

Annual Review of the Effectiveness of Internal Audit

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REASON FOR ITEM

The Accounts and Audit Regulations (England) 2011 include the requirement that the Council *'must 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'* (6 (1)). Section 6(3) already requires larger relevant bodies to conduct a review of the effectiveness of its internal audit at least annually.

The purpose of this report is to present the results of the review of the effectiveness of the internal audit function in relation to the year 2012/13 and make suggestions about how it can improve.

For many years the internal audit service was primarily reviewed against the CIPFA¹ Code of Practice for Internal Audit in Local Government (2006). In December 2012 a common standard for all internal audit services across the UK public sector was introduced. It is based on the IIA's² International Standards, Definition of Internal Auditing and Code of Ethics and is called the Public Sector Internal Audit Standards, PSIAS. CIPFA published a Local Government Application Note for the PSIAS in April 2013 that clarified how the Standards could apply to local authorities. CIPFA also published in 2010 a 'Statement on the role of the Head of Internal Audit in public service organisations' (the Statement).

The review took into account the requirements of the new PSIAS and applied a checklist supplied with the Application Note to gauge compliance currently and what improvement actions could be considered for the future. The service was also reviewed against the CIPFA Code since that was the standard for 2012/13. The review also bore in mind relevant improvement suggestions mentioned in previous annual reviews. The applicability of the Statement was not reviewed this time since the service's new (permanent) Head of Internal Audit takes up his post in July 2013.

OPTIONS AVAILABLE TO THE COMMITTEE

The Audit Committee should note that the review concludes that the internal audit service has been complying with the majority of the requirements of the Public Sector Internal Audit Standards and that consideration be given by the committee and the new Head of Internal Audit to implement the recommendations made with a

¹ The Chartered Institute of Public Finance and Accountancy

² The Institute of Internal Auditors, a body based in the United States with chapters in many countries

view to complying more fully with the standards and to help improve the service's effectiveness.

INFORMATION

1. Background

1.1. The Accounts and Audit Regulations (England) 2011 include the requirement that the council '*must 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*' (6 (1)). Section 6(3) requires the council to conduct a review of the effectiveness of its internal audit at least annually.

1.2. For many years the internal audit service was primarily reviewed against the CIPFA³ Code of Practice for Internal Audit in Local Government (2006). In December 2012 representatives from CIPFA, other professional bodies and the main public sector organisations in the UK agreed a common standard for all internal audit services across the UK public sector. It is based on the IIA's⁴ International Standards, Definition of Internal Auditing and Code of Ethics and is called the Public Sector Internal Audit Standards, PSIAS. CIPFA published a Local Government Application Note for the PSIAS in April 2013 that clarified how the Standards could apply to local authorities. The Note acknowledges the particular context of local authorities.

1.3. The review took into account the requirements of the new PSIAS and applied a checklist supplied with the Application Note to gauge compliance. The review also reviewed the service against the CIPFA Code (since the service was delivered during the year to this Code) and bore in mind relevant improvement items mentioned in previous annual reviews.

1.4. A more detailed explanation of the PSIAS, the local context and the revised internal audit Terms of Reference (Charter) is provided in the report entitled 'Review of the Internal Audit Terms of Reference' elsewhere on this agenda.

2. The Components and Objectives of the Review

2.1. The review comprised:

- a detailed assessment against the PSIAS through the Application Note checklist
- an assessment against the CIPFA Code
- an examination of a sample of audit files and committee reports
- an assessment of the audit planning and review process and of the current staffing and resources
- an appraisal of the Audit Manual and quality assurance actions, audit recording system and Audit Committee minutes
- a review of improvement actions recommended in the last two effectiveness statements.

³ The Chartered Institute of Public Finance and Accountancy

2.2. The objectives were to:

- establish the extent of compliance with the PSIAS and CIPFA Code
- identify any areas where improvements could be made, bearing in mind the imminent arrival of a new Head of Internal Audit.

3. Review Findings

3.1. The internal audit service was found to meet the PSIAS in all material respects, especially if the matters mentioned below are actioned.

- introduce annual declarations of compliance with the PSIAS Code of Ethics for all auditors
- formalise the quality assurance aspects of internal audit work to align more clearly with the PSIAS concept of a quality assurance (QA) and improvement programme (for example, assigning a QA role to an auditor, periodic assessments of conformance, and an annual review of policies and conformance declaration)
- decide either to exclude investigation work from the operational aspects of PSIAS or ensure that relevant documents and processes are incorporated into the Audit Manual.

3.2. The service was found to meet the requirements of the CIPFA Code for 2012/13. The two suggestions made in last year's effectiveness report (to the June 2012 meeting of this committee and not affecting compliance with the Code) related to quality assurance: that the Head of Internal Audit sign off audit terms of reference and occasionally call in audit files where concerns are identified. These recommended actions were partially complied with in 2012/13 and have been taken into account when recommending formalising the QA process. A third suggestion, relating to positioning the internal audit function in relation to significant change projects, was being progressed in 2012/13: internal audit was able to play a more prominent role in some projects, but this could be further developed in the current year.

3.3. Other actions to consolidate particular aspects of the PSIAS into day-to-day auditing are also suggested for consideration in the following areas:

- provide training refresh sessions for auditors that include topics related to ethics, the Terms of Reference (Charter), objectivity and ICT controls
- refresh the Audit Manual to more closely follow the PSIAS, including prompts within forms to include the above items
- introduce bi-annual Standards workshops with audit staff to ensure on-going understanding of the Standards.

3.4. A number of more operational improvement suggestions have been made that the new Head of Internal Audit can consider with his management team. These cover areas such as:

- how further IA can assist in BID programmes to ensure control and risk related issues are effectively addressed
- ensuring fieldwork for planned audits is completed by the end of March, despite the inevitable operational challenges during the year
- enhancing the audit planning and governance process by earlier discussion with heads of service of risks within their area through the Control Assurance Statement process
- reviewing aspects of the service such as the audit performance system, the Audit Manual, audit universe, follow up reviews and graduate trainee scheme.

BACKGROUND PAPERS

NIL