

A Review of the Effectiveness of Internal Audit

Purpose

- 1.1 When Members of this Committee completed their annual self-assessment exercise in February 2020, they felt that the question “Does the committee review the adequacy of internal audit staffing and other resources?” was not an area that they had chance to comment on. Therefore, the former Strategic Director of Corporate Resources (the Council’s s151 Officer at the time), was asked to provide an annual overall opinion on the effectiveness of the internal audit function, which would include a review of the adequacy of its staffing resource.
- 1.2 This report provides my review of the effectiveness of Internal Audit in 2022/23.

Recommendations

- 2.1 To review my assessment and note my conclusion in paragraph 4.38.

Reasons

- 3.1 The Audit and Governance Committee is responsible for providing assurance to the Council on the effectiveness of its governance arrangements, its risk management framework and the internal control environment. The work of Internal Audit supports Committee in providing this assurance.
- 3.2 The Audit and Governance Committee has a role to play in evaluating the effectiveness of the internal audit function. This assessment should be performed on a regular basis. Any evaluation of internal audit should also include an assessment of internal audit’s objectivity and independence.

Supporting information

Background

- 4.1 Section 151 of the Local Government Act 1972 sets out the mandatory requirement for an internal audit function for local authorities. As the Strategic Director of Corporate Resources, I am delegated to fulfil this function. The Accounts and Audit Regulations 2015 require that

“A relevant authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, and taking into account public sector internal auditing standards or guidance.”

- 4.2 The definition of Internal Audit, as per the Public Sector Internal Audit Standards (PSIAS) is as follows:

“Internal Audit is an independent, objective assurance and consulting function that is designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluating, reporting on and recommending improvements where necessary to secure effective risk management, control and governance processes.”

- 4.3 The internal audit function for the Council is provided by the Central Midlands Audit partnership (CMAP). The Partnership was formed in January 2012. The Partnership is contractually bound by a Partnership Agreement which runs until 31st March 2025. The Chair of this Committee sits on the Partnership Board.

- 4.4 Internal Audit is a key source of independent assurance to management and the Council and outcomes from the work of Internal Audit are collated into the Head of Internal Audit's "Annual Audit Opinion", which also informs the Council's Annual Governance Statement.

- 4.5 To reach my opinion on the effectiveness of internal audit, I have considered whether Internal Audit provides the assurance needed, that as s151 Officer I have confidence in the ability of the Council's people, processes, and systems to achieve our objectives and where there are opportunities to improve, does Internal Audit provide actionable information that enables the appropriate changes to be made?

- 4.6 To be "effective", Internal Audit needs to:

- Provide evidenced assurance to management and the Audit and Governance Committee on governance, risk and control frameworks;
- Provide appropriate advice and support to management to ensure efficiency, effectiveness and economy of their services and functions and to help them respond to new and emerging issues;
- Add value and assist in achieving the Council's objectives
- Work in partnership with Directorates
- Utilise and target its resources efficiently and effectively

4.7 My opinion is based on assessing the following key areas:

- The structure and resourcing level within CMAP.
- The extent of conformance with the PSIAS in producing quality work.
- Delivering audit work in the most appropriate areas on a prioritised (risk) basis.
- The overall performance of the Internal Audit team.
- Audit Committee reporting.
- Implementation of Internal Audit recommendations.

Assessment of Effectiveness

a) Structure and Staffing of Internal Audit

- 4.8 The Head of Internal Audit is responsible for reviewing the staffing and skills needs across the Partnership. I note from the 2021/22 report that the team underwent a minor re-structure in April 2021 to increase capacity at the operational level while reducing the management tier by one post. However, the existing ICT audit capacity has been under resourced since May 2021 due to the departure of a member of team. Budget constraints have meant that CMAP has now deleted this vacant IT Auditor post.
- 4.9 Audit work is undertaken by experienced and qualified staff. Reviewing the structure and the skill needs of the team to meet the Council's assurance needs should be kept under permanent review. Currently, in terms of academic and professional qualifications, CMAP has:
- Six members of staff who are CCAB qualified accountants,
 - One member of staff who is a CIA qualified auditor,
 - Three members of staff who are PIIA qualified (IIA Diploma in Internal Audit Practice), and another member of staff has the IIA Certificate in Internal Audit and Business Risk.
 - Two members of staff hold CIPFA's Certificate in Investigative Practice and another member of staff holds the Advanced Professional Certificate in Investigative Practice;
 - The Principal IT Auditor has a degree in computing as well as professional IT qualifications (ITIL and CISA)
- 4.10 One key area that CMAP is addressing is its succession planning at the leadership level. As my predecessor outlined in his June 2022 assessment, both Group Auditors are only part qualified. However, both individuals are seeking to address this through completing the Chartered Institute of Internal Auditor's "Certified by Experience" route to obtaining a professional internal audit qualification.
- 4.11 Succession planning is on track elsewhere within the team, particularly at Auditor level. One Auditor passed her final professional accountancy exams in 2022 and is now a member of the Association of Chartered Certified Accountants (ACCA). As part of CMAP's career grade she has been promoted to Senior Auditor level. The other Auditor is on Year 2 of the level 7 Internal Audit Apprenticeship course at Birmingham City University which as well as studying for an MSc in Internal Audit Management and Consultancy also includes studying for the Institute of Internal Auditors (IIA) professional qualification (2 papers out of 3 have been taken and passed).

- 4.12 CMAP also has two Trainee Auditors. One is currently on the first year of the level 7 Internal Audit Apprenticeship course at Birmingham City University, the other has recently stopped studying the level 7 Apprenticeship and the Head of Internal Audit is currently exploring the internal audit training options available.

b) Training and development

- 4.13 All professionally qualified staff within CMAP undertake mandatory Continuing Professional Development (CPD) with their respective Institutes.
- 4.14 All CMAP staff have personal development objectives and are encouraged to attend relevant workshops and courses to enhance their understanding of both internal audit and public sector developments. Personal development and attendance on courses is monitored through the Council's appraisal system and recorded in CMAP's Audit Management System.

c) Resourcing the Plan

- 4.15 Audit work is actively managed within the resource available and progress toward delivery of the Quarterly Internal Audit Plans is reviewed regularly by the Head of Internal Audit and this is also discussed at monthly one-to-one meetings that I have with the Head of Internal Audit. Focus is maintained on scoping and coverage for planned assurance activity; timing of work and availability of stakeholders; and control over the allocation of resources for investigation referrals and in-year requests for advice/support. There are still occasions when the completion of internal audit assignments is not as timely as the Head of Internal Audit would envisage. I am aware that, with the backing of this Committee, my predecessor and the former Chair of Audit and Governance Committee wrote to Service Directors and Heads of Service to express the need for full engagement in the internal audit process.
- 4.16 Any resourcing considerations for effective delivery of internal audit work is discussed at one-to-one meetings. CMAP has a call off agreement with KPMG should any short-term deficiencies in resources arise.

d) Compliance with Professional Standards

- 4.17 From 1st April 2013 (revised in 2017), the Public Sector Internal Audit Standards (PSIAS) became effective. These standards apply to the internal audit functions in all parts of the public sector in the UK and are mandatory. The objectives of the PSIAS are to:
- Define the nature of Internal Auditing within the Public Sector.
 - Set basic principles for carrying out Internal Audit.
 - Establish a framework for provision of Internal Audit.
- 4.18 The Chartered Institute of Public Finance and Accountancy (CIPFA) has produced a local government application note in the United Kingdom for the PSIAS. The Accounts and Audit Regulations deem this as a "proper practice." Consequently the Council's internal audit function must conform with the provisions of the PSIAS.

- 4.19 Within the PSIAS there is a requirement for an independent external review of the internal audit function once every five years by a qualified and independent assessor from outside the organisation. It can be a full external evaluation or a self-assessment with independent external validation. CMAP had an External Quality Assessment undertaken in September 2022. The overall assessment was that CMAP “Generally Conforms with the Public Sector Internal Audit Standards”. The report also states that CMAP compared favourably with peer groups in both local government and the private sector. CMAP came out as “best in class” position in terms of all the EQA reviews that the external assessor had done within local government. Feedback to the CMAP Operational Group was that CMAP was an established team that was well regarded by clients.
- 4.20 There was a number of areas of good practice identified during the review which the external assessor highlighted:
- An Internal Audit Charter setting out the role and responsibilities of Internal Audit guides delivery and establishes the basis upon which the Head of Internal Audit’s Annual Opinion will be based.
 - The service has developed a documented internal audit methodology and supporting templates that delivers a consistent service.
 - Consistent supervisory processes ensure that a standard approach delivers a robust assurance report.
 - Routine reporting informs clients and the Audit Committee regarding progress regarding completion of the internal audit plan, findings and the follow up of recommendations.
 - Self-assessment identifies areas in which future development will be beneficial and is based upon the development of job descriptions, performance appraisals, the establishment of a training matrix and client feedback.
- 4.21 The EQA did also mention some areas where further improvements were potential for consideration. These were:
- Increasing integration of the use by internal audit of risk-based techniques with the risk appetite of each client particularly in terms of planning at a strategic and engagement level would be mutually beneficial, the degree to which this is possible is hampered by the variable maturity of client risk management processes.
 - Developing a clear alignment through the working papers for each assignment to focus on agreed management objectives and the associated significant risks and relevant key controls will assist in the provision of a transparent assurance opinion in the final audit report.
 - Consideration should be given to the revision of the basis for expressing internal audit recommendations and opinions in line with risk impact definitions recognised by each client within its Risk Management Policy rather than rely on those of a generic nature.
 - Formalise Quality Assurance Improvement Programme processes.
- 4.22 The results of the EQA review demonstrate that the Internal Audit service complies with the requirements of the PSIAS.

e) Planning Internal Audit Work

- 4.23 In accordance with the PSIAS, Internal Audit must develop a risk-based plan to determine the priorities of its internal audit activity. The changing risk environment in which the Council operates had shown the limitations of producing an annual internal audit plan, which necessitated frequent adjustments in response to changes in the Council's risks. For the 2020/21 internal audit plan, the Head of Internal Audit commenced planning on a quarterly basis to mitigate the need for frequent amending of the plan. This means that the Head of Internal Audit brings more firm audit plans back to the Committee on a quarter-by-quarter basis. I note that this process has been endorsed by the Committee and my predecessor.
- 4.24 The constant pace of change has meant that to be of value to the organisation the Head of Internal Audit needs to keep their audit plans up to date. The move to quarterly audit plans has helped facilitate this. There has also been a shift in audit coverage towards strategic goals based around the Recovery Plan and moving forward, the Council Plan. The flexibility being introduced in the way Internal Audit is planning its workload is also seen through swifter advice or assurance in response to emerging issues.
- 4.25 I can see that the internal audit plans are now more clearly aligned to the topics that are most important for the success of the Council and that there exists the ability for Internal Audit to respond to emerging risks or issues and the changing priorities of the Council.

f) Improvements and Service Developments

- 4.26 CMAP has developed and maintains a quality assurance and improvement programme (QAIP) that covers all aspects of the internal audit activity. It is designed to enable an evaluation of the internal audit activity's conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The programme also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement. The QAIP Improvement plan is regularly reported through to this Committee as part of the Head of Internal Audit's Quarterly Progress Reports.
- 4.27 CMAP has produced an Audit Charter to provide stakeholders with a formally defined purpose, authority and responsibility of the Audit Partnership. It has been developed in accordance with Public Sector Internal Audit Standards and demonstrates that the Audit Partnership is consistent with this Code. The Charter is reported through to this Committee in March each year.

g) Quality of Reporting

- 4.28 Audit reports are shared with relevant managers (agreed when scoping the Audit). Reporting styles have been and will continue to be reviewed and refreshed. The quality of internal audit reports is discussed at my one-to-one meetings with the Head of Internal Audit. I still want to see more concise audit reporting with clear signposting to the key issues and assurances.

- 4.29 The Head of Internal Audit brings quarterly progress reports to this Committee which provide members with an overview of progress with the internal audit work, in particular:
- the findings from individual assignments and an assurance rating from that piece of work
 - Management's progress on the implementation of agreed audit actions

The Head of Internal Audit also advises Committee on specific concerns around implementation of agreed actions, which provides the Committee with the opportunity to call in specific managers and question them on the issues being raised.

- 4.30 The Head of Internal Audit continues to review and trial some different approaches in how internal audits are carried out, how the individual assignment reports are structured and how the assurance is presented. CMAP are in the process of procuring a new Audit Management System in 2023/24 which will give further opportunity to develop Internal Audit's formal output.

h) Implementation of Internal Audit Recommendations

- 4.31 The process for monitoring implementation of recommendations includes the regular reporting on implementation status to Service Directors and Strategic Directors. This Committee receives regular updates through the quarterly progress report, which provides the opportunity for members to challenge progress and outcomes.
- 4.32 Increased engagement by Directorates, over the past couple of years has seen an improvement in the implementation rate of recommendations, however, there are still challenges for some managers to understand the need to fully engage in this process. The consistent and full implementation of Internal Audit recommendations continues to be an area in need of improvement. Both management and the Audit and Governance Committee need to monitor this consistently with acceleration and appropriate action to have greater assurance that agreed improvements to risk mitigation and internal control are actually fully implemented within reasonable timescales.

i) Service Delivery and KPI's

- 4.33 The Partnership Board monitors the overall performance of the Partnership. The standard KPIs that CMAP maintain across the Partnership are:
- Service Delivery - Plan Completion - This is calculated by determining how complete each audit assignment is, in the revised plan. Each audit assignment is weighted in accordance with the number of days allocated. The target plan completion for each Partner at the year-end is 90%. The Head of Internal Audit is reporting plan completion for Derby City of 90.2% for 2022/23 (90.33% across the Partnership).

- **Productive Percentage** - The number of productive days expressed as a percentage of the overall days available. This measure compares the number of days spent on audit assignments, advice etc. compared with the number of days spent on administrative and managerial tasks. The percentage was much improved on the 2021/22 figure across the Partnership, being 67.17% for 2022/23 compared to 62% in 2021/22.
- **Customer Satisfaction** - CMAP issues customer satisfaction questionnaires at the end of the vast majority of our audit assignments. These surveys elicit the auditee's opinion on the service provided and provide an opportunity for them to pass comment. The target is to achieve an average score of at least 44 out of 55 on all the Customer Satisfaction Surveys returned in the last 12 months. For Derby, the average score in 2022/23 reported by the Head of Internal Audit is 49.5 compared to 47.9 in 2021/22.

- 4.34 Performance Management of the service and for individual auditors is focused on deployment of auditor time to best effect. This has three main elements related to how much time is spent auditing, completion of audits within set timescales and effectiveness of time deployed. These form part of the individual auditor's appraisal process.
- 4.35 There continues to be positive responses to customer satisfaction returns and positive feedback on several specific assignments. Equally, constructive feedback is received, which assists the team in reviewing specific areas and initiating improvements to become more effective. In 2022/23, CMAP received 23 forms back. The ratings are shown in Table 1 below:

Table 1 : Customer Satisfaction Survey – Ratings

Rating	Number	%
Excellent	17	73.9%
Good	5	21.7%
Fair	1	4.4%
Poor	0	
Very Poor	0	

Other Measures of effectiveness of Internal audit

- 4.36 There has been good engagement between Internal Audit and senior management and the Audit and Governance Committee. The introduction of a business partnering approach by CMAP in 2021/22 has improved communication with Service Directors. With the move from individual Directorate Management/Leadership team meetings, the Head of Internal Audit is looking at how CMAP will move forward with the business partnering concept in 2023/24. Strong engagement between internal audit and the Committee is imperative for both the effectiveness of internal audit and good corporate governance. Both need a clear understanding of their roles, commitment and expectations to develop the relationship into a dynamic partnership. There are now good foundations in place at Derby for this partnership to grow.

- 4.37 In 2021/22, CMAP developed the use of data analytics to assist in its audit work and to help management find solutions to issues through the use of data. The benefits of CMAP using data analytics can enhance both efficiency and effectiveness – for example, scripts can be re-used for periodic audits, resulting in efficiency benefits through using analytics vs performing the analysis manually; and performing whole population testing is more effective than random or judgmental sampling.

Conclusion

- 4.38 My overall conclusion is that CMAP continues to deliver an effective internal audit service to the Council.

Public/stakeholder engagement

- 5.1 None

Other options

- 6.1 None

Financial and value for money issues

- 7.1 None

Legal implications

- 8.1 None

Climate implications

- 9.1 None

Socio-Economic implications

- 10.1 None arising directly from this report

Other significant implications

- 11.1 None

This report has been approved by the following people:

Role	Name	Date of sign-off
Legal Finance Service Director(s) Report sponsor Other(s)		
Background papers:	None	
List of appendices:	None	