating effectively and can be relied upon when considering the Annual Governance Statement for 2013-14.

3 Key Issues and Reasons for Recommendation

- 3.1 Under the Accounts and Audit Regulations 2011 the Council is required to undertake an annual review of the effectiveness of its internal audit.
- 3.2 The review has comprised:
- (i) a self-assessment review undertaken by the Chief Internal Auditor of the section's work against the Public Sector Internal Audit Standards and the Local Government Application Note;
 - (ii) a self assessment review undertaken by the Chief Internal Auditor of compliance with Cipfa's Role of the Head of Internal Audit in Public Service Organisations; and
 - (iii) an independent review by the Head of Governance.

3.3 In addition to the formal review the Section has carried out an exercise to review internal working practices within the team with the support of an experienced Internal Audit Practitioner. The outcome of the review is in the table below.

Review Area	Opinion	Narrative
RESOURCES	Established	The resources of the team are appropriate and deployed effectively to deliver the service.
COMPETENCY	Established	The team has appropriate skills and experience in line with PSIAS and internal procedures are effective.
DELIVERY	Developing	The team delivers an adequate service, however it was identified that the work of the team was not sufficiently focused on key risk areas for the Council when carrying out each assignment and in the classification of recommendations.

3.4 The annual review of effectiveness has shown that overall Internal Audit is operating effectively and can be relied upon when considering the Annual Governance Statement for 2013-14.

4 Relationship to Corporate Priorities

4.1 This report supports the Council's Corporate Priorities as follows:

- (i) The system of internal control is a key element of the Council's corporate governance arrangements which cut across all corporate priorities.

5 Report Detail

5.1 This is the first review following the introduction of the Public Sector Internal Audit Standards and Local Government Application Note. The Chief Internal Auditor has prepared a self-assessment against conformance with these requirements as well as updating the self-assessment against the Role of the Head of Internal Audit document.

5.2 The review by the Head of Governance, which included a review of both of the self-assessments, concluded that there were no areas of significant non-conformance with the PSIAS/LGAN or the paper on the Role of the Head of Internal Audit. For the areas of partial conformance the effectiveness of the section was not considered to be seriously affected; a small number of the areas partial compliance with PSIAS/LGAN is considered to be acceptable due to local circumstances.

- 5.3 One area of significant non-conformance with the standards was identified and this relates to PSIAS 1110 Organisational Independence. The standards require the “Chief Audit Executive” report functionally to the Board and indicate that this includes the Audit Committee Chair and Chief Executive commenting on the PDR and the Audit Committee setting remuneration for the “Chief Audit Executive”.

This is not a common practice in Local Government where Members do not routinely get involved in detailed employment matters. It is also felt that sufficient other safeguards to the independence of Internal Audit are currently in place within the Council such as allowing the Chief Internal Auditor the unfettered right of access to the Audit Committee Chair and Chief Executive to raise any concerns. It is therefore felt that this area of non-conformance does not compromise the effectiveness of Internal Audit although PSIAS/LGAN require it to be disclosed in the Annual Audit Report.

- 5.4 Summaries of the reviews of compliance are attached as follows:

- (i) the Public Sector Internal Audit Standards and the Local Government Application Note - attached at Appendix 1; and
- (ii) the Cipfa paper on the Role of the Head of Internal Audit in Public Service Organisations - attached at Appendix 2.

- 5.5 In addition to the compliance with professional standards the section has also reviewed:

- (i) the performance of the service ie the delivery of the audit plan; and
- (ii) the quality of the service – this has included satisfaction with the service, the number of recommendations made and the implementation of recommendations.

As shown in the Annual Audit Report for 2013-14, the Internal Audit Service has met its key performance targets. The section has

- (i) delivered 94% of the planned audit work in the year; and
- (ii) has received a 98% satisfaction score on the post audit questionnaires.

- 5.6 The review of the self-assessments by the Head of Governance was in agreement with the views of the Chief Internal Auditor.

- 5.7 The External Auditors have concluded that the internal audit service continues to provide an independent and satisfactory service to the Council and that internal audit work contributes to an effective internal control environment at the Council.

- 5.8 In addition to the formal review the Section has carried out an exercise to review internal working practices within the team with the support of an external experienced Internal Audit Practitioner. This review provided an overview assessment of 3 key areas and provided a view for each along with an action plan for improvement. It is proposed to provide focused workshop training with the team to address the points raised in the action plan. The opinion relating to each review area is as follows:

Review Area	Opinion	Narrative
RESOURCES	Established	The resources of the team are appropriate and deployed effectively to deliver the service.
COMPETENCY	Established	The team has appropriate skills and experience in line with PSIAS and internal procedures are effective.
DELIVERY	Developing	The team delivers an adequate service, however it was identified that the work of the team was not sufficiently focused on key risk areas for the Council when carrying out each assignment and in the classification of recommendations.

- 5.9 As part of the PSIAS, Internal Audit are required to produce a Quality Assurance and Improvement Programme (QAIP) this has not yet been formally produced as a stand alone document, although most of its elements already exist including –
- Documented Working Practices;
 - File Review Process;
 - Performance Monitoring;
 - Annual Review of Effectiveness of Internal Audit; and
 - Action Plan for Improvement of the Service.
- 5.10 As part of the development of the QAIP document the future options for the delivery of the review of the effectiveness of Internal Audit will be considered. This will include a summary of the options for undertaking the mandatory external review. The QAIP will be presented to the Audit & Accounts Committee for approval in due course.
- 5.11 From the review a small number of areas for improvement have been identified and these are contained in an Improvement Plan which is attached as Appendix 3.
- 5.12 Overall, the review has shown that the internal audit is operating effectively and can be relied upon when considering the Annual Governance Statement 2013-14.

6 Implications

6.1 Financial

None.

6.2 Legal

None.

6.3 Human Resources

None.

6.4 Section 17 (Crime Prevention)

None.

6.5 Human Rights Act

None.

6.6 Data Protection

None.

6.7 Risk Management

None.

6.8 Equality & Diversity

None.

6.9 Best Value

None.

7 Appendices to the Report

Appendix 1 - Summary of Compliance with the the Public Sector Internal Audit Standards and the Local Government Application Note

Appendix 2 – Summary of Compliance with Cipfa’s paper on the Role of the Head of Internal Audit.

Appendix 3 – Improvement Plan

Previous Consideration

None

Background Papers

Files available from the Chief Internal Auditor

APPENDIX 1

SUMMARY OF CONFORMANCE WITH THE PUBLIC SECTOR INTERNAL AUDIT STANDARDS AND LOCAL GOVERNMENT APPLICATION NOTE – 2013-14

Conformance with the Standard	Y	P	N	Comments
Definition of Internal Auditing				
The PSIAS defines Internal Audit as - “Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.”	✓			Internal Audit has adopted the PSIAS definition and this is included in the Audit Charter
Code of Ethics				
The Code of Ethics contained in PSIAS applies to all Internal Auditors working in the Public Sector in addition to any requirements placed on them by other professional bodies. It is aimed at promoting an ethical culture across the profession of Internal Audit and is seen as essential in ensuring the trust placed in Internal Auditors to provide objective assurance about the organisation’s risk management, control and governance arrangements.	✓			Internal Audit complies with the Code of Ethics and a copy of this has been issued to all members of the team..
The Code of Ethics covers the following areas:				
<ul style="list-style-type: none"> • Integrity • Objectivity • Confidentiality • Competency 	✓			
Public Sector Internal Auditors are also required by PSIAS to have regard to the “Seven Principles of Public Life” as defined by the Committee on Standards in Public Life which cover:	✓			
<ul style="list-style-type: none"> • Selflessness • Integrity • Objectivity • Accountability • Openness • Honesty • Leadership 			✓	A draft competency framework is being produced which will help evidence compliance with this.

Conformance with the Standard	Y	P	N	Comments
Attribute Standards				
1000 – Purpose, Authority and Responsibility				
<p>The purpose, authority and responsibility of the internal audit activity must be formally defined in an audit charter. The internal audit charter is a formal document setting out:</p> <ul style="list-style-type: none"> • internal audit's position within the organisation; • its reporting lines; • access to personnel, information and records; • the scope of internal audit activities • define what the term "board" means (It is anticipated that the Audit Committee will generally fulfil the duties assigned to the board for the Council.) <p>The charter must be periodically reviewed and presented to senior management and the board.</p>	✓			The Charter was approved by the Audit Committee in august 2013

Conformance with the Standard	Y	P	N	Comments
1100 – Independence & Objectivity				
<p>Internal Audit activity must be independent and internal auditors must be objective in performing their work. This comes from the position of Internal Audit in the organisation and ensuring that Internal Audit management has unrestricted access to the Audit Committee and Senior Managers should this be necessary. Internal Auditors should also not be compromised in their work by personal views or having operational responsibility for other areas. Any impairments or potential to independence or objectivity must be reported to appropriate parties.</p> <p>Organisational independence is effectively achieved when the chief audit executive reports functionally to the board. Examples of functional reporting to the board involve the board: approving the internal audit charter;</p> <ul style="list-style-type: none"> • approving the risk based internal audit plan; • approving the internal audit budget and resource plan; • receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters; • approving decisions regarding the appointment and removal of the chief audit executive; • approving the remuneration of the chief audit executive; and • making appropriate enquiries of management and the chief audit executive to determine whether there are inappropriate scope or resource limitations. <p>Governance requirements in the UK public sector would not generally involve the board approving the CAE's remuneration specifically. The underlying principle is that the independence of the CAE is safeguarded by ensuring that his or her remuneration or performance assessment is not inappropriately influenced by those subject to audit. In the UK public sector this can be achieved by ensuring that the chief executive (or equivalent) undertakes, countersigns, contributes feedback to or reviews the performance appraisal of the CAE and that feedback is also sought from the chair of the audit committee.</p>			✓	<p>The Terms of Reference for the Audit Committee need updating to reflect their role in approving the Audit Charter</p> <p>The Chair of the Audit Committee does not have a role in the appointment of the "Chief Audit Executive" or contribute feedback to the PDR. This is outside the scope of normal Council operations and is the only major area of non-conformance with PSIAS. However the Head of Governance who manages the Chief Internal Auditor is directly managed by the Chief Executive and any concerns from the Chief Executive relating to Internal would be highlighted in her PDR.</p>

Conformance with the Standard	Y	P	N	Comments
1200 – Proficiency & Due Professional Care				
<p>The Internal Audit Team should have the correct knowledge, skills and competencies for the work that it carries out and to ensure they enhance knowledge and skills through Continuing Professional Development. The PSIAS specifically requires the “Chief Audit Executive” to hold a relevant professional qualification. Due professional care must be taken to ensure appropriate work is undertaken to identify risks, support findings and meet the objectives of all work undertaken.</p>		✓		<p>The Chief Internal Auditor and one of the Senior Auditors are Cipfa Qualified and we have 1 ACCA, 1 IIA and 1 AAT qualified members in the team. The annual PDR process ensures members of the team follow CPD requirements.</p> <p>Working practices are defined. However, the external review of working practices has identified a need for greater focus on the identification of risks in audit work.</p>
1300 – Quality Assurance and Improvement Programme				
<p>A quality assurance and improvement programme is designed to:</p> <ul style="list-style-type: none"> • allow an assessment of Internal Audit’s activity against the PSIAS requirements; • to assess the efficiency and effectiveness of Internal Audit’s activity; • identify opportunities for improvement. <p>This requires both internal and external assessments to be performed. The PSIAS requires an independent external assessment to be carried out at least once every five years. Both internal and external assessments have to be carried out by individuals or organisations who have sufficient knowledge of Internal Audit standards and operation.</p> <p>The outcome of the review must be reported to the Board and Senior Management as part of the Internal Audit Annual Report which must disclose any areas of non-conformance with PSIAS. Where these are significant they should be considered for inclusion in the Annual Governance Statement.</p>		✓	✓	<p>The section has most elements of the QAIP in place but has not yet drafted a formal document consolidating these.</p> <p>Also work needs to be done to review the performance indicators for the team and formalise their collection and reporting.</p> <p>The Section has not yet had an independent review but is aiming to complete this within the 5 year timescale. A partial external independent review has been carried out to improve working practices of the team.</p>

Conformance with the Standard	Y	P	N	Comments
Performance Standards				
2000 – Managing the Internal Audit Activity				
<p>The Chief Audit Executive must effectively manage the internal audit activity to ensure it adds value to the organisation.</p> <p>This includes the development of a risk based audit plan to inform the Annual Audit Opinion. The Plan should be presented to Senior Management and the Board for approval. The Chief Audit Executive should ensure the resources available to the team are sufficient, appropriate and effective to deliver the audit plan and that any limitations which may impact on the plan or the annual audit opinion are reported to the Board.</p> <p>Where possible the work of Internal Audit should be coordinated with other providers of assurance to ensure appropriate coverage and minimise duplication.</p> <p>Internal Audit’s activity must be reported to Senior Management and the Board. This should include performance in delivering the audit plan, significant risks or control issues identified and any other relevant matters.</p>	<p>✓</p> <p>✓</p> <p>✓</p> <p>✓</p>			<p>The team follow a risk based plan which is approved by Leadership Team and the Audit Committee</p> <p>An Assurance Map is under development to identify other sources of assurance for key risk areas so that these can be taken into account when planning Internal Audit’s work.</p> <p>Performance is reported quarterly to the Head of Governance and the Audit Committee</p>
2100 – Nature of Work				
<p>Internal Audit’s activity must evaluate and contribute to the improvement of governance, risk management and control processes using a systematic and disciplined approach.</p>				<p>The Internal Audit team provide recommendations as part of their work which will improve the Council’s governance framework. In addition ad hoc advice and consultancy is provided in relation to changes in systems.</p> <p>More work is needed by Internal Audit to evaluate the Council’s ethics related objectives, programmes and activities.</p>

Conformance with the Standard	Y	P	N	Comments
2200 – Engagement Planning				
<p>A plan/brief should be prepared for each piece of audit work carried out to include the scope, objectives, timing and resource allocation. The scope should be sufficient to contribute to the annual audit opinion. Sufficient and appropriate resources should be identified for each review to achieve the intended objectives of the review.</p>		✓		<p>Internal Audit have defined procedures which include producing and agreeing a brief for each assignment. The annual audit plan is produced to provide adequate coverage to inform the annual audit opinion</p> <p>The review of working practices has identified a need to shift the focus of audit work to further improve testing of key risks for areas under review.</p>
2300 – Performing the Engagement				
<p>Internal Auditors should identify sufficient, reliable, relevant and useful information to achieve the objectives of the review. Conclusions should be based on the results of appropriate analysis and evaluation of the evidence and sufficient information documented to allow the testing to be repeated.</p>		✓		<p>All assignments are completed in line with agreed working practices and are subjected to a file review process to verify that the conclusions and recommendations made are supported by sufficient evidence derived from appropriate audit testing.</p>
2400 – Communicating Results				
<p>Results of audit work should be reported and where the section issues an opinion or conclusion it must be supported by sufficient relevant information. Communications must be accurate, clear, concise and timely and issued to appropriate parties. In the Public Sector an annual audit report containing an audit opinion must be issued so that it can be used by the organisation to inform its Annual Governance Statement.</p>		✓		<p>The review of working practices has identified a need for greater linkages to the Council's risk management framework when providing opinions and classifying recommendations. However further work is needed on the Risk Management Strategy & Methodology to enable Internal Audit to do this.</p>

Conformance with the Standard	Y	P	N	Comments
2500 – Monitoring Progress				
The results of audit work should be monitored to identify that management actions are being effectively implemented or that management accepts the risks of not taking action.	✓			All action plans are agreed by management or acceptance of risks relating to non-implementation is obtained. Internal Audit follow-up areas which are not deemed to be effective to monitor the progress made in implementing the agreed recommendations.
2600 – Communicating the Acceptance of Risks				
When the Chief Audit Executive concludes that management has accepted a level of risk that may be unacceptable to the organisation, the Chief Audit Executive must discuss the matter with senior management. If the Chief Audit Executive determines the matter has not been satisfactorily resolved they should communicate the information to the board.	✓			A process is in place where such matters would be discussed initially with the relevant member of Leadership Team. Areas where management are accepting a significant risk without some action are reported to the Audit Committee for consideration.

APPENDIX 2

SUMMARY OF COMPLIANCE WITH THE CIPFA PAPER ON THE ROLE OF HEAD OF INTERNAL AUDIT – 2013-14

Adherence to the Standard	Yes	Partial	No
1. The HIA in a Local Authority plays a critical role in delivering the organisation’s strategic objectives by championing best practice in governance, objectively assessing the adequacy of governance and management of existing risks, commenting on responses to emerging risks and proposed developments.			
CIA’s role in governance and how it fits with other key officers (s151, Head of Paid Service & Monitoring Officer) is defined in the Job Description	✓		
Managers do not always adequately consult with Internal Audit on changes to systems or new projects/initiatives to ensure adequate governance arrangements are in place. However most major changes in processes are consulted on.		✓	
The Council have a number of policies in place relating to conduct of employees and governance arrangements. However a number of these are in need of updating and more work needs to be done to promote compliance with the policies across the Council.		✓	
HIA does promote good governance, behaviour and high standards across the authority.	✓		
There is a corporate requirement to report suspected or confirmed frauds to Internal Audit	✓		
2. The HIA in a Local Authority plays a critical role in delivering the organisation’s strategic objectives by giving an objective and evidence based opinion on all aspects of governance, risk management and internal control.			
Internal Audit is separate to External Audit and the HIA does not manage other operational services. IA has defined terms of reference which cover key relationships as well as reporting arrangements. The HIA has arrangements for providing an opinion on the governance arrangements which feeds into the Annual Governance Statement but the HIA is not responsible for writing the AGS.	✓		
The Council does not have a clear system to prompt reviews of key policies on a periodic basis. This means that policies which ensure and promote good governance are not always regularly reviewed and updated.		✓	
HIA has responsibility and the remit to review the Council’s control environment and governance arrangements including risk management and significant partnerships, the result of audit work is reported and an annual opinion provided. The HIA liaises with External Audit to share knowledge and maximise the use of resources but EA do not direct the work of IA.	✓		
The HIA is able to report in their own name without fear or favour. The HIA works well with other key officers to bring key issues to the attention of the Leadership Team & Audit Committee to ensure significant recommendations are implemented.	✓		

Adherence to the Standard	Yes	Partial	No
3. The HIA in a Local Authority must be a senior manager with regular and open engagement across the organisation, particularly with the Leadership Team and with the Audit Committee.			
HIA functions are generally carried out by the Chief Internal Auditor although some aspects are with the Head of Governance. Both these officers are sufficiently senior and independent within the Council's structure to allow the HIA role to be carried out effectively. Internal Audit have unfettered right to documents and to seek explanations.	✓		
The Chief Internal Auditor is managed by the Head of Governance who is part of the Leadership Team. Both officers work to raise the profile of Internal Audit.	✓		
The Council has an audit committee which operates in line with best practice. The committee has carried out a self-review exercise relating 2013-14. The terms of reference for the Committee and IA set out the relationships of the HIA to the committee.	✓		
The Audit Strategy and Audit plan are discussed with the Leadership Team and the Audit Committee prior to being finalised.	✓		
4. The HIA in a Local Authority must lead and direct an internal audit service that is resourced and fit for purpose.			
Internal Audit aims to meet the needs of the council and external stakeholders. IA has established an appropriate quality assurance framework and the team are always looking for ways to develop the effectiveness of the service. The IA team aim to lead by example with high standards including integrity, objectivity, openness, competence and confidentiality.	✓		
Where resources/skills are lacking in-house (eg IT Audit) the section looks to bring in outside expertise. During the Audit Plan process the CIA assesses resources against the need to carry out a satisfactory level of audit work to inform the annual opinion. Adequate recruitment procedures exist to select appropriate employees/suppliers to deliver internal audit work. The skills and needs of the team are assessed and training is sought to maintain/develop appropriate skills.	✓		
5. The HIA in a Local Authority must be professionally qualified and suitably experienced.			
The HIA is CCAB qualified and suitably experienced Internal Auditor to effectively perform the role. The HIA adheres to professional and Internal Audit standards.	✓		
The HIA has sufficient knowledge of the Internal Audit and regulatory environment as well as an awareness of the full range of the Council's activities and processes.	✓		

APPENDIX 3

IMPROVEMENT PLAN FOR INTERNAL AUDIT – 2013-14

Source	Actions	Person Responsible for Implementation	Timescale
PSIAS	Finalise and implement the Competency Framework for the Internal Audit Team as part of the PDR process.	Chief Internal Auditor	December 2014
PSIAS	Produce a formal Quality Assurance & Improvement Programme for Internal Audit consolidating the existing arrangements into one document which contains the options for carrying out the mandatory independent external review in line with PSIAS/LGAN requirements. The QAIP will be approved by the Audit Committee	Chief Internal Auditor	September 2014
PSIAS	The Terms of Reference for the Audit Committees to be updated to reflect the changes required by PSIAS/LGAN	Head of Governance/ Head of Law & Administration	March 2015
External Review/ PSIAS	A workshop is being arranged to revise working processes to focus more on risk when carrying out audit work and to enable assurances and classification or recommendations to be based on the definitions contained in the Risk Management Framework.	Chief Internal Auditor	June 2015
External Review/ PSIAS	Work with Risk Management function to develop and champion risk management within the Council	Head of Governance/ Chief Internal Auditor/ Risk & Resilience Manager	March 2015
PSIAS	A review of performance indicators for the Internal Audit function is to be carried out to ensure an appropriate performance management framework is in place.	Chief Internal Auditor	September 2014
PSIAS	An Assurance Map for the Council is to be developed to inform the Audit Planning process this will enable greater integration with other assurance providers.	Chief Internal Auditor	September 2014
PSIAS/ Role of HIA	The role of Internal Audit in promoting and ensuring compliance with the Council's ethical framework and values will be documented.	Head of Governance/ Chief Internal Auditor	March 2015