



Review of the Effectiveness of Internal Audit 2014/15

SUMMARY

- 1.1 This report is designed to give Members an overview of the effectiveness of Internal Audit, as required by the Accounts and Audit (England) Regulations 2011.
- 1.2 The findings of the review are highlighted in sections 5 to 7 and in the associated appendices, and conclude that the Council has an effective internal audit function.

RECOMMENDATION

- 2.1 To note the findings and the conclusion that the Council has an effective internal audit function.

REASONS FOR RECOMMENDATION

- 3.1 To meet the requirements of the Accounts and Audit (England) Regulations 2011.

SUPPORTING INFORMATION

4 Background

- 4.1 Paragraph 6(3) of the Accounts and Audit (England) Regulations 2011 requires that 'A larger relevant body must, at least once in each year, conduct a review of the effectiveness of its internal audit and have the findings considered by a Committee'.
- 4.2 Internal audit is one of the key areas of assurance for the council and has a significant impact on the annual governance statement. It is important that those charged with governance are assured that internal audit itself is effective. The Council has a responsibility to maintain an effective Internal Audit function.
- 4.3 There is no mandatory requirement or guidance on who should perform the review. It was considered appropriate by this Committee that the Council's Section 151 Officer should undertake the annual assessment.

- 4.4 All local authorities have a statutory requirement to make provision for internal audit and for the purpose of the regulations, in accordance with proper standards of professional practice as set out in the Public Sector Internal Audit Standards from 1 April 2013.
- 4.5 Since 1 January 2012, the internal audit function has been provided by the Central Midlands Audit Partnership (CMAP), an internal audit partnership formed by Derby City Council and South Derbyshire District Council. Derby Homes joined as a partner on 1 April 2013.

5 The Effectiveness of Internal Audit

- 5.1 This review of effectiveness has been primarily based on the framework guide developed by the Chartered Institute of Public Finance and Accountancy (CIPFA) Better Governance Forum which aims to provide practical support to help make internal audit more effective. This has been achieved by assessing the internal audit function against the building blocks for effective internal audit identified in the guidance. The building blocks are:
- Leadership
 - Governance and relationships
 - Customer focus
 - People
 - Systems and processes
 - Professional Standards
- 5.2 **Leadership** - There is a clear vision for Internal Audit which is laid down in the Internal Audit Strategy. This is a high-level statement of how the internal audit service will be delivered and developed in accordance with the terms of reference and how it links to the organisational objectives and priorities.
- 5.3 In 2010, CIPFA published 'The Role of the Head of Internal Audit (HIA) in public sector organisations' to clarify the role of the HIA and to raise the profile of internal audit. The Statement articulates the core responsibilities of the HIA, as well as the personal and professional skills that they need. The Statement sets out the five principles that define the core activities and behaviours that belong to the role of the HIA in public service organisations and the organisational arrangements needed to support them. My assessment is shown in Appendix 2, and demonstrates compliance with best practise.
- 5.4 The Head of Governance and Assurance is the designated Head of Internal Audit for the Council, and is also the Head of the Central Midlands Audit Partnership.
- 5.5 **Governance and relationships** - Internal Audit is responsible for reviewing and reporting on the adequacy of the authority's internal control environment and also making recommendations for improvement. Based on the work of Internal Audit, the Head of Governance and Assurance provides a level of assurance to the Council on the effectiveness of its system of internal control in his annual audit opinion.

- 5.6 The Audit and Accounts Committee continues to be very supportive of Internal Audit, and there is a good working relationship between the Committee and the Head of Governance and Assurance.
- 5.7 The positioning and profile of the internal audit function within the Council is well defined and provides clarity of internal audit's role and relationship within the organisation. The Head of Governance and Assurance, who also acts as the Head of the Partnership, has monthly meetings with the Section 151 Officer to discuss audit issues.
- 5.8 **Customer Focus** - The audit partnership has a framework for consulting with all of its clients at the audit planning stage, following completion of the fieldwork, through draft report and then post audit feedback.
- 5.9 Following every audit review, a customer satisfaction survey is sent to the relevant manager. The responses received from managers in 2014/15 show that 26 (84%) rate the service as excellent, 4 (13%) as good and 1 (3%) as fair. No responses were received for a poor or very poor service.
- 5.10 **People** - The Internal Audit partnership team have the appropriate technical skills and knowledge to perform effectively and access to training and other material to maintain their skills. The majority of the team have either a professional accountancy qualification (3 CIPFA and 2 ACCA) or an internal auditing qualification (1 CMIIA and 3 PIIA), and the IT Audit staff both have relevant IT degrees and have gained the CISA (Certified Information Systems Auditor) qualification. One IT Auditor and an Assistant Audit Manager have completed the ITIL Foundation qualification. The Audit Partnership also benefits from having one member of staff who is IRRV qualified. In addition, 4 staff have completed the CIPFA Certificate in Investigative Practice.
- 5.11 All of the staff have personal development and training plans as part of their Individual Performance process. Post audit assessments are completed by the Assistant Audit Managers on each piece of work undertaken by the auditors. Personal development is achieved through a combination of sources including in-house training, external courses/seminars/groups, personal research and studying for a relevant professional qualification. In 2014/15, 40 days were recorded under training/personal development. There are also development activities that staff do in their own time which is not recorded.
- 5.12 **Systems and Processes** - Internal Audit has developed processes that support the delivery of high quality work that are regularly reviewed by its management team to maintain efficiency, relevance and effectiveness. Audit assignments are properly planned and work undertaken is evidenced appropriately. Audit reports include an opinion on risk and the control environment, are agreed with the appropriate officer and all recommendations are followed up to ascertain the progress being made on implementation.
- 5.13 The scope of audit assignment include where necessary consideration of the need to identify any incidences of fraud or corruption.

- 5.14 In 2014/15 the actual productivity rate achieved was 74.1% against a target of 71.1%.
- 5.15 **Professional standards** – Conformance with the Public Sector Internal Audit Standards (PSIAS) has been assessed in appendix 3. All elements of the internal audit function *‘generally conform’* to the PSIAS.

6 Other Sources of Assurance

- 6.1 **External Audit reliance on Internal Audit’s work** - Within their Audit Plan report, the external auditor reported to this Committee on 25 March 2015 that :

“We have completed a high level review of internal audit's overall arrangements. Our work has not identified any issues which we wish to bring to your attention. We also reviewed internal audit's work on the Council's key financial systems to date. We have not identified any significant weaknesses impacting on our responsibilities. Overall, we 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. Our review of internal audit work has not identified any weaknesses which impact on our audit approach.”

- 6.2 **Characteristics of effectiveness** - A self-assessment relating to “characteristics of effectiveness” (including compliance with proper practices) has been undertaken and is attached at Appendix 4.
- 6.3 **Internal Audit Plan, Annual Report and reporting to the Audit and Accounts Committee** - The annual audit plan is prepared before the start of the audit year and shows the areas of coverage. The plan takes into account the organisations risk appetite set by management for different activities and parts of the organisation. The Head of Audit uses this methodology, but also applies their own judgement of risks which allows the work of the audit team to be directed towards those areas of highest risk. The annual report of Internal Audit will be presented on this agenda. Progress reports have been submitted throughout the year, identifying work completed and highlighting any specific matters of concern.
- 6.4 **Audit Plan Coverage** - in 2014/15, 89.4% of the audit plan was completed against a target of 91.0%. At the start of the year the Section 151 officer takes a view as to the level of comfort provided by the coverage of the plan. In 2014/15 a number of audits were removed from the plan during the year as a result of a significant number of investigations commissioned by the Council, which required internal audit time and resources. Deferment of parts of the plan does not provide full comfort; however the work completed, as highlighted in this review, is considered to be effective.
- 6.5 **CMAF Board** – The Chief Finance Officers and appointed elected Members of partnership organisation form the CMAF Board. This Board reviews the performance of the internal audit function and holds the Head of the Partnership to account.

7 Conclusion

- 7.1 From the evidence reviewed, my overall conclusion is that the Council has an effective internal audit function upon which it can place reliance.

OTHER OPTIONS CONSIDERED

8.1 N/A

This report has been approved by the following officers:

Legal officer	n/a
Financial officer	n/a
Human Resources officer	n/a
Estates/Property officer	n/a
Service Director(s)	n/a
Other(s)	n/a

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Background papers:	Public Sector Internal Audit Standards
List of appendices:	Appendix 1 – Implications Appendix 2 – Assessment against the CIPFA Statement on the role of the HoA Appendix 3 – Conformance with PSIAS Appendix 4 – Characteristics of effectiveness

IMPLICATIONS

Financial and Value for Money

- 1.1 None directly arising.

Legal

- 2.1 Under the Accounts and Audit (England) Regulations 2011, the Council is required to undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control.

Personnel

- 3.1 None directly arising

IT

- 4.1 None directly arising

Equalities Impact

- 5.1 None directly arising

Health and Safety

- 6.1 None directly arising

Environmental Sustainability

- 7.1 None directly arising

Property and Asset Management

- 8.1 None directly arising

Risk Management

- 9.1 Internal Audit provides the organisation with objective assurance on whether the major business risks are being managed appropriately and provides assurance that the risk management and internal control framework is operating effectively.

Corporate objectives and priorities for change

- 10.1 Internal Audit contributes through its review work on the major corporate risks to the Council achieving corporate objectives and priorities. This is achieved by the audit of key systems and corporate governance issues and the associated risks.

Assessment against CIPFA's "The Role of the Head of Internal Audit in public organisations"

Principle	Compliant	Current position
<p><u>Principle 1:</u> 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</p>	Yes	The Head of Governance & Assurance (HoGA) is responsible for promoting corporate governance and spreading good practice. The internal audit strategy sets out how as Head of Internal Audit, the post will fulfil this role. Through internal audit, the HoGA reviews and makes a judgement on the whole range of controls including those relating to achieving value for money and the prevention and detection of fraud and corruption.
<p><u>Principle 2:</u> Giving an objective and evidence based opinion on all aspects of governance, risk management and internal control</p>	Yes	The HoGA provides the Council with a range of assurances which includes the Annual Head of Audit Opinion.
<p><u>Principle 3:</u> A senior manager with regular and open engagement across the organisation, particularly with the Leadership Team and with the Audit Committee</p>	Yes	The HoGA has full access across the Council, especially to the Chief Executive and the Chair of Audit and Accounts Committee.
<p><u>Principle 4:</u> Must lead and direct an internal audit service that is resourced to be fit for purpose</p>	Yes	The Central Midlands Audit Partnership resources are currently proportionate to the size, complexity and risk profile of the Council and enable the HoGA to give a reliable opinion on the Council's control environment. Because reliance is placed on the work of internal audit, the HoGA ensures that all the work is consistently of a high quality and in line with professional standards. The HoGA ensures that all staff demonstrate the highest ethical standards.
<p><u>Principle 5:</u> Must be professionally qualified and suitably experienced</p>	Yes	The HoGA is a qualified accountant and a member of the Chartered Institute of Public Finance & Accountancy with 28 years internal audit experience, of which 22 years have been as a Head of Internal Audit.

Compliance with the Public Sector Internal Audit Standards

PSIAS requirement - Summary	Standard	Findings
Definition of Internal auditing	Generally conforms	The opinions and recommendations that CMAP provide do help the organisation and are valued by stakeholders.
Code of ethics	Generally conforms	CMAP sets high standards for doing their job and maintain these in practice.

Attribute standards

<i>1000 Purpose, Authority and Responsibility</i>	Generally conforms	CMAP's internal audit activity has a formal definition of its purpose, authority and responsibility
<i>1100 Independence and Objectivity</i>	Generally conforms	CMAP's Internal Audit Charter and planning documents do not contain major restrictions upon its internal audit activity
<i>1200 Proficiency and Due Professional Care</i>	Generally conforms	CMAP formally defines how it operates in its Internal Audit Charter and documented procedures.
<i>1300 Quality Assurance and Improvement Programme</i>	Generally conforms	CMAP has established a culture of continuous improvement to prevent problems and to underpin day-to-day delivery of a reliable assurance and consulting service.

Performance standards

<i>2000 Managing the Internal Audit Activity</i>	Generally conforms	CMAP's internal audit work adds value to the Council (and its stakeholders) through objective and relevant assurance, and contributes to the effectiveness and efficiency of governance, risk management and control processes.
<i>2100 Nature of Work</i>	Generally conforms	CMAP's internal audit work evaluates and contributes to the improvement of governance, risk management, and control processes using a systematic and disciplined approach.
<i>2200 Engagement Planning</i>	Generally conforms	CMAP develops and documents a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations.
<i>2300 Performing the Engagement</i>	Generally conforms	The internal auditors identify, analyse, evaluate, and document sufficient information to achieve the engagement's objectives.
<i>2400 Communicating Results</i>	Generally conforms	Internal auditors communicate results of each audit engagement.
<i>2500 Monitoring Progress</i>	Generally conforms	The Head of Governance & Assurance (Head of the Audit Partnership) has established and maintains a system to monitor the disposition of results communicated to management.
<i>2600 Communicating the Acceptance of Risks</i>	Generally conforms	The Head of Governance & Assurance (Head of the Audit Partnership) communicates in both audit

PSIAS requirement - Summary	Standard	Findings
		reports and reports to Audit and Accounts Committee any instances where the identification of risk has been accepted by management and monitors progress on actions taken by management and reports accordingly on progress of implementation.

Definitions as per IIA

Generally Conforms means the evaluator has concluded that the relevant structures, policies, and procedures of the activity, as well as the processes by which they are applied, comply with the requirements of the individual *Standard* or element of the Code of Ethics in all material respects. For the sections and major categories, this means that there is general conformance to a majority of the individual *Standards* or elements of the Code of Ethics, and at least partial conformance to the others, within the section/category. There may be significant opportunities for improvement, but these must not represent situations where the activity has not implemented the *Standards* or the Code of Ethics, has not applied them effectively, or has not achieved their stated objectives. As indicated above, general conformance does not require complete/perfect conformance, the ideal situation, successful practice, etc.

Partially Conforms means the evaluator has concluded that the activity is making good-faith efforts to comply with the requirements of the individual *Standard* or element of the Code of Ethics, section, or major category, but falls short of achieving some major objectives. These will usually represent significant opportunities for improvement in effectively applying the *Standards* or Code of Ethics and/or achieving their objectives. Some deficiencies may be beyond the control of the activity and may result in recommendations to senior management or the board of the organisation.

Does Not Conform means the evaluator has concluded that the activity is not aware of, is not making good-faith efforts to comply with, or is failing to achieve many/all of the objectives of the individual *Standard* or element of the Code of Ethics, section, or major category. These deficiencies will usually have a significant negative impact on the activity's effectiveness and its potential to add value to the organisation. These may also represent significant opportunities for improvement, including actions by senior management or the board. Often, the most difficult evaluation is the distinction between general and partial. It is a judgment call keeping in mind the definition of general conformance above. Carefully read the *Standard* to determine if basic conformance exists. The existence of opportunities for improvement, better alternatives, or other successful practices do not reduce a generally conforms rating.

Appendix 4

Internal Audit – Characteristics of Effectiveness

Characteristic of 'effectiveness'	Evidence of Achievement
IA operates in accordance with "proper practices" as defined in professional codes of practice.	CMAP conforms with the Public Sector Internal Audit Standards
IA can demonstrate that its work provides assurance that the control framework is sound and that standards of risk management are improving.	A review of controls is a fundamental part of each audit. The results of audit work are reported to Audit & Accounts Committee, including specific reports on the risk management process.
IA understands its position in respect to the organisation's other sources of assurance and plan its work accordingly.	Internal Audit identifies other sources of assurance and takes this into account when preparing the internal audit plan.
Understand the whole organisation, its needs and objectives.	Internal audit work takes into account the Council plan and individual Directorate service plans. Another information source is the corporate risk register, which is considered in formulating the annual audit plan.
Be seen as a catalyst for change at the heart of the organisation.	Audit recommendations include suggestions for improving processes and controls.
Add value and assist the organisation in achieving its objectives.	Demonstrated through individual audit assignments and also corporate work.
Be involved in service improvements and projects as they develop, working across internal and external boundaries to understand shared goals and individual obligations.	Internal Audit provides help and advice on request and supports specific projects identified in plan and on <i>ad hoc</i> basis. Internal Audit has contributed to key new systems such as procurement cards
Be innovative and challenging – shaping the values and standards of the organisation; providing internal inspection and validation and encouraging service managers to take ownership of processes, systems and policy.	Internal audit has taken an innovative approach to its reporting arrangements by focusing on risks and engaging managers in developing actions to manage risks, thereby encouraging ownership of the control environment
Ensure the right resources are available – the skills mix, capacity, specialism and qualifications/experience requirements all change constantly.	Internal Audit continually assesses its skills mix to ensure that it is appropriate to the demands placed on internal audit. Resource issues are addressed in the Strategy as well as the CMAP Business Plan. On-going consideration is given to alternative sources of audit resource, including areas requiring specialist skills.