

A Review of the Effectiveness of Internal Audit

Purpose

- 1.1 When Members of this Committee completed the 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. As the Strategic Director of Corporate Resources (the Council’s s151 Officer), I was asked to provide an overall opinion on the effectiveness of the internal audit function, which would include a review of the adequacy of its staffing resource. My report to the June 2021 meeting concluded that CMAP was delivering an effective internal audit service to the Council, but there were areas where I had identified scope for improvement.
- 1.2 This report provides my latest review of the effectiveness of Internal Audit.

Recommendations

- 2.1 To review my assessment and note my conclusion.

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. 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.
- 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:
- Five 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 still needs to address is succession planning at the leadership level. As I outlined in my June 2021 assessment, both Group Auditors are only part qualified. However, both individuals are still seeking to address this through completing the Chartered Institute of Internal Auditor's requirements.
- 4.11 Succession planning is on track elsewhere within the team. Both of the Auditors are studying for professional qualifications. One Auditor is completing her final year of the Association of Chartered Certified Accountants (ACCA) Accountancy qualification and has passed the three exams she has sat, with one more to sit in June. The other Auditor has recently started studying for the Institute of Internal Auditors (IIA) professional qualification having completed the IIA Certificate in Internal Audit and Business Risk.
- 4.12 In September 2021, two Trainee Auditors commenced employment with CMAP. Both successfully passed their probation period and will be starting their professional training in the next few months.

4.13 CMAP is currently exploring potential routes to fill the vacant IT Auditor post.

b) Training and development

4.14 All professionally qualified staff within CMAP undertake mandatory Continuing Professional Development (CPD) with their respective Institutes.

4.15 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

4.16 Audit work is actively managed within the resource available and progress toward delivery of the Audit Plan is reviewed regularly by the Head of Internal Audit and this is 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 I would envisage, and this continues to be an area for improvement that the Head of Internal Audit is seeking to address.

4.17 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

4.18 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.

4.19 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.

4.20 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. The last external review for CMAP was completed in 2017 and "general" conformance with each of the 56 Standards was achieved. The next external assessment is required by November 2022 at the latest.

- 4.21 CMAP carries out an annual self-assessment against the Standard which satisfies the requirements set out in PSIAS 1311 and 1312 for periodic self-assessments. The results of these self-assessments are reported to the Partnership Board and each Partner's Audit Committee as part of the Internal Audit Annual report.
- 4.22 Given that the self-assessments have indicated no areas on non-conformance, it can be concluded that in all material aspects, 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. 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.
- 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 am seeing 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 reported through to this Committee as part of the Head of Internal Audit's Annual Report.

- 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 There is still development to be done around timely and meaningful assurance that is communicated in a way that is understood by all stakeholders. The Head of Internal Audit has been reviewing and trialling some different approaches in audit assignment reports on how the assurance is presented. He is also looking at the final presentation of the output, in particular "one page audit reports" and agreed actions replacing recommendations.

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 88.6% for 2021/22.
 - 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. This was below target for 2021/22 across the Partnership and is something that the Head of Internal Audit is keen to address.
 - 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 2021/22 reported by the Head of Internal Audit is 47.9.
- 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 (although the return rate is only 44% in 2021/22) and positive feedback on a number of specific assignments. Equally, constructive feedback is received, which assists the team in reviewing specific areas and initiating improvements to become more effective.

Other Measures of effectiveness of Internal audit

- 4.36 This year, I have also considered how good the engagement is 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, although it is not yet fully embedded into internal audit processes. 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 main focus of this work was to contribute to a full overview of current projects and contractual areas within the council. Throughout this work, Internal Audit have identified areas of potential concern. 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 is delivering an effective internal audit service to the Council, but there are areas where I have identified scope for improvement which I am discussing with the Head of Internal Audit.

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

Other significant implications

- 10.1 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