

<u>Committee and Date</u>
Audit Committee 27 November 2014

INTERNAL AUDIT CHARTER

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1. Summary

The Internal Audit team works to a Charter which is in compliance with the Public Sector Internal Audit Standards applied in the UK based on the international standards. The Charter is reviewed and considered on an annual basis by the Audit Committee.

2. Recommendations

The Committee are asked to consider and endorse, with appropriate comment, the Internal Audit Charter (**Appendix A**).

REPORT

3. Risk Assessment and Opportunities Appraisal

- 3.1 An Audit Committee has a key function in ensuring and maintaining effective corporate governance arrangements are in place in the Council. The Internal Audit Charter provides evidence of such arrangements in respect of the provision of the Internal Audit function and has been updated to reflect the recent adoption of the Public Sector Internal Audit Standards.
- 3.2 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998. There are no direct environmental, equalities, consultation or climate change consequences of this proposal.

4. Financial Implications

- 4.1 There are no direct financial implications from adopting this Charter.

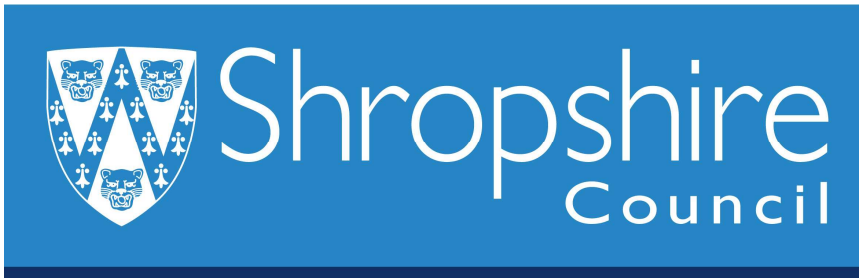
5. Background

- 5.1 Public Sector Internal Audit Standard 1000 requires the Purpose, Authority and Responsibility to be defined in an Audit Charter. In addition the Internal Audit Charter establishes internal audits position within the organisation, including the

nature of the Audit Service Manager’s functional reporting relationship with the Audit Committee; authorises access to records, personnel and physical properties relevant to the performance of audit work and defines the scope of internal audit activities. Final approval of the Internal Audit Charter resides with the Audit Committee.

- 5.2 The Internal Audit Charter should also refer to;
- The nature of assurance services provided to the Council.
 - Organisational independence.
 - Individual objectivity.
 - Impairment to independence or objectivity.
 - Proficiency and due professional care.
 - Continuing professional development.
 - Quality assurance and improvement programme – internal and external.
- 5.3 The charter will communicate the contribution that Internal Audit makes to the Council and includes:
- Internal Audit’s purpose and responsibilities.
 - Independence and objectivity.
 - Competencies and standards.
 - Internal audit planning.
 - Nature of work.
 - Internal audit reporting.
 - Quality assurance.
 - Fraud and corruption.
 - Rights of access.
- 5.4 There are no adjustments recommended for the Charter this year. A copy of the proposed Charter can be found at **Appendix A**.

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; Public Sector Internal Audit Standards 2013
Cabinet Member (Portfolio Holder) Keith Barrow (Leader of the Council) and Brian Williams (Chairman of Audit Committee)
Local Member All
Appendices Internal Audit Charter



INTERNAL AUDIT CHARTER

MISSION STATEMENT

“To objectively examine, evaluate and report on the adequacy of the control environment as a contribution to the proper economic, efficient and effective use of resources for Shropshire Council and our external clients.”

INTERNAL AUDIT CHARTER

INTRODUCTION

1. This charter defines for the Council and the community internal audit activity's purpose, authority and responsibilities consistent with the requirements of the Public Sector Internal Audit Standards (PSIAS)¹. It establishes Internal Audit's position within the Council, including functional reporting relationships with the Audit Committee², authority to access records, personnel and physical properties relevant to the performance of its engagements³; and defines the scope of the Internal Audit activity. Final approval of this Charter rests with the Audit Committee⁴.
2. The PSIAS which encompasses the mandatory elements of the Institute of Internal Auditors (IIA) define Internal Audit as follows: *"Internal Audit is an assurance function that provides an independent and objective opinion to the organisation on the control environment, 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 resource"*.
3. The basis of internal financial administration within the Council lies in the Financial Rules contained in the Council's Constitution. This Charter should be read in conjunction with the relevant sections of these Financial Rules.
4. The authority for the internal audit function is derived from legislation. The requirement for an internal audit function derives from two pieces of legislation: - Section 151 of the Local Government Act 1972 requires that authorities 'make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs'. The Accounts and Audit Regulations 2011, requires that a relevant body 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. (The PSIAS is now the definitive proper practice)

Any officer or member of a relevant body shall if the body requires:-

¹ PSIAS apply the IIA International Standards to the UK Public Sector and have been endorsed as proper practices by CIPFA, the internal audit standard setters for Local Government.

² See glossary for translation of the terms used in the Public Sector Internal Audit Standards in respect of Shropshire Council's Internal Audit activity and those of its external clients.

³ Engagement is the term in the PSIAS used to represent audit work.

⁴ The Audit Committee is referenced in the PSIAS as the Board.

- a) Make available such documents and records as appear to that body to be necessary for the purposes of the audit; and
- b) Supply the body with such information and explanation as that body considers necessary for that purpose. The relevant body shall, at least once in each year, conduct a review of the effectiveness of its system of internal control.

The findings of the review referred to above shall be considered as part of the consideration of the system of internal control.

5. The Financial Rules (Part 4, Appendix C2) state the Section 151 Officer has a 'statutory responsibility for the overall financial administration of the Council's affairs and is responsible for maintaining an adequate and effective internal audit'.
6. In accordance with good practice, this Charter will be reviewed annually by the Audit Committee, after consultation with senior management⁵.

INTERNAL AUDIT PURPOSE AND RESPONSIBILITIES

Purpose

7. Internal Audit led by the Audit Service Manager⁶ is '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.'⁷

Objectives

8. Internal audit's objective is to give assurance and an opinion to the Section 151 Officer, Audit Committee and the Council, on the adequacy of the Council's risk management, governance and control environment and the extent that it can be relied upon, in line with the Accounts and Audit (England) Regulations 2011.

Responsibilities

9. Internal Audit is responsible for conducting an independent appraisal of all the Council's (and that of its external clients) activities, financial or otherwise, including services provided in partnership or under contract with external organisations. It provides this service to the Council and all levels of management.
10. Internal audit complies with the requirements of the Public Sector Internal Audit Standards (PSIAS) including the Definition of Internal Auditing and the Code of Ethics (see **Annex A**) and other relevant guidance; including those issued by individual auditors' professional bodies.

⁵ Senior management comprises of the Head of the Paid Service, Monitoring Officer, Section 151 Officer and directors.

⁶ The Audit Service Manager is the Council's Chief Audit Executive as defined in the PSIAS.

⁷ Source Public Sector Internal Audit Standards April 1st 2013.

11. The scope of internal audit includes:
- reviewing, appraising and reporting on the following:
 - the soundness, adequacy and application of internal controls;
 - the extent to which the Council's assets are accounted for and safeguarded from losses of all kinds arising from fraud and other offences, waste, extravagance and inefficient administration, poor value for money or other causes;
 - the suitability and reliability of financial and other management data developed within the Council;
 - carrying out selected value for money reviews of the efficiency and economy of the planning and operation of the Council's functions;
 - providing a responsive, challenging and informative internal advice and consultancy service for committees and services;
 - undertaking any non-recurring studies as directed by the Section 151 Officer;
 - advising on or undertaking fraud investigation work, with the exception of benefit fraud in accordance with the Council's Fraud Investigation procedure, prosecutions policy and the disciplinary guide. In addition to participating in the National Fraud Initiative; and
 - periodically undertaking an audit needs assessment taking into consideration the authorities risk management process.
12. Internal audit also carry out special reviews or assignments where requested by management, which fall outside the approved work plan and for which a contingency is included in the audit plan.

INDEPENDENCE AND OBJECTIVITY

13. Independence is the freedom from conditions that threaten the ability of the internal audit activity to carry out their responsibilities in an unbiased manner.
14. Objectivity is an unbiased mental attitude that allows internal auditors to perform audit reviews in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others.
15. Threats to objectivity and independence must be managed at the individual auditor, audit, functional and organisational levels.
16. Internal Audit has no executive responsibilities and is independent of the activities that it audits to enable Auditors to provide impartial and unbiased professional evaluations, opinions and recommendations. Internal audit is free to plan, undertake and report on its work as the Audit Service Manager deems appropriate, in consultation with relevant managers.

17. The Audit Service Manager has direct access to the Section 151 Officer, the External Auditor, senior managers, the Leader, Audit Committee and other members as required.
18. The Audit Service Manager fosters constructive working relationships and mutual understanding with management, external auditors and with other review agencies.
19. Constructive working relationships make it more likely that internal audit work will be accepted and acted upon, although the internal auditor does not allow their objectivity or impartiality to be impaired.
20. Internal auditors are required to have an impartial, unbiased attitude characterised by integrity and objectivity in their approach to work. They avoid conflicts of interest and a register of interests is maintained. Audit reviews are planned to ensure potential conflicts are avoided. Auditors should not allow external factors to compromise their professional judgement and must maintain confidentiality in their work.
21. The Audit Service Manager cannot be expected to give total assurance that control weaknesses or irregularities do not exist. Managers are fully responsible for the quality of internal control within their area of responsibility. They should ensure that appropriate and adequate control and risk management processes, control systems, accounting records, financial processes and governance arrangements i.e. the control environment, exist without depending on internal audit activity to identify weaknesses.
22. The Audit Service Manager is to be consulted about significant proposed changes in the internal control system and the implementation of new systems and shall make recommendations on the standards of control to be applied. This need not prejudice the audit objectivity when reviewing the systems at a later date.

COMPETENCIES AND STANDARDS

23. Audits must be performed with proficiency and due professional care. Internal auditors must possess the knowledge, skills and other competencies needed to perform their individual responsibilities.
24. The Audit Service Manager holds a relevant professional accountancy qualification and is suitably experienced. In addition they must maintain a team of staff who are properly trained to fulfil all their responsibilities and continue to enhance their knowledge, skills and competencies through continuing professional development.
25. Internal auditors are expected to:
 - exercise due professional care based upon appropriate experience, training, ability, integrity and objectivity;

- apply confidentiality as required by law and best practice and
- obtain and record sufficient audit evidence to support their findings and recommendations.

INTERNAL AUDIT PLANNING

26. The Audit Service Manager produces the Council's annual risk based audit plan, in consultation with the Section 151 Officer, to establish priorities, achieve objectives and ensure the efficient and effective use of audit resources. The plan takes into account the Accounts and Audit (England) Regulations 2011, the management of risk, previous internal/external audit work, discussions with the Head of the Paid Service and senior managers, external networking intelligence, local and national risks, comments from the Audit Committee and any requirements of the External Auditor.
27. The Plan is subject to regular reviews and revisions as required to reflect changes to the risk environment and these changes are approved when significant. The Plan includes an element of contingency to allow internal audit to be responsive to changing risks and requests for assistance from managers. It is the responsibility of the Section 151 Officer to ensure that the budget⁸ and resources allocated to internal audit are sufficient to ensure delivery of the plan and to report any concerns to the Audit Committee. The Audit Committee agree the annual risk based plan and any significant change to the plan during the year.

NATURE OF WORK

28. The internal audit activity must evaluate and contribute to the improvement of governance, risk management and control processes using a systematic and disciplined approach.

Governance

29. The internal audit activity must assess and make appropriate recommendations for improving the governance process in its accomplishment of the following objectives:
- Promoting appropriate ethics and values within the organisation;
 - Ensuring effective organisational performance management and accountability;
 - Communicating risk and control information to appropriate areas of the organisation;
 - Coordinating the activities of and communicating information among the audit committee, external and internal auditors and management.

⁸ The budget, including the remuneration the Audit Service Manager is approved by Council.

- The internal audit activity must assess whether the information technology governance of the organisation supports the organisation's strategies and objectives.

Risk Management

30. Determining whether risk management processes are effective is a judgment resulting from the internal auditor's assessment that:
- Organisational objectives support and align with the organisation's mission;
 - Significant risks are identified and assessed;
 - Appropriate risk responses are selected that align risks and their mitigation with the organisation's risk appetite.
 - Relevant risk information is captured and communicated in a timely manner across the organisation, enabling staff, management and the board to carry out their responsibilities.
31. The internal audit activity must evaluate the potential for the occurrence of fraud and how the organisation manages fraud risk.
32. When assisting management in establishing or improving risk management processes, internal auditors must refrain from assuming any management responsibility by actually managing risks.

Control

33. The internal audit activity must evaluate the adequacy and effectiveness of controls in responding to risks within the organisation's governance operations and information systems regarding the:
- Achievement of the organisation's strategic objectives;
 - Reliability and integrity of financial and operational information;
 - Effectiveness and efficiency of operations and programmes;
 - Safeguarding of assets; and
 - Compliance with laws, regulations, policies, procedures and contracts.
34. In accordance with the PSIAS, most individual audits are undertaken using the risk based systems audit approach, the key elements of which are listed below:-
- Identify and record the objectives, risks and controls.
 - Establish the extent to which the objectives of the system are consistent with higher level corporate objectives.
 - Evaluate the controls in principle to decide whether or not they are appropriate and can be reasonably relied upon to achieve their purpose.
 - Identify any instances of over and under control.
 - Determine an appropriate strategy to test the effectiveness of controls, i.e. through compliance and/or substantive testing.

- Arrive at conclusions and produce a report, leading to management actions as necessary and providing an opinion on the effectiveness of the control environment.
35. To reduce duplication of effort we will work in partnership to identify and place reliance on assurance work completed elsewhere in the Council and a computerised audit management and working papers system is used to streamline working practices based upon best professional practice.

INTERNAL AUDIT REPORTING

36. Internal audit report their findings in writing to appropriate managers against four assurance opinions (good, reasonable, limited and unsatisfactory). The Audit Service Manager sets standards for reporting and makes arrangements for their review and approval before issue. The reports:
- prompt management action to implement recommendations for change, leading to improvement in performance and control;
 - provide a formal record of points arising from the assignment, and where appropriate, of agreements reached with management;
 - state scope, purpose and extent of conclusions;
 - make recommendations relative to the risk which are appropriate, relevant and flow from the conclusions;
 - acknowledge the action taken or proposed by management; and
 - ensure that appropriate arrangements are made to determine whether action has been taken on internal audit recommendations, or that management has understood and assumed the risk of not taking action.
37. The Audit Service Manager reports regularly to the Section 151 Officer and at least three times a year to the Council's Audit Committee on progress against the annual audit plan and other issues of concern in respect of the control environment and emerging issues. The Audit Committee meet at least four times per year and they have a detailed work plan agreed for the year. In addition, the Audit Service Manager produces an annual report to the Section 151 Officer and Audit Committee on the main issues raised by Internal Audit during the year and on the performance of Internal Audit. In particular the annual report:
- Includes an opinion on the overall adequacy and effectiveness of the Council's control environment.
 - Discloses any qualifications to that opinion, together with the reasons for the qualification.
 - Presents a summary of the audit work undertaken to formulate the opinion, including reliance placed on work by other assurance bodies.
 - Draws attention to any issues the Audit Service Manager considers particularly relevant to the preparation of the Annual Governance Statement.

- Compares the work actually undertaken with the work that was planned and summarises the performance of the Internal Audit function against its performance measures and criteria.
- Comments on compliance with these standards and communicates the results of the Internal Audit quality assurance and improvement programme.

QUALITY ASSURANCE

38. In order to ensure Internal Audit independence, the audit of any areas managed by the Audit Service Manager will be carried out by an appropriate auditor and reviewed by an audit senior. The Audit Service Manager will take no part in the audit or review process other than in the role of auditee. The final report will be issued to the Section 151 Officer as the Audit Service Manager's line manager.
39. The Audit Service Manager will develop and maintain a quality assurance and improvement programme covering all aspects of the internal audit activity and conforming to the relevant standards. This will include an on-going internal assessment covering adequate supervision of work performed, an internal review process and the retention of appropriate evidence. In addition, at least once every five years an external assessment of internal audit by an appropriate person⁹ from outside the Council will be conducted. The timing, form of the assessment, qualifications of any external assessor, results and any improvement plans will be agreed with and reported to the Audit Committee in the annual report¹⁰. Significant deviations will be considered for inclusion in the Annual Governance Statement.
40. The Audit Service Manager develops and maintains a set of performance measures which are reported to the Section 151 Officer and Audit Committee.

FRAUD AND CORRUPTION

41. The Internal Audit Service is not responsible for the prevention or detection of fraud and corruption. Managing the risk of fraud and corruption is the responsibility of management.
42. The Audit Service Manager should be informed of all suspected or detected fraud, corruption or impropriety and will consider the implications for their opinion on the adequacy and effectiveness of the relevant controls, and the overall internal control environment.

RIGHTS OF ACCESS

43. Under the Council's Financial Rules, internal auditors have the authority to:
- Access at reasonable times, premises or land used by the Council.
 - Access all assets, records, documents, correspondence and control systems except for those from which they are statutorily prevented.

⁹ Qualified independent assessor or assessment team

¹⁰ For both internal and external reviews

- Require and receive any information and explanation considered necessary concerning any matter under consideration.
- Require any employee of the Council to account for cash, stores or any other Council property under his/her control and produce supporting evidence and assets for inspection if required.
- Access records belonging to third parties, such as contractors, when required.

Reviewed 27th November 2014

Public Sector Internal Audit Standards

The definition of Internal Auditing within the Standards is: Internal Auditing is 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.

Code of Ethics -

Internal auditors in UK public sector organisations must conform to the Code of Ethics within the Standards. If individual internal auditors have membership of another professional body then he or she must also comply with the relevant requirements of that organisation.

There are four principles in the code of ethics:

1. **Integrity** – The integrity of internal auditors establishes trust and thus provides the basis for reliance on their judgement.
2. **Objectivity** – Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the activity or process being examined. Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgements.
3. **Confidentiality** – Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.
4. **Competency** – Internal auditors apply the knowledge, skills and experience needed in the performance of internal audit services.

Internal auditors who work in the public sector must also have regard to the Committee on Standards of Public Life's Seven Principles of Public Life.¹¹

¹¹ Information can be found at www.public-standards.gov.uk

Glossary of Terms for External Clients where they are different to the Council

Shropshire and Wrekin Fire and Rescue Authority

Senior Management	Chief Fire Officer Treasurer Directors
Board	Audit and Performance Management Committee Fire and Rescue Authority

Oswestry Town Council

Senior Management	Town Clerk
Board	Town Council

STaR

Senior Management	Managing Director and direct reports
Board	Finance, Audit and Risk Sub Committee

West Mercia Energy

Senior Management	Section 151 Officer Managing Director
Board	Joint Committee

Shropshire County Pension Fund

Senior Management	Section 151 Officer Directors
Board	Pensions Committee