Derby City Council

Internal Audit Strategy 2011/12

March 2011

1. Introduction

1.1 This document sets out the overall strategy for the Council's internal audit service for the current year 2011/12 and the strategic approach to delivering internal audit services.

1.2 Section 151 of the Local Government Act requires the authority (through its chief financial officer) to ensure the proper administration of the Council's financial affairs. The work of the internal audit function supports the appointed S151 officer in this. Internal Audit assists managers to administer the Council's finances in a sound manner related to the associated risks, and it provides information and assurance to the Corporate Director of Resources on the extent of proper administration.

1.3 The Accounts and Audit Regulations 2003, as amended in 2006, sets out the requirements for local authorities for internal audit;

"A relevant body shall maintain **an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with the proper internal audit practices…** "

1.4 The Code of Practice for Internal Audit in Local Government provides a professional definition of what internal audit is;

"Internal Audit is an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment comprising risk management, internal control and governance by evaluating its effectiveness in achieving the organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources."

2. Purpose of the Strategy

2.1 The purpose of the audit strategy is to put in place an approach that will enable Internal Audit to be managed in a way which will facilitate:
- How the service is delivered
- The provision to the Council, through the Audit and Accounts Committee of an overall opinion each year on the Council's risk management, control and governance, to support the Annual Governance Statement
- Audit of the Council's risk management, control and governance systems through audit plans in a way which affords suitable priority to the Council's objectives and risks
- The identification of audit resources required to deliver an audit service which meets required professional standards
- The relative allocation of resources between assurance, fraud related and consultancy services provided by Internal Audit.

3.   Current Internal Audit Approach

3.1   The current audit process is mainly functionally driven – the audit 'universe' consists of a mix of activities, cross service or corporate risk and financial audits, where processes such as payments, payroll etc are separately identified for audit.

3.2   Delivery of the plan is through in-house resources, including assurances from other assurance providers. The current plan is based on a one year cycle based on an underlying risk assessment. The inherent risks existing within each area are then identified for audit as part of the audit planning process.

3.3   Internal Audit reviews the Council's fundamental financial systems each year. The Council's External Auditor assesses the extent to which reliance can be placed on the work of Internal Audit. Councils are awarded "managed audit" status if certain standards, including reliance on audit work, are achieved. This enables the External Auditor to reduce the work they carry out, thus cutting their charges to the Council and avoiding duplication. The financial systems are audited using a systems based approach with the addition of an assessment of any other risks that impinge on the area.

3.4   Separate time allocation is allowed in the audit plan for fraud, consultancy activities, advice & guidance and follow up audits. The plan is prepared on the basis of audit need, and is then compared to existing audit resources to identify whether any shortfalls exist.

4.   Standards

4.1   Internal Audit must meet the standards laid down by the Chartered Institute of Public Finance and Accountancy (CIPFA) as published in its Code of Practice for Internal Audit in Local Government in the United Kingdom 2006.

4.2   Internal Audit will comply with the Council's Policies etc.

4.3   The Head of Audit and Risk Management is a fully qualified accountant and is a Member of the Chartered Institute of Public Finance and Accountancy and has to also comply with their professional rules and ethical standards, including completing continuous professional development.

4.4   An independent review of the effectiveness of the system of internal audit will be conducted annually by the authority in accordance with the Accounts and Audit Regulations. In addition external reviews will be carried out by the Council's External Auditors.

4.5   The Audit Manager will ensure that there is an up to date Audit Manual in place setting out the standards for the service and the methodology to be adopted throughout the audit process and will monitor compliance with these in liaison with the Head of Audit and Risk Management by means of quality reviews.

5.   What Internal Audit Needs To Do

5.1   In meeting the professional standards and organisational needs, Internal Audit will:

- Provide an assurance on the Council's internal control system, and hence there is need to audit areas of financial and non-financial risk as this will encompass some of the key governance systems.
- Audit the main financial systems and other systems related to possible material mis-statements, regardless of comparative risk.
- Deliver risk based assurance on those controls that manage significant risks.
- Fully comply with best practice as defined by CIPFA in the Code of Practice 2006,
- Better integrate the outcomes and other information gathered as part, of the internal audit process, with the risk management processes of the Council.
- Maintain ongoing effective relationships with the new External Auditor and deliver complimentary plans of work so as to deliver an efficient audit service collectively, for the Council.
- Ensure that appropriate resources, suitably experienced, and with skills to deliver the whole plan of work are maintained within Internal Audit.
- Improve the efficiency and effectiveness of operations of the service.
- Promote good corporate governance and control practices and contribute to a good governance culture.
- Work in a positive manner alongside clients, supporting them in the effective management of risk and service delivery.
- Contribute to embedding risk management throughout the Council's processes.
- Contribute to the development and maintenance of an effective counter fraud culture within the Council.

6. Delivery of the Audit Service

6.1 The Audit Manager is responsible for delivering the audit service. To ensure that this can be achieved there are appropriate arrangements for audit planning and ensuring that the plan is adequately resourced with the necessary level of skilled and experienced staff.

6.2 The service will be delivered on the basis of a risk based audit plan compiled by the Audit Manager, using a risk assessment model which allocates a risk factor of high, medium or low to all the areas for audit review to be undertaken. The annual audit plan will be subject to approval by the Audit and Accounts Committee in June each year. Changes to the plan will be reported to Committee as and when required.

6.3 The audit plan sets out the number of days required for Internal Audit to adequately review the areas involved and indicates the priority level for each planned audit assignment. The overriding objective of this approach is to ensure that the Head of Audit and Risk Management is able to present an annual opinion on the Council's overall control environment by directing adequate resources based on the relative risks of operations, resources and services involved.

6.4 The audit plan balances the following requirements:

- The need to ensure the plan is completed in line with the agreed performance targets
- The need to ensure the core financial systems are adequately reviewed to provide assurance that management has in place proper arrangements for financial control
- The need to appropriately review both strategic risk and operational risk areas

- The need to have a sufficient contingency element to deal with unplanned issues and investigations that arise during the year
- To enable positive, timely input to assist corporate and service developments
- To meet the requirements of the managed audit arrangements with the Council's external auditors to ensure that they can comply with the International Auditing Standard, including system documentation and evaluation for all business critical systems, grants verification and validation of performance indicator outturns

6.5 Progress in completing the audit plan, as well as achieving its performance targets will be monitored by the Head of Audit and Risk Management and the Audit and Accounts Committee.

6.6 In the delivery of each assignment, Internal Audit will look to make practical recommendations based on the findings of the review completed. These will be discussed with managers with the agreed actions being detailed in an implementation plan attached to the report. A summary of all audit reports will be submitted to the Audit and Accounts Committee as part of the Internal Audit Progress report.

7. How will we achieve this?

7.1 **Review of the whole internal control environment -** We will deliver a comprehensive plan of audit reviews such that the key elements of the internal control environment, including non-financial areas are covered on a cyclical basis. This will be evidenced through our annual audit plan. We will use the evidence from this work to deliver an annual opinion on the internal control environment to the Audit and Accounts Committee.

7.2 **Review of Main Financial & Material Systems** - As part of our "joined up working" with External Audit we will review of controls in the Council's main financial systems. This will reduce the level of testing that External Audit need to do, which in turn keeps the External Auditor's fees charged to the Council at the agreed level.

7.3 **A System of Risk-Based Auditing** - is fundamental to our ability to comply with the assurance framework requirements that must be in place to comply with professional standards. We will continue to develop our risk based approach so as to ensure it is effective in providing assurance to managers within the Council and to Members. We will identify and review those areas which are most significant to the control of those risks that threaten the achievement of the Council's objectives/priorities.

7.4 **Compliance with Best Practice –** we are developing a methodology to measure our achievement of compliance with the Code of Practice. We will monitor ourselves against these professional standards and endeavour to rectify any gaps.

7.5 **Relationship with Risk Management** - We are not responsible for the management of the Council's risks; this is entirely the responsibility of the management. However, Internal Audit will take account of the corporate risk management processes in our reviews of the control of risks. We will endeavour to emphasise the importance of risk management to all managers as part of the delivery of our service.

Internal Audit staff provide advice on internal control and the management of risks. We do this not only as part of their designated audit reviews but in response to direct

approaches to us by clients seeking help and support. This helps to ensure the sound and effective control of business, strategic and operational risks within the Council.

Through our work we are assisting managers to better understand risk management and the feedback from the audit work will enable them to keep their registers up-to-date and relevant. This is an important educational / informative role that adds value to the organisation.

The Head of Audit and Risk Management is responsible for advising on the corporate risk management methodology and for developing the processes for recording the risks.

7.6 **Relationship with External Auditor –** we will always endeavour to work with the External Auditor and share plans so as to deliver an effective corporate assurance service to the council. We will maintain a process of regular liaison meetings with the External Auditor.

7.7 **Appropriate Resources** – we will endeavour to maintain an effective staffing resource to undertake the planned workload. We will apply staff in the most effective way in accordance with their experience and skills and in accordance with the Code of Practice. The section is being re-structured to better meet the requirements being placed on it. We have a partnering arrangement with another internal audit supplier to ensure that we can maintain the necessary level of resources to achieve the audit plan. We will develop the skills and competencies of our staff through a systematic development and training process. This will be addressed through the Council's Managing Individual Performance scheme.

7.8 **Efficiency Improvements** – we will utilise technology and benchmark working practices with the specific objective of improving our efficiency and performance. We will seek to minimise the time spent on audits whilst at the same time delivering effective audits. Our efficiency will also support more efficient service delivery by our clients as we try to minimise disruption and distraction to normal service delivery. We will continue to develop this. We will comment on the efficient, economic and effective use of resources where appropriate in our internal audit work.

7.9 **Promoting Good Corporate Governance** – in all we do we will seek to promote good corporate governance, including in the giving of advice and the assessment of internal controls. We will also contribute to both the Council's counter fraud culture and policy and strategy through a programme of anti-fraud checks, and by reviewing the policy and strategy. We will promote this via our work, on our web pages and in coordination with the External Auditor and other key governance managers within the Council. We will develop new ways of working by exploring the use of data matching between Council systems. Internal Audit has established a Corporate Fraud Group and will use the Group as a forum for implementing best practice within the Council on anti-fraud measures.

7.10 **Good Customer Service** - we will continue to strive to be responsive to our customers and their individual needs and to add value to the organisation where it can. This will be achieved through acting as a control assurance function providing assurance to managers and to the organisation as a whole on the state of its internal control arrangements. We also add value by pointing out inefficiencies and by

supporting managers in the management of risk, which increases the overall likelihood of successful service, target and objective achievement.

8.   How do we measure performance and quality?

8.1   The Audit Manager is responsible for producing monthly performance monitoring information. Currently work is on-going to develop a balanced scorecard approach for measuring the overall performance of the internal audit service.

8.2   All audit staff participate in the Council's Managing Individual Performance (MIP) scheme. The MIP makes sure each person in the team has a clear idea of what they are expected to do and how that contributes to the overall goals of the Council.

8.3   We collect feedback on individual audits through a Client Satisfaction Survey being forwarded to each auditee following the completion of the audit review.

8.4   An internal review process takes place on each individual audit assignment.

9.   What are our Objectives/Service Targets

9.1   Through continuous improvement, internal audit will strive to provide cost effective, high quality internal audit services that meet the needs and expectations of all its customers.

9.2   The audit team has a number of objectives:
   • Deliver agreed Audit Plan in accordance with agreed Performance Targets.
   • Achieve high level of customer satisfaction and improve perception of Audit service.
   • Become more efficient and improve the quality of service delivered to our customers.
   • Improve each customer's overall control environment and where necessary provide assurance.
   • Develop a strong Anti-Fraud culture within our customers' organisations.
   • Provide better value for money by delivering Internal Audit services to other public sector organisations.

10.   Income Generation - External Work

10.1   We currently provide an internal audit service to 4 external organisations. Our aim over the next few years is to expand the level of external work that we undertake.