

Audit Committee



06 June 2008

Review of the effectiveness of the system of Internal Audit

Report of the Head of Internal Audit and Risk Management

Purpose of the report

1. The Council has a new requirement under the Accounts and Audit (Amended) (England) Regulations 2006 to review the effectiveness of its system of internal audit each year. The review has to be considered by a committee of the Council as part of the consideration of the system of internal control, which supports the Annual Governance Statement (AGS).

Supporting Information

2. The CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 sets the Standard for Internal Audit across 11 key areas of activity. In order to inform this review a desktop self-assessment against the checklist was carried out, which in the absence of best practice guidance is the approach currently adopted by a number of high performing County Councils.
3. In seeking to provide independent evidence of compliance with the CIPFA Standard, Internal Audit is able to draw upon the observations of the Audit Commission's triennial review of Internal Audit, which formally identified as part of its 2006/07 programme of work, that "in many respects the division's operations represent best-practice working arrangements". Details of all high priority recommendations for improvement, identified within the action plan that accompanied the External Auditor's report and which were noted by Members at the Audit Committee meeting of 10 December 2007, have now been addressed.
4. Internal Audit activity also helps to support the internal control element of the CPA Use of Resources (UoR), an assessment of which has been completed by the Audit Commission for 2006/07, where a score of 3 (consistently above minimum requirements, performing well) was achieved. An additional source of assurance comes from our customer satisfaction surveys. For 2007/08, the performance of Internal Audit was rated by our customers as good at 1.31 (very good = 1, good = 2, satisfactory = 3, poor = 4).
5. Keeping Members informed of the work of Internal Audit is clearly critical in enabling the Authority to form an opinion on the comprehensiveness and reliability of the Council's key methods of assurance. In this regard, Internal Audit reports on a range of performance measures to Members, formerly to Cabinet and from December 2007, to the Audit Committee on a quarterly basis in accordance with the Audit Charter.

Summary and Key Observations

6. Our assessment against the checklist confirms that Internal Audit complies with the CIPFA Code of Practice in the majority of areas. The assessment, supporting evidence and an action plan of proposed improvements are included as Appendix 2 for Members to consider.

Recommendation

7. Members are asked to consider this report together with the supporting evidence provided and confirm that, subject to implementing those areas identified for improvement, they are assured that the system of Internal Audit for 2007/08 has operated effectively.

Background Papers - **Audit Files & Working Papers**

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Appendix 1: Implications

Local Government Reorganisation

(Does the decision impact upon a future Unitary Council?)

No

Finance

There are no direct financial implications arising for the Council as a result of this report, although we aim through our audit planning arrangements to review core systems in operation and ensure through our broad programme of work that the Council has made safe and efficient arrangements for the proper administration of its financial affairs.

Staffing

None

Equality and Diversity

None

Accommodation

None

Crime and disorder

None

Sustainability

None

Human rights

None

Localities and Rurality

None

Young people

None

Consultation

None

Health

None

Review of the Effectiveness of Internal Audit 2007/08

2006 Code Standard	Evidence of Achievement	Areas for development
<p>1. Scope of internal audit</p> <ul style="list-style-type: none"> • Terms of reference • Scope • Responsibilities in respect of other organisations • Fraud and corruption 	<p>Terms of reference (TOR) reflecting the Code of Practice have been completed, in the form of an Audit Charter, and were approved by the Audit Committee on 10 December 2007</p> <p>Scope of audit work takes into account risk management processes and wider internal control. Audit Plan and Resource levels were reviewed and commented on in a report to the Audit Committee on 21 June 2007 and revised for further consideration on 10 December 2007.</p> <p>The TOR identify responsibilities in respect of other organisations, including all key partnerships and LAAs.</p> <p>The Audit Charter defines audit responsibilities in relation to fraud.</p>	<p>TOR currently being developed for new Unitary Council and will be expanded to identify responsibilities in respect of other organisations, including all key partnerships and LAAs.</p>
<p>2. Independence</p> <ul style="list-style-type: none"> • Organisational independence • Status of head of internal audit • Independence of individual internal auditors • Independence of internal audit contractors • Declaration of interest 	<p>Internal Audit has no management responsibility for the development, implementation or operation of systems.</p> <p>The Head of Internal Audit (HIA) has direct access to those charged with governance as defined within the Council's Financial Regulations. He can report to the Chief Executive, Chair of the Audit Committee and Leader of the Council as appropriate.</p> <p>For administrative and budgetary purposes the Internal Audit Division is part of the Treasurer's Service. The HIA is a member of the Treasurer's Management Team and, as Assistant County Treasurer, his reporting line for operational purposes is direct to the County Treasurer.</p> <p>Auditors are independent of the activity they audit, and have no operational responsibilities, allowing them to perform their duties in a manner which facilitates impartial judgements and recommendations.</p> <p>Individual auditors (including contracted in staff) declare interests and Audit Managers review these and take appropriate action, for example, on the allocation of audit work to avoid the risk of conflicts of interest.</p>	
<p>3. Ethics:</p> <ul style="list-style-type: none"> • Integrity • Objectivity • Competence 	<p>Areas are covered within staff appraisal activity. All qualified staff are subject to professional ethics of relevant body (CIPFA, AAT, IIA)</p>	

2006 Code Standard	Evidence of Achievement	Areas for development
<ul style="list-style-type: none"> Confidentiality 		
<p>4. Audit Committee</p> <ul style="list-style-type: none"> Purpose of the Audit Committee Internal Audit's relationship with the Audit Committee 	<p>TOR for the Audit Committee have been formally approved by full Council on 02 May 2007</p> <p>TOR includes monitoring and reviewing the risk, control and governance processes and associated assurance processes to ensure Internal Control systems are effective and that policies and practices are in compliance with statutory and other regulations and guidance;</p> <p>Reviewing the Council's Accounts prior to approval by the County Council;</p> <p>External and Internal Audit;</p> <p>Risk Management;</p> <p>Making recommendations concerning relevant governance aspects of the Constitution;</p> <p>The HIA attends the meetings of the Audit Committee, reports in his own name on the outcome of audit work, identifying where necessary changes to the audit plan and presents an annual report and opinion on the internal control and risk management framework. DCC Cabinet report 21 June 2007</p>	
<p>5. Relationships</p> <ul style="list-style-type: none"> With management With other internal auditors With external auditors With other regulators and inspectors With elected Members 	<p>Managers are consulted on the audit plan and on the scope of each review to be undertaken.</p> <p>Joint Statements on the working arrangements between Service Management and Internal Audit were agreed at CMT meeting of 29 January 2008</p> <p>Internal Audit networks with a number of other internal review agencies, sharing information on areas of common interest.</p> <p>Good working relationships exist with External Auditor, Joint working arrangements operate and opportunities to maximise audit resources is sought, quarterly meetings are held to discuss progress made.</p> <p>Internal Audit works with Members, particularly the Audit Committee in helping them develop their understanding. Training was provided to Members on 14 November 2007 covering areas of need.</p>	<p>Joint statements should be revised to reflect current arrangements with other bodies eg. DPA and CDDFRA.</p>
<p>6. Staffing, training and development</p>	<p>The skills and competencies required for each post have been determined.</p> <p>Individual training plans are developed and agreed through appraisal.</p>	
<p>7. Audit Strategy and Planning</p>	<p>The Council should have an Audit Strategy that complies with the Code of Practice and has been formally approved by the Audit Committee.</p> <p>Corporate/Service risk registers are considered in conjunction with the Galileo (Audit Management system) risk scoring mechanism in determining the content of the plan (discussion also takes place with SMTs to identify emerging issues). This has been assessed by the Audit Management Team, who also carried out their own risk assessment.</p> <p>Available resources have been compared with the resource needed, and appropriate steps taken to</p>	<p>Audit strategy document currently being developed for new Unitary Council</p>

2006 Code Standard	Evidence of Achievement	Areas for development
	<p>address any identified shortfall.</p> <p>The risk-based Audit Plan was approved by an appropriate Committee see section 1.</p>	
<p>8. Undertaking Audit Work</p> <ul style="list-style-type: none"> • Planning • Approach • Recording and Assignments 	<p>An audit brief is prepared identifying the objectives, scope and approach of each audit review, for agreement with management prior to commencing each review.</p> <p>A risk-based approach is used and an audit opinion is given.</p> <p>Issues are discussed with management as they arise, and formal feedback is given at the end of the visit, prior to completing the report.</p> <p>Standards of submitted electronic working papers are specified and checked by Audit Managers as part of the Galileo approval process.</p> <p>Adequate working papers supporting conclusions drawn and recommendations made are maintained and retained in accordance with defined policy.</p> <p>Reports are issued to appropriate managers in accordance with defined policy.</p>	
<p>9. Due professional care</p> <ul style="list-style-type: none"> • Responsibilities of the individual auditor • Responsibilities of the Head of Internal Audit 	<p>All internal auditors are aware of their individual responsibilities for due professional care.</p> <p>Arrangements are in place to monitor this:</p> <p>Audit Managers review audit working papers and reports.</p> <p>Annual Appraisal and training needs are identified and delivered.</p> <p>A whistle-blowing procedure is maintained.</p> <p>Work is assigned so as to avoid potential conflicts of interest.</p>	
<p>10. Reporting</p> <ul style="list-style-type: none"> • Reporting on audit work • Annual reporting 	<p>Audit reports give an opinion on risks and controls, using approved methodology.</p> <p>Scope of audit is set out in report.</p> <p>Recommendations are prioritised according to risk. Field-work outcomes are discussed with management, action plans agreed in response to recommendations made.</p> <p>Reports are issued to appropriate managers and where necessary, are referred to the risk manager.</p> <p>Assurances are sought from managers on delivery of agreed actions, and appropriate follow-up actions carried out to assess the effectiveness of recommendations.</p> <p>An escalation procedure has been defined within the Joint Statement on the working arrangements.</p> <p>Where necessary, the opinion is revised in the light of the delivery of agreed actions.</p> <p>An annual report to support the Statement on Internal Control was presented to the Audit Committee. The report includes an opinion on the control environment and any qualifications to that opinion. The work on which the opinion is based is set out in the report. The report highlights any significant issues</p>	

2006 Code Standard	Evidence of Achievement	Areas for development
<p>11. Performance, quality and effectiveness</p> <ul style="list-style-type: none"> • Principles of performance, quality and effectiveness • Quality assurance of audit work • Performance and effectiveness of the internal audit service 	<p>Interim reports submitted to Audit Committee every quarter advising of how the opinion is developing.</p> <p>Policies and procedures are defined in an audit manual.</p> <p>Audits are assigned according to the skills mix required and so that there is adequate supervision.</p> <p>Performance measures are defined and results reported to the Audit Committee.</p> <p>Internal quality reviews are undertaken by Audit Manager for all audit work.</p> <p>Client satisfaction surveys are issued with each final report and are summarised in progress report.</p> <p>A desktop self-assessment of the work of internal audit has been undertaken which incorporates other areas of assurance.</p>	<p>Audit manual is to be updated to reflect working arrangements currently being developed for new Unitary Council.</p> <p>Process could be formalised.</p>

CIPFA Code of Practice – Characteristics of Effectiveness

Characteristic of 'effectiveness'	Evidence of achievement	Areas for development
<p>Understand its position in respect to the organisation's other sources of assurance and plan its work accordingly</p>	<p>Internal Audit, identifies other sources of assurance (for e.g. the SIC and risk management processes, and takes this into account when preparing the internal audit plan.</p> <p>There is a mechanism in place for reviewing the effectiveness of the system of Internal Audit.</p> <p>DCC has revised its Code of Corporate Governance and Police and Fire Authority are in the process of conducting similar reviews. Members are requested to endorse the Council's Revised Code of Corporate Governance attached as Appendix 2 of this report for inclusion within the Council's Interim Constitution to be adopted at the Annual Meeting on 23 May</p> <p>Code of Corporate Governance</p>	
<p>Understand the whole organisation, its needs and objectives.</p>	<p>The audit plan demonstrates how audit work will provide assurance in relation to the authority's objectives.</p> <p>Individual audit assignments identify risks to the achievement of those objectives.</p>	<p>Audit plan currently aligned to Services rather than to the authority's objectives</p>
<p>Be seen as a catalyst for change at the heart of the organisation.</p>	<p>Internal Audit participates in the UoR and CPA processes. Supportive role of the audit team is also demonstrated through corporate developments such as corporate governance review and risk management.</p> <p>Also individual assignments or special assignments are also catalyst for change, for example the role of the team regarding value for money.</p>	
<p>Add value and assist the organisation in achieving its objectives.</p>	<p>Demonstrated through individual audit assignments and also corporate work such as risk management, the SIC process, CPA etc.</p>	
<p>Be involved in service improvements and projects as they develop, working across internal and external boundaries to understand shared goals and individual obligations.</p>	<p>Internal audit provides help and advice on request and supports specific projects identified in plan and on ad hoc basis.</p> <p>Also supported management on implementation of the DRIVE project.</p>	
<p>Be forward looking – knowing where the organisation wishes to be and aware of the national agenda and its impact.</p>	<p>When identifying risks and in formulating the plan changes on the national agenda are considered.</p> <p>The audit section maintains awareness of new developments in the services it audits, risk management and corporate governance and disseminates this knowledge to other parts of the local authority.</p>	

Characteristic of 'effectiveness'	Evidence of achievement	Areas for development
Be innovative and challenging - shaping the values and standards of the organisation; providing internal inspection and validation and encouraging service managers to take ownership of processes, systems and policy.	Internal audit has taken an innovative approach to its reporting arrangements by focusing on risks and encouraging managers to develop their own responses to the risks, rather than audit merely wait for recommendations. The aim of this is to encourage greater ownership of the control environment amongst managers. Internal audit will also look to review the process for internal service assessments, and make appropriate recommendations for improvements.	
Ensure the right resources are available – the skills mix, capacity, specialism and qualifications/experience requirements all change constantly.	Staff encouraged to undertake professional qualifications, and relevant training plans linked to staff appraisals are in place. Arrangements are in place to obtain specialist input on IT audit where required.	Skills assessment still to be completed.

Completed by the Head of Internal Audit on: 28 April 2008

OPINION:

Following the above review of the effectiveness of the Audit Division, it is my opinion that the system of Internal Audit within Durham County Council is effective.

Signed..... (Head of Internal Audit)

Reviewed by the Audit Committee on:

Signed..... (Chair of the Audit Committee)