



<u>Committee and Date</u>	<u>Item</u>
Audit Committee	
29 June 2017	
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ANNUAL REVIEW OF INTERNAL AUDIT: QUALITY ASSURANCE AND IMPROVEMENT PROGRAMME (QAIP) 2016/17

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1. Summary

- 1.1 The Accounts and Audit Regulations 2015 (5) require the Council to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account Public Sector Internal Auditing Standards (PSIAS) or guidance.
- 1.2 As part of the Service's Quality Assurance and Improvement Programme (QAIP), this report provides the results of a self-assessment of the Internal Audit Service against the requirements of the Public Sector Internal Audit Standards. Compliance with these standards demonstrates an effective Internal Audit Service. Audit Committee is required to review this report and its findings.
- 1.3 This review should be read in conjunction with the Annual Internal Audit report, found elsewhere on this agenda. When read together the two reports 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 employs an effective internal audit to evaluate its risk management, control and governance processes

that complies with the principles of the Public Sector Internal Audit Standards and has planned improvement activities to work towards full compliance where appropriate.

REPORT

3. Risk Assessment and Opportunities Appraisal

- 3.1 The Accounts and Audit Regulations 2015 (section 5) require a relevant authority to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards (PSIAS) or guidance.
- 3.2 Under the PSIAS, Internal Audit's mission is, 'to enhance and protect organisational value by providing risk-based and objective assurance, advice and insight.' 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. 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.
- 3.3 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. Under 1310 of the PSIAS there is a requirement for Internal assessments which include:
- Ongoing monitoring of the performance of the internal audit activity; and
 - Periodic self-assessments or assessments by other persons within the organisation with sufficient knowledge of internal audit practices.
- 3.4 Ongoing monitoring is an integral part of the day-to-day supervision, review and measurement of the internal audit activity and is incorporated into the routine policies and practices used to manage the activity. It uses processes, tools and information considered necessary to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics and the Standards.
- 3.5 This Report provides Members with details of an annual assessment conducted to evaluate conformance with the Definition of Internal

Auditing, the Code of Ethics and the Standards. It is completed by the Head of Audit and discussed with the Section 151 Officer before the results and improvement plan are reported to Audit Committee.

- 3.6 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998. There are no direct environmental, equalities or climate change consequences of this proposal.

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. The Chairman, Section 151 Officer and the Head of Audit have delegated authority to consider the approach/scope of the assessment and agree this with an external assessor and report back to the Committee.

5. Background

- 5.1 The Public Sector Internal Audit Standards (PSIAS) are mandatory for all principal local authorities and were updated in 2017. They consist of:
- Mission of Internal Audit;
 - Definition of Internal Auditing;
 - Core Principles for the Professional Practice of Internal Auditing;
 - Code of Ethics; and
 - Standards for the Professional Practice of Internal Auditing.
- 5.2 The 'Mission' of Internal Audit is, 'to enhance and protect organisational value by providing risk based and objective assurance, advice and insight'. Internal Audit's effectiveness is demonstrated when the following principles are present and operating effectively.
- Demonstrates integrity
 - Demonstrates competence and due professional care
 - Is objective and free from undue influence
 - Aligns with the strategies, objectives, and risks of the organisation
 - Is appropriately positioned and adequately resourced
 - Demonstrates quality and continuous improvement
 - Communicates effectively
 - Provides risk based assurance
 - Is insightful, proactive and future focused
 - Promotes organisational improvement.
- 5.3 In April 2013, CIPFA produced a Local Government Application Note for the United Kingdom Public Sector Internal Audit Standards. Internal Audit is reviewed using this guidance for compliance with the Standards, the results of which are summarised in **Appendix A**.

- 5.4 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 in both managing the financial affairs of the Council and producing the annual governance statement.
- 5.5 In complying with the PSIAS, Shropshire Council can provide assurances to Internal Audit's external customers of the teams' professionalism, quality and effectiveness.
- 5.6 **Appendix A** 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 within the appendix, to ensure full conformance to the standards in future.

Areas of potential non-conformance

- 5.7 **Code of Ethics - 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 is 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.

There is therefore **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.

- 5.8 **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.

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, this is completed for Shropshire Council.

The Section 151 Officer also seeks, as he deems appropriate, opinions from the Chairs of externally serviced Audit Committees and their key officers on the Head of Audit's performance for use in her appraisal.

- 5.9 The above are not considered significant variations in respect of the principles of the PSIAS to require specific mention in the Annual Governance statement.
- 5.10 In addition to the internal assessment, an external assessment was conducted on and reported by CIPFA earlier this year (February 2017). The opinion of CIPFA was that Shropshire Council Audit Services generally conforms to the requirements of the Public Sector Internal Audit Standards and to the requirements of the Local Government Application Note'. The action plan attached in the Appendix shows an updated position on recommended improvements agreed following the external assessment, which were of a minor nature. An external assessment will next be due in five years.

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 2015
- Public Sector Internal Audit Standards 2016

- Local government application note for the UK Public Sector Internal Audit Standards CIPFA
- Completed Conformance Checklist 2016/17 and supporting evidence
- Internal Audit Quality Assurance Improvement Programme – External assessment report, Audit Committee, February 2017.

Cabinet Member (Portfolio Holder)

Peter Nutting, Leader of the Council and Peter M Adams, Chairman of Audit Committee

Local Member N/A

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

Public Sector Internal Audit Standards 2017 conformance assessment and improvement plan

Standard	Conformance	Observations and actions proposed	When?	Who?
Mission of Internal Audit	Yes			
Definition of Internal Auditing	Yes			
Core Principles for the Professional Practice of Internal Auditing	Yes			
Code of Ethics	Yes	S3 ¹ It is suggested that the annual declaration of gifts, hospitality and interests forms completed by every member of SCAS' team is expanded to include sections relating to compliance with the relevant codes of ethics or Committee on Standards of Public Life Seven Principles of Public Life.	Implemented May 2017	
Integrity	Yes			
Objectivity	Partially			
Confidentiality	Yes	2.3.2 Ensure all filing conforms with retention guidelines	Sept 2017	Seniors
Competency	Yes	2.4.3 Set dates for appraisals in first and third quarters	Implemented April and arranged for October 2017	Seniors

¹ Suggestion following CIPFA external assessment

Standard	Conformance	Observations and actions proposed	When?	Who?
Attribute Standards				
1000 Purpose, Authority and Responsibility	Partially	<p>R1² The Charter will include a statement that resources are from a mix of internal employees or contractors dependent on available budgets and resource needs.</p> <p>R2 The Charter definition of Assurance will be updated to read: Overall Assurance is provided on the organisation's risk management, governance and internal control processes to confirm that they are operating effectively. Opinions take into account the expectations of senior managers, the board and other stakeholders and are supported by sufficient, reliable, relevant and useful information. Audit assurance opinions for engagements are awarded on completion of audit reviews reflecting the efficiency and effectiveness of the controls in place and consideration of the engagement results and their significance.</p>	<p>Nov 17</p> <p>Nov 17</p>	<p>Head of Audit</p> <p>Head of Audit</p>
1100 Independence and Objectivity	Partially	R3 The Head of Audit includes a statement specifically confirming that the service has been free from interference	Implemented June 2017	

² Recommendation following CIPFA external assessment

Standard	Conformance	Observations and actions proposed	When?	Who?
		<p>throughout the year in her annual report to the audit committee.</p> <p>R4 A section is added to the audit charter stating that to ensure integrity and objectivity are not impaired, auditors will not audit areas of previous responsibility for a period of at least twelve months after the responsibility ended</p> <p>R5 The Charter section on consultancy will be updated to read 'Any auditor asked to provide consultancy services or undertake a consultancy-style activity should consult their manager or the Head of Internal Audit before agreeing to provide such services. For any significant additional consulting services not already included in the plan, approval will be sought from the Audit Committee prior to accepting the engagement'. In practice any significant change to the plan would be covered in the quarterly reporting to Audit Committee and so would always be reported. Consultancy work by its very nature at times requires an instant response to an assurance request. To allow for this there are approved contingencies in place in the</p>	<p>Nov 2017</p> <p>Nov 17</p>	<p>Head of Audit</p> <p>Head of Audit</p>

Standard	Conformance	Observations and actions proposed	When?	Who?
		plan: unplanned, general advice, and counter fraud. In addition, to ensure transparency, codes are set up for jobs that require more time.		
1110 Organisational Independence	Yes			
1111 Direct Interaction with the Board	Yes			
1120 Individual Objectivity	Yes	3.3.8 Plan to improve the IT skills across the audit team and move the type of audit review conducted by auditors to a more technical one to reflect digital transformation plans. 3.3.9 Review the use of CAATS to assist data transfer/ cleansing and reconciliation of systems	March 2018	Head of Audit/ Principal Auditor IT
1130 Impairment to Independence or Objectivity	Yes			
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	3.4.1.2 Complete this assessment and continue to report to Audit Committee annually along with a high level improvement programme.	Implemented June 2017	

Standard	Conformance	Observations and actions proposed	When?	Who?
		3.4.1.1 Ongoing review of the IA manual and the quality review processes to ensure complete compliance with the standards and suitable guidance for staff	March 2018	Seniors
1310 Requirements of the Quality Assurance and Improvement Programme	Yes			
1311 Internal Assessments	Yes			
1312 External Assessments	Yes			
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	3.4.25 Report outcome of this assessment to June Audit Committee 2017 on compliance with the standards and a resulting QIAP.	June 2017	Head of Audit
1322 Disclosure of Non-conformance	Yes			
Performance Standards				
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	Yes	4.1.36 Continue to ensure senior	March 2018	Head of Audit

Standard	Conformance	Observations and actions proposed	When?	Who?
and the Board		managers are informed of changes in the internal control environment		
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			
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			

Standard	Conformance	Observations and actions proposed	When?	Who?
2431 Engagement Disclosure of Non-conformance	Yes			
2440 Disseminating Results	Yes	<p>S1 It is suggested that a paragraph is included in the standard audit report template regarding the limitations on distribution and the use of the results by external parties. The next review of the standard report template will consider this.</p> <p>S2 It is suggested that the Head of Audit routinely includes greater detail on the audits with limited and no assurance opinions in the progress reports to the audit committee. Audit will consider a greater level of detail in an appendix to performance reports.</p>	<p>Implemented May 2017</p> <p>Implemented from Feb 2017</p>	
2450 Overall Opinion	Yes			
2500 Monitoring Progress	Yes			
2600 Communicating the Acceptance of Risks	Yes			