



Committee and Date

Audit Committee

26 June 2014

ANNUAL REVIEW OF THE EFFECTIVENESS OF THE SYSTEM OF INTERNAL AUDIT AND QUALITY ASSURANCE AND IMPROVEMENT PROGRAMME (QAIP) 2013/14

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1. Summary

- 1.1 The Accounts and Audit Regulations 2011 require the Council to conduct an annual review of the effectiveness of its internal audit; Audit Committee is required to review this report and its findings.
- 1.2 This report provides the results of a self-assessment of the Internal Audit Service against the requirements of the Public Sector Internal Audit Standards (PSIAS) which the Chartered Institute of Public Finance and Accountancy (CIPFA) developed in collaboration with the Chartered Institute of Internal Auditors (CIIA) and which came into force on 1st April 2013. Compliance with these standards demonstrates an effective Internal Audit service.
- 1.3 This review should be read in conjunction with the Annual Internal Audit report, found elsewhere on the committee's agenda. When read together they demonstrate the effectiveness of internal audit. The update of the self-assessment has confirmed that the Council continues to operate an effective Internal Audit function. There are no areas where the Internal Audit function is not complying with the Code and whilst there are areas of partial compliance, these are not considered significant and do not compromise compliance with the code.

2. Recommendations

- 2.1 The Committee is asked to consider and endorse, with appropriate comment, the conclusion that the Council has an effective system of internal audit in place that complies with the principles of the Public Sector Internal Audit Standards and has planned improvement activities to ensure full compliance.

REPORT

3. Risk Assessment and Opportunities Appraisal

- 3.1 An effective Internal Audit Service provides, 'an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes'. Thereby providing assurances on the Council's internal control systems by identifying areas for improvement or potential weaknesses and engaging with management to address these in respect of current systems and during system design. Internal Audit will also continue to align its work with the Strategic Risk Register.
- 3.2 The use of a consistent framework for internal audit across the UK public sector has benefits for both partnership working and for internal auditors who work across different parts of the public sector. The standards are designed to drive improvement and lead to better public finance arrangements.
- 3.3 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998 and the Accounts and Audit Regulations 2011.
- 3.4 There are no direct environmental, equalities or climate change consequences of this proposal. Consultation has been used to inform the evidence gathered in support of the self-assessment against the Public Sector Internal Audit Standards (PSIAS).

4. Financial Implications

- 4.1 The Internal Audit service is provided within approved budgets. There may be a small cost to enable an external assessment of Internal Audit's conformance with the PSIAS in compliance with standard 1312 (external inspection) to be conducted. Presently this remains unassessed and information will be provided on this nearer the time.

5. Background

- 5.1 The Accounts and Audit Regulations 2011 6(3), requires the Council to undertake an annual review of the effectiveness of its internal audit and to report the findings of this review to the Audit Committee.
- 5.2 The Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors (CIIA) agreed to collaborate in the development of the internal audit profession in the public sector. As a result, national Public Sector Internal Audit Standards (PSIAS), based upon the mandatory elements of the global CIIA's International Professional Performance Framework have been developed.
- 5.3 The PSIAS came into force on 1st April 2013 and consist of the following:
 - Definition of Internal Auditing;
 - Code of Ethics; and

- Standards for the Professional Practice of Internal Auditing.
- 5.4 The PSIAS replace the Code of Practice for Internal Audit in Local Government in the United Kingdom, last revised in 2006. In local government, the PSIAS are mandatory for all principal local authorities and other relevant bodies subject to the Accounts and Audit (England) Regulations 2011.
- 5.5 In April 2013, CIPFA produced a Local Government Application Note for the United Kingdom Public Sector Internal Audit Standards. This was used to review the Internal Audit service against initially in September 2013, the results of which were reported to Audit Committee. Following this review an improvement plan was proposed to move the service to a position of full conformance. This report reviews the evidence in support of compliance with the PSIAS and the implementation of actions proposed in the original improvement plan.
- 5.6 The PSIAS aim to promote further improvement in the professionalism, quality and effectiveness of internal audit across both the public and private sectors. They reaffirm the importance of robust, independent and objective internal audit arrangements to provide the Head of Finance, Governance and Assurance (the Section 151 Officer) with the key assurances he needs to support them both in managing the council and in producing the annual governance statement.
- 5.7 In complying with the PSIAS Shropshire Council can provide assurances to Internal Audit's external customers of the teams' professionalism, quality and effectiveness.
- 5.8 A summary of the results of the self-assessment by the Audit Service Manager against the PSIAS are summarised in **Appendix A**. The appendix also provides an update against the previously approved improvement plan. The majority of standards are complied with totally. Where there are areas of non-compliance these are detailed below for members to consider further. Where further improvements have been identified in areas of compliance these, along with the actions outlined below, appear in the improvement plan appendix to ensure full conformance to the standards in future.

Areas of potential non-conformance

- 5.9 **Objectivity Standard:** Do internal auditors display objectivity by not taking part in any activity or relationship that may impair or be presumed to impair their unbiased assessment?

Finding: It is felt important that internal audit is consulted during system, policy or procedure development. Auditors have been assigned to business review projects where there is a possibility that internal control systems will be affected. This is seen as an opportunity for internal audit to add value and strengthen internal control arrangements. Where specific auditors have been involved in providing system advice they will be excluded from carrying out the audit as far as possible i.e. another auditor would be allocated to the audit. If this was not possible, it is felt the benefit of using the experience of developing controls and procedures outweighs concerns of independence and the review process will help to ensure that the review and report remain objective and evidenced based.

Therefore there is **partial** conformance. This is not considered to be to the detriment of the principles of auditing and the independent review process helps to mitigate any risks, therefore no actions are proposed.

5.10 **1100 Independence and Objectivity Standard:** Does the Chief Audit Executive (CAE) confirm to the board, at least annually, that the internal audit activity is organisationally independent? The following examples **can be** used by the CAE when assessing the organisational independence of the internal audit activity: The board:

- **approves the internal audit budget and resources plan.**

Finding: It is the responsibility of the Section 151 Officer to ensure that the budget and resources allocated to internal audit are sufficient to ensure delivery of the plan and to report any concerns to the Audit Committee.

- **approves decisions relating to the appointment and removal of the CAE**

Finding: It is the responsibility of the Section 151 Officer to ensure that the budget and resources allocated to internal audit are sufficient to ensure delivery of the plan, including the appointment and removal of the CAE, and to report any concerns to the Audit Committee.

Does the Chief Executive or equivalent undertake, countersign, contribute feedback to or review the performance appraisal of the CAE? Is feedback sought from the chair of the audit committee for the CAE's performance appraisal?

Finding: Both of these activities are now completed.

Therefore **partial** conformance: Governance requirements in the UK public sector would not generally involve the board approving the CAE's remuneration specifically. The underlying principle is that the independence of the CAE is safeguarded by ensuring that their remuneration or performance assessment is not inappropriately influenced by those subject to audit. In the UK public sector, CIPFA advise that this can be achieved by ensuring that the Chief Executive (or equivalent) undertakes, countersigns, contributes feedback to or reviews the performance appraisal of the CAE and that feedback is also sought from the Chair of the Audit Committee.

Further improvement actions proposed to address issues for this standard are:

1. External clients Audit Committee's Terms of Reference will be reviewed as appropriate.
2. Consideration be given to extending the opportunity for Chairs of externally serviced Audit Committees and their key officers to provide feedback, through the Section 151 Officer, on the Audit Service Manager's appraisal.

5.11 1312 External Assessments Standard: Has an external assessment been carried out, or is planned to be carried out, at least once every five years?

Finding: The new standards came in from the 1st April 2013. Therefore, an external assessment under the standards needs to be conducted by March 2018. No plans have been made for such an assessment, but there is every intention to have one when further guidance on the requirements of the assessment is available.

It is likely that the shape and size of the present Internal Audit team will change to reflect the business plans of the Council over the next five years and therefore early completion of such an assessment may only be of short term benefit. Conversely an earlier assessment may inform the delivery of the service going forward. Early discussions with the Section 151 Officer and Audit Committee members have confirmed a preference for a later assessment once more details are known.

Therefore currently we are not conforming to the standard and propose to consider the approach and timing of an external audit assessment with the Section 151 Officer or a self-assessment with 'independent validation' when more guidance is available.

5.12 This is not considered a significant variation in respect of the principles of the PSIAS to require specific mention in the Annual Governance statement since the intention is to comply with the PSIAS within the prescribed time frames once further details are known.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

Accounts and Audit Regulations 2011.
 CIPFA Code of Practice for Internal Auditors in Local Government 2006 – published December 2006.
 Public Sector Internal Audit Standards 2013
 Local government application note for the UK Public Sector Internal Audit Standards. CIPFA
 Completed Conformance Checklist 2013/14 and supporting evidence

Cabinet Member (Portfolio Holder)

Keith Barrow, Leader of the Council and Brian Williams, Chairman of Audit Committee

Local Member N/A

Appendix A: Public Sector Internal Audit Standards 2013 conformance assessment and improvement plan

Public Sector Internal Audit Standards 2013/14 conformance assessment and improvement plan

Standard	Conformance	Observations and actions proposed	When?	Who?
Definition of Internal Auditing	Yes			
Code of Ethics				
Integrity	Yes			
Objectivity	Partially	No action proposed: the independent quality review process of all files and therefore evidence mitigates the slight risks identified in the Audit Committee report		
Confidentiality	Yes			
Competency	Yes	Centrally held training records have been established and updated		
Attribute Standards				
1000 Purpose, Authority and Responsibility	Yes			
1100 Independence and Objectivity	Yes			
1110 Organisational Independence	Yes	The Terms of Reference of external clients Audit Committee's will be reviewed as appropriate to ensure compliance with PSIAS Feedback for the Audit Service Managers appraisal from all clients CEO equivalents and Audit Committee Chairs will be considered	November 2014	Audit Service Manager Section 151 Officer
1111 Direct Interaction with the Board	Yes			
1120 Individual Objectivity	Yes			
1130 Impairment to Independence or	Yes			

Standard	Conformance	Observations and actions proposed	When?	Who?
Objectivity				
1200 Proficiency and Due Professional Care	Yes			
1210 Proficiency	Yes			
1220 Due Professional Care	Yes			
1230 Continuing Professional Development	Yes			
1300 Quality Assurance and Improvement Programme	Yes	There is a QAIP in place however, the IA manual and associated procedures would benefit from a review to include those processes which are now electronic and to reflect the standards	March 2015	Audit Service Manager
1310 Requirements of the Quality Assurance and Improvement Programme	Yes			
1311 Internal Assessments	Yes	There are performance monitoring targets in place and service level agreements with external clients. These will be reviewed to ensure that they stay SMART and efficient in terms of the information used and monitored.	SLA's as they come up for renewal	Engagement Auditor
1312 External Assessments	No	Consider the approach and timing of an external audit assessment with the Section 151 Officer or a self-assessment with 'independent validation'.	March 2018	Section 151 Officer
1320 Reporting on the Quality Assurance and Improvement Programme	Yes			
1321 Use of 'Conforms with the International Standards for the Professional Practice of Internal Auditing'	Yes			
1322 Disclosure of Non-conformance	Yes			
Performance Standards				

Standard	Conformance	Observations and actions proposed	When?	Who?
2000 Managing the Internal Audit Activity	Yes			
2010 Planning	Yes			
2020 Communication and Approval	Yes			
2030 Resource Management	Yes			
2040 Policies and Procedures	Yes			
2050 Coordination	Yes			
2060 Reporting to Senior Management and the Board	Yes			
2070 External Service Provider and Organisational Responsibility for Internal Auditing	Yes			
2100 Nature of Work	Yes			
2110 Governance	Yes			
2120 Risk Management	Yes			
2130 Control	Yes			
2200 Engagement Planning	Yes			
2210 Engagement Objectives	Yes			
2220 Engagement Scope	Yes			
2230 Engagement Resource Allocation	Yes			
2240 Engagement Work Programme	Yes			
2300 Performing the Engagement	Yes			
2310 Identifying Information	Yes			
2320 Analysis and Evaluation	Yes			
2330 Documenting Information	Yes			
2340 Engagement Supervision	Yes			
2400 Communicating Results	Yes			

Standard	Conformance	Observations and actions proposed	When?	Who?
2410 Criteria for Communicating	Yes			
2420 Quality of Communications	Yes			
2421 Errors and Omissions	Yes			
2430 Use of 'Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing'	Yes			
2431 Engagement Disclosure of Non-conformance	Yes			
2440 Disseminating Results	Yes			
2450 Overall Opinion	Yes	The wording of all annual audit opinions have been reviewed to ensure compliance with the PSIAS		
2500 Monitoring Progress	Yes			
2600 Communicating the Acceptance of Risks	Yes	Audit Committee and senior managers received a list of areas identified as 'will not be', or 'are unlikely to be', audited on a regular basis. This communication will be repeated annually.		