

**Report to:** Audit Committee  
**Date:** 12<sup>th</sup> March 2009  
**Report of:** Gordon Fletcher, Audit Manager  
**Subject:** Review of the effectiveness of the system of Internal Audit for 2008/2009  
**Ward:** All

## **1. Purpose of Report**

- 1.1. The Accounts and Audit (Amendment) Regulations 2006 require councils to review the effectiveness of their system of internal audit once a year and for the findings of the review 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 (previously the Annual Statement of Internal Control), which in turn supports the authority's financial statements.
- 1.2. In essence the purpose of this review is to ensure that the opinion in the annual report of the Head of Internal Audit can be relied upon as a key source of evidence in the Annual Governance Statement.

## **2. Consultation**

- 2.1. Prior to submission to Audit Committee this report has been reviewed by the Council's Management Team on the 16<sup>th</sup> February 2009.

## **3. Position Statement**

- 3.1. This review is based on evidence from a number of sources as shown below: -
- 3.2. The Audit Commission's Annual Governance Report in September 2008, which examined the arrangements for completing the Annual Governance Statement, which includes the Internal Audit function.
- 3.3. The internal control element of the Use of Resources assessment for 2007/2008 has been completed by the Audit Commission, (dated December 2008), where the score attained was 3 (consistently above minimum requirements, performing well) and the assessment was reported to Council in March 2009.
- 3.4. To support this report a detailed self assessment checklist has been completed by myself as Audit Manager and discussed with my Director, the Section 151 Officer and the Head of Financial Management my Head of Service. The assessment is prepared in accordance with the CIPFA Code of Practice (2006) and is set out in Appendix 1.
- 3.5. The following assessment has been made against the characteristics of internal audit effectiveness criteria as suggested by CIPFA's Financial Advisory network and from performance data and quality assurance results carried out. i.e:-

- 3.5.1. The Internal Audit Manager is the Council's key contact for the national fraud initiative (NFI), which provides an element of assurance in terms of fraud prevention. During 2008 data matching exercises were carried out on Benefits, Rents, Payroll and Creditors data.
- 3.5.2. As a member of the Council's Risk Management Strategy Steering Group the Internal Audit Manager continued to support and co-ordinate both strategic and operational risk assessment activity throughout the year, which forms part of the assurance gathering process at service level.
- 3.5.3. The summary of the annual audit work for 2007/2008 achieved against planned work was reported to Audit Committee on 22<sup>nd</sup> May 2008. The 2008/2009 summary will be reported to Audit Committee on the 24<sup>th</sup> March 2009.
- 3.5.4. The Audit Plan for 2008/09 took into account any new areas of risk and significant developments facing the Council over the year. However, because of LGR work most of the audit work concentrated on the main systems of the Council, and the key controls examined areas where the Council may be at risk due to loss of staff due to LGR. Internal audit's focus on risk encourages managers to take greater ownership of risk management and the control environment contributes to improving governance across the Council.
- 3.5.5. Due to LGR no strategic plan was completed, and the annual internal audit plan for 2008/2009, was approved by the Audit Committee on 13<sup>th</sup> March 2008.
- 3.5.6. Provision is made within the annual audit planning process for contingencies and ad-hoc work and if any adjustments during the year were required which would prevent the full achievement of the original plan, and then this would have been reported to the Audit Committee.
- 3.5.7. During 2008/09 the internal audit section did not lose any staff due to LGR (however one member of staff was seconded for 3 months to Durham County Council to help with school audits) and the audit work was delivered by the 'In house' team, which offers a cost effective mixture of flexibility, local knowledge, experience and specialist skills.
- 3.5.8. Every quarter the internal audit manager reports the progress made against the agreed plan to the Audit Committee, and any special investigations are reported separately.
- 3.5.9. The Audit Manager is confident that the 2008/09 audit plan coverage together with other sources of assurance is sufficient to support the annual opinion of effectiveness of Internal Control.
- 3.5.10. The Annual Governance Statement for 2007/2008 was agreed by the Audit Committee on 22<sup>nd</sup> May 2008.
- 3.5.11. Local Performance Indicators for Internal Audit includes feedback from clients in relation to audit work during the year and the results of these are reported every 6 months to the Audit Committee, the latest report being on 11<sup>th</sup> September 2008. That report indicated that the quality of work from the internal audit section is at a high level and that most of the results exceeded the targets set.

3.5.12 The Internal Audit Charter for the Council was last updated and agreed by the Audit Committee on 30<sup>th</sup> November 2006, following changes to the council's constitutional arrangements and the establishment of an Audit Committee.

3.5.13. A benchmarking exercise was previously carried out with other Durham Districts audit teams and reported to Audit Committee on 21<sup>st</sup> December 2006, this identified areas where Internal Audit were performing well and where improvement could be made. Because of LGR no further exercise was planned.

#### **4. Implications**

##### **4.1. Legal Implications.**

It is a requirement of law that the Council maintains an adequate and effective Internal Audit service.

##### **4.2. Financial**

There are no direct financial implications for the Council as a result of this report.

##### **4.3. Policy**

There are no direct policy implications for the Council as a result of this report.

##### **4.4. Local Government Review Implications**

This report does not directly have any implications for LGR as it refers to the 2008/2009 work of Internal Audit. References to Audit Plans beyond 2009/10 will be reviewed within the finance work stream as part of the review process.

##### **4.5. Risk**

There are no direct risk implications for the Council as a result of this report.

##### **4.6. Communications**

There are no direct communications implications for the Council as a result of this report.

#### **5. Corporate Implications**

##### **5.1. Corporate Plan and Priorities**

Priority 2 – Striving for excellence in the workplace.  
SFE2 – To develop the capacity to achieve in the organization.

##### **5.2. Equality and Diversity**

There are no direct implications.

##### **5.3. E. Government**

There are no direct implications.

**5.4. Procurement**

There are no direct implications.

**5.5. Performance Management and Scrutiny**

The assessment provides assurance towards the Annual Governance statement for the Council.

**5.6. Sustainability**

There are no direct implications.

**5.7. 'Well being powers'**

There are no direct implications.

**5.8. Human Resources**

There are no direct implications.

**5.9. Crime and Disorder**

There are no direct implications.

**5.10. Human Rights**

There are no direct implications.

**5.11. Social Inclusion**

There are no direct implications.

**6. Conclusions**

**6.1.** The work of Internal Audit in Easington has been and is subject to regular review internally by the Audit Committee and externally by the Audit Commission. However, in order to fully comply with the regulations there is a need to formalise this review process by bringing together the evidence as shown in this report, which when considered, will provide the Audit Committee with assurance that governance arrangements in this area of work are effective and robust.

**7. Recommendations**

**7.1.** The Committee is asked to consider this report and agree that the Council's system of internal audit is effective, and that this review will form part of the Council's Annual Governance Statement and included in the Council's statement of accounts.

**8. Background Papers/Documents Referred to in Preparing this Report**

Audit Commission reports  
CIPFA Code of Practice 2006  
Audit Committee reports.

## Appendix 1

### CIPFA Code of Practice - Standards

Code standard	Evidence of Achievement	SELF ASSESSMENT
<p><b>1.Scope of internal audit:</b></p> <ul style="list-style-type: none"> <li>• Terms of reference</li> <li>• Scope</li> <li>• Responsibilities in respect of other organisations</li> <li>• Fraud and corruption</li> </ul>	<p>Terms of reference reflecting current Code of Practice were approved.</p> <p>Scope of audit work takes into account risk management processes and wider internal control.</p> <p>Resource levels reviewed and commented on in a report to Audit Committee.</p> <p>The terms of reference identify responsibilities in respect of other organisations, including all key partnerships and LAAs.</p> <p>Terms of reference define audit responsibilities in relation to fraud.</p>	<p>Updated Internal Audit charter approved by Audit Committee 30<sup>th</sup> November 2006.</p> <p>Strategic and Annual plans consider areas within the risk register.</p> <p>Considered during Strategic and Annual Plans. (Audit Committee 13<sup>th</sup> March 2008).</p> <p>Audit Charter refers to SLAs and client responsibilities.</p> <p>Terms of reference are included in Audit Manual.</p>
<p><b>2. Independence:</b></p> <ul style="list-style-type: none"> <li>• Organisational independence</li> <li>• Status of head of internal audit</li> <li>• Independence of individual internal auditors</li> <li>• Independence of internal audit contractors</li> <li>• Declaration of interest</li> </ul>	<p>Audit Manager has direct access to those charged with governance through the Audit Committee.</p> <p>Reports are made in own name to management and to Audit Committee.</p> <p>No conflict of interest between operational responsibilities and audit has been found.</p> <p>Rotation of audit work within the team is the norm.</p> <p>Auditors are required to declare interests and have been vetted.</p>	<p>Monthly 1 to 1s with Chair of Audit Committee and is recorded in Audit Committee Terms of reference.</p> <p>Yes, see reports.</p> <p>Audit Manager has this in mind when allocating audits.</p> <p>Audit Manager considers this when allocating audits.</p> <p>During personnel appointment process.</p>

<p><b>3. Ethics:</b></p> <ul style="list-style-type: none"> <li>• Integrity</li> <li>• Objectivity</li> <li>• Competence</li> <li>• Confidentiality</li> </ul>	<p>Staff appraisal system considers these issues.</p> <p>Significant points have been identified.</p> <p>Staff have been made aware of ethics requirements.</p> <p>Guidance has been circulated.</p>	<p>Included in welfare interviews.</p> <p>None identified.</p> <p>During interview, and included in Audit Manual.</p> <p>Audit Manual on computer, which is accessible to all. Updated by Audit Manager when required.</p>
--	--	--

<p><b>4. Audit Committee:</b></p> <ul style="list-style-type: none"> <li>• Purpose of the Audit Committee</li> <li>• Internal audit's relationship with the Audit Committee</li> </ul>	<p>Terms of reference have been formally approved and are regularly reviewed.</p> <p>They include responsibility for the review of the AGS.</p> <p>Audit committee approves and monitors audit strategy and plans.</p> <p>Head of Internal Audit attends the meetings, reports on the outcome of internal audit work, identifies necessary changes to the audit plan, and presents an annual report and opinion or assurance on the internal control and risk management framework. See Audit Committee papers.</p>	<p>Yes. Audit Committee set up and T of R approved. (Dated 28<sup>th</sup> February 2006).</p> <p>Yes.</p> <p>Yes. See 13<sup>th</sup> March 2008 report.</p> <p>See various reports throughout the year and annual work program for Audit Committee.</p>
--	---	---

<p><b>5. Relationships:</b></p> <ul style="list-style-type: none"> <li>• with management,</li> <li>• with other internal auditors</li> <li>• with external auditors</li> <li>• with other regulators and inspectors</li> <li>• with elected Members</li> </ul>	<p>Managers are consulted on the audit plan and on the scope of each audit.</p> <p>Responsibilities for managers and internal audit are defined in relation to internal control, risk management and fraud and corruption matters.</p> <p>Good working relations established with external audit, including consultation on plan and opportunities for joint working.</p> <p>Sharing of information is undertaken with other internal review agencies.</p> <p>There is liaison with external regulators and inspectors.</p> <p>The responsibilities of internal audit officers and Members, particularly those of the Audit Committee are understood; training of members is carried out as necessary.</p>	<p>See E.Mail sent January /February 2008 to Directors and Heads of Services. Managers are sent planning memo before every audit and given opportunity to discuss scope of audit work. Included in Audit Manual.</p> <p>In Financial Regs. and also refer to fraud and corruption strategy.</p> <p>Various meetings throughout the year when required.</p> <p>Yes. Whenever appropriate.</p> <p>When appropriate eg N.F.I.</p> <p>Various training has been given.</p>
--	--	--

<p><b>6. Staffing, training and development</b></p>	<p>The skills and competencies required of each post have been determined.</p> <p>Actual skills and competencies have been assessed and a gap analysis completed.</p> <p>Individual training and development plans have been agreed through the appraisal process and are delivered.</p> <p>Professional staff are required to complete CPD.</p> <p>Training plan is linked to business plan.</p>	<p>See job descriptions.</p> <p>CIPFA audit skills matrix is carried out annually. (Carried out January 2009).</p> <p>Welfare interviews and above is used annually. (Carried out January 2009)</p> <p>Training record kept by Audit Manager. Staff complete own records.</p> <p>Council's activities are linked to training plan. Eg IDEA, contract audit.</p>
<p><b>7. Audit Strategy and Planning</b></p>	<p>The Audit Strategy complies with the Code of Practice and has been formally approved by the Audit Committee.</p> <p>It is reviewed each year.</p> <p>The risk-based Audit Plan has been prepared in accordance with the strategy.</p> <p>The corporate risk register has been used as the basis of the plan to the extent appropriate according to the extent to which risk management has been implemented in the authority.</p> <p>Assessed by the Audit Manager, whom has also carried out his own risk assessment.</p> <p>Available resources have been compared with the resource need and a report submitted to the Audit Committee setting out proposals on dealing with the shortfall.</p> <p>The annual plan has been Approved by the Audit Committee.</p>	<p>Yes. Included in Annual Audit Plan, see Audit Committee report 13<sup>th</sup> March 2008.</p> <p>Yes. See reports.</p> <p>Yes. See reports.</p> <p>Yes. Included in reports.</p> <p>Yes. Within audit work program, and audit risk matrix.</p> <p>Included in reports to Committee for Strategic and Annual plans.</p> <p>See Committee report 13<sup>th</sup> March 2008.</p>

<p><b>8. Undertaking Audit Work:</b></p> <ul style="list-style-type: none"> <li>• Planning</li> <li>• Approach</li> <li>• Recording and Assignments</li> </ul>	<p>An audit brief is prepared and agreed with management for each audit.</p> <p>A risk-based approach is used and an audit opinion is given.</p> <p>Issues are discussed with management as they arise.</p> <p>Standards of working papers are specified and checked as part of the file review.</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>Planning memo completed for each audit, which is discussed with auditee.</p> <p>CIPFA Audit programmes also incorporates the use of GRACE (General Risk and Control Evaluation) matrices.</p> <p>Yes. Included in audit working papers and reports, if required.</p> <p>Audit Manager completes quality review form after each audit. See working papers.</p> <p>Yes. See audit files.</p> <p>Yes. See audit files. Policy included in Audit Manual.</p>
<p><b>9. Due professional care:</b></p> <ul style="list-style-type: none"> <li>• Responsibilities of the individual auditor</li> <li>• Responsibilities of the Head of Internal Audit</li> </ul>	<p>All internal auditors are aware of their individual responsibilities for due professional care.</p> <p>Arrangements are in place to monitor this:</p> <ul style="list-style-type: none"> <li>• Chief Internal Auditor reviews all audit files and reports.</li> <li>• Appraisal and training.</li> </ul> <p>A whistle-blowing procedure is maintained.</p> <p>Work is assigned so as to avoid potential conflicts of interest.</p>	<p>Recorded in Audit Manual.</p> <p>Audit Manager completes quality review forms. Audit Manger when required carries out operational updates.</p> <p>Included in Financial regs. and Anti Fraud and Corruption Strategy. Reviewed annually.</p> <p>Yes. Audit Manager aware of this when allocating audits.</p>

<p><b>10. Reporting:</b></p> <ul style="list-style-type: none"> <li>• Reporting on audit work</li> <li>• Annual reporting</li> </ul>	<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.</p> <p>Draft reports are discussed with management and action plans agreed in response to recommendations made.</p> <p>Reports are issued to appropriate managers.</p> <p>Where necessary, issues are referred to risk manager.</p> <p>Assurances are sought from managers on delivery of agreed actions.</p> <p>An escalation procedure has been defined and is used as appropriate.</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 Annual Governance Statement is presented to the Audit Committee.</p> <p>The report includes the opinion on the control environment and any qualifications to that opinion.</p> <p>The work on which the opinion is based is set out in the report.</p> <p>The report highlights significant issues.</p> <p>Interim reports are submitted to the Audit Committee advising of how the opinion is developing.</p>	<p>Yes. Included in Action plans that are agreed with auditee.</p> <p>Yes. See audit reports.</p> <p>See action plans.</p> <p>Yes. See draft reports for discussion with auditee.</p> <p>Yes. See reports.</p> <p>Yes. Where appropriate.</p> <p>Timescale included in Action Plans.</p> <p>See various Audit Committee reports.</p> <p>If appropriate, this will be included in the Action Plan comments.</p> <p>Yes. See Audit Committee report 22<sup>nd</sup> May 2008.</p> <p>Yes. See above report.</p> <p>Yes.</p> <p>Yes.</p> <p>Included in Quarterly Internal Audit reports, and Risk Management progress reports by Risk Manager.</p>
--	--	--

<p><b>11. Performance, quality and effectiveness:</b></p> <ul style="list-style-type: none"> <li>• Principles of performance, quality and effectiveness</li> <li>• Quality assurance of audit work</li> <li>• Performance and effectiveness of the internal audit service</li> </ul>	<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 Audit Committee in the annual report.</p> <p>Internal quality reviews are undertaken by the Head of Internal Audit for all audit work.</p> <p>Client satisfaction surveys are issued with each final report and are summarised in annual report.</p> <p>An annual assessment of the work of internal audit is undertaken by the external auditor.</p>	<p>Yes. See Audit Manual.</p> <p>Yes. By Audit Manager and/or Senior Auditor.</p> <p>Yes. See Audit Committee report dated 11<sup>th</sup> September 2008.</p> <p>Yes. See audit files for quality review sheet.</p> <p>Yes. Questionnaire sent out after each audit by Audit Manager. Reported to Audit Committee. (See Committee report dated 11<sup>th</sup> September 2008).</p> <p>Only carried out every 3 years by Audit Commission but a summary is Included in Annual Governance report. (See September 2008 report)</p>
--	---	---