

## **Internal Audit Strategy and Review of the Terms of Reference**

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### **REASON FOR ITEM**

The CIPFA<sup>1</sup> Code of Practice for Internal Audit in Local Government (2006) required the Head of Internal Audit to produce an Audit Strategy and Annual Operational Plan, and to ensure that the Audit Committee receives, understands and approves it.

This report sets out the strategy for delivery and development of the Internal Audit Service 2013-14 and the associated Annual Internal Audit Operational Plan. It details how the service will be delivered, the assurance that it will provide and how the Head of Internal Audit will contribute to corporate governance arrangements, risk management processes and key internal control systems. The Internal Audit Strategy underpins the assurance the Head of Internal Audit provides for the Annual Governance Statement.

This report also takes into account that from April 2013 the current CIPFA Code of Practice is being replaced by new UK standards for internal audit in the public sector. CIPFA is publishing a Local Government Application Note for the PSIAS on the 3<sup>rd</sup> April. There will then be a review of how the new standards and Application Note will affect the internal audit framework for 2013/14 and later years, and the results of the review will be reported to the next meeting of this committee.

### **OPTIONS AVAILABLE TO THE COMMITTEE**

The Audit Committee should review and approve the Internal Audit Strategy for 2013-14 and note that a review of the Terms of Reference will be reported to the June meeting of this Committee.

### **INFORMATION**

#### **1. INTERNAL AUDIT STRATEGY 2013-14 AND TERMS OF REFERENCE**

- 1.1. The Audit Strategy is a high level document, which deals with how the service will be delivered and developed. The Audit Plan provides details of how this strategy translates into a detailed work plan. Both documents are updated annually.
- 1.2 There are also an Internal Audit Terms of Reference that describe the purpose and authority of the Council's Internal Audit service, as well as its principal responsibilities and operating methods.
- 1.3 The Terms of Reference have taken into account CIPFA's Code of Practice for Internal Audit in Local Government and also take due cognisance of the standards of other bodies, such as the Chartered Institute of Internal Auditors, the Auditing Practices Board and the CCAB<sup>2</sup>.

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<sup>1</sup> The Chartered Institute of Public Finance and Accountancy

<sup>2</sup> Consultative Committee of Accountancy Bodies

- 1.4 In 2012 representatives from CIPFA, other professional bodies and the main public sector organisations in the UK agreed to produce a common standard for all internal audit services across the UK public sector. It is based on the IIA's<sup>3</sup> International Standards, Definition of Internal Auditing and Code of Ethics and is called the Public Sector Internal Audit Standards, PSIAS. It was issued in December 2012.
- 1.5 CIPFA is publishing a Local Government Application Note for the PSIAS on the 3<sup>rd</sup> April, and once received, both the Terms of Reference and the Internal Audit Strategy will be reviewed in the light of the PSIAS and the Application Note to establish what changes may need to be made. It is not anticipated that any changes will be very significant. A report will then be presented to the June meeting of this committee to reflect this review. In the meantime, Internal Audit will operate under the current Terms of Reference and produce an Internal Audit Strategy 2013-14.

## **2. OBJECTIVES AND OUTCOMES**

- 2.1. The objective of Internal Audit is to provide an independent and objective opinion on the organisation's control environment by evaluating its effectiveness in achieving the organisation's objectives.
- 2.2. Auditing standards recognise that its remit extends to the whole control environment of the organisation, including the systems of governance, risk management and internal control. A fuller expansion of this definition and the roles and responsibilities of Hillingdon Internal Audit is contained in the Terms of Reference for the service, which is available on the Council's website, but is subject to the review referred to in 1.5 above.
- 2.3. Audits will be carried out using a risk-based methodology, which looks at the objectives of an identified area as set out in service, group and team plans and assesses how far the controls in place will assist in addressing the risks to the achievement of objectives.
- 2.4. The outcome will be an assurance opinion at year-end that is based on an assessment of key risks to the Council.

## **3. EVIDENCE FOR THE OPINION**

- 3.1. Internal Audit use a risk based approach to audit planning, which considers the total possible auditable areas in the Council (known as the Audit Universe) and weights them according to a set of risk factors. These include the obvious considerations such as value, volume and ease of removal of assets that would be considered in any financial context, but also a range of non financial factors such as risks to service users and to the reputation of the Council. Risk assessments are updated at the end of every audit.
- 3.2. As the services the Council delivers or the methods of delivery are changed, the Audit Universe is continually revised and re-risked to ensure it keeps pace with emerging challenges. Risk is therefore reconsidered at the beginning of each year

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<sup>3</sup> The Institute of Internal Auditors, a body based in the United States with chapters in many countries

and a new Annual Operational Plan is based on a revised universe and risk assessment.

- 3.3. The model allows higher risk audits to be carried out annually, if necessary, and can accommodate varying frequencies for other audits such as triennial auditing of schools, and a programme of reviews for establishment audits. At the same time, the methodology ensures that all audits in the universe are carried out within a defined period (five years) because of the greater time since the last audit, it naturally falls into a higher risk category. At the end of each audit the risk assessment for the area will be revised resulting in an automatic recalculation of priorities.
- 3.4. The audit strategy method is therefore to take the updated Audit Universe and create a rolling five-year operational plan – this determines the audits for the forthcoming year that are organised into the annual Operational Plan. An element of contingency is budgeted into the plan so that in-year urgent issues can be dealt with as they arise.
- 3.5. This methodology results in a plan that supports Directors in delivering their strategic priorities and provides an overall view on the internal control environment, which is a key part of good corporate governance.

#### **4. IDENTIFYING AND ADDRESSING SIGNIFICANT LOCAL AND NATIONAL ISSUES**

- 4.1. Internal Audit meets regularly with Directors and Managers within the Council to discuss emerging issues and changing priorities, both locally and nationally. Any relevant issues are incorporated into the audit universe and risk rated in the normal way.
- 4.2. Risk registers are regularly checked and risks and their current mitigation are taken into account in the annual planning round.
- 4.3. The team also scan professional journals, news media, web-based professional discussion groups and other on-line media to keep up to date with the wider audit and local government environment.
- 4.4. Where investigations have identified poor or weak controls as contributing factors to a loss or irregularity, immediate action plans are recommended and the system or function is placed in a high risk category so that an early audit or follow up can be scheduled.

#### **5. HOW THE SERVICE WILL BE PROVIDED**

- 5.1. The in-house team will carry out most audits, the exception being the audit of some IT systems, particularly where a high level of technical skill is required. A contract for 40 days of audit is in place with RSM Tenon. Less technical aspects of IT audit are incorporated into general audit work when systems are under review.
- 5.2. There is a dedicated schools' auditor, which allows delivery of a service that not only provides audit to schools but also adds value by providing advice, guidance

and a regular newsletter. We continue to work closely with Schools Finance, HR and Governors' Services to provide school support that reflects a more coherent approach.

- 5.3. During the year the majority of secondary schools have achieved Academy status and are no longer the responsibility of the local authority. This has reduced the time required on dedicated schools audit and consultation has taken place to address the changing requirement.
- 5.4. Anti-fraud awareness training and proactive detection will continue to be delivered by the Audit team as will preliminary investigation of suspected or alleged fraud and corruption. The Corporate Fraud Team has been active in dealing with wider fraud issues that affect the council such as Tenancy and Blue Badge fraud.
- 5.5. Data analysis software is used to match large volumes of data to identify suspicious transactions.
- 5.6. The team experienced some staff turnover in the year 2012/13. The schools' auditor left, but a replacement was successfully recruited, also a CCAB<sup>4</sup> accountant. One trainee also left, but another equally suitable trainee has taken their place. This allows for the planning of the full complement of 11.36 FTE in 2013/14.

## **6. RESOURCES AND SKILLS REQUIRED TO DELIVER THE STRATEGY**

- 6.1. The in-house team has a wide pool of skills and experience and we encourage staff to further their professional training. This has resulted in a team with a particularly high professional qualification level. The Head of Internal Audit and one Audit Manager are qualified CIPFA accountants: one Audit Manager is CMIIA<sup>5</sup> (Institute of Internal Auditors) qualified. This provides a wide range of technical skills at manager level. Two Senior Auditors are internationally qualified accountants. The Schools Auditor is a chartered accountant<sup>6</sup> and one trainee has now also qualified as CMIIA and become a Senior Auditor.
- 6.2. The three trainees are, or will be, pursuing professional training supported by the Council. Two trainees have completed the first year of IIA training. One trainee will start studying for the IIA in September.
- 6.3. The qualification status for the current team is therefore as follows:

|                                  |   |
|----------------------------------|---|
| Qualified Accountants            | 5 |
| Members of the CIIA (CMIIA)      | 2 |
| Studying for CIIA examinations   | 3 |
| Unqualified but very experienced | 2 |
- 6.4. Continuing Professional Development for all staff is addressed through the PADA process.

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<sup>4</sup> Qualified member of any of the five accountancy bodies that are themselves members of the Consultative Committee of Accountancy Bodies

<sup>5</sup> Qualified member of the Chartered Institute of Internal Auditors, the UK chapter of the IIA

<sup>6</sup> Qualified member (Fellow) of the Institute of Chartered Accountants in Ireland

**BACKGROUND PAPERS**

*Code of Practice for Internal Audit in Local Government in the United Kingdom (CIPFA, 2006)*

*Public Sector Internal Audit Standards (CIPFA and others, 2012)*