

Audit Committee

30 June 2023

Annual Review of the System of Internal Audit 2022/2023



Report of Paul Darby, Corporate Director of Resources

Electoral division(s) affected:

Countywide.

Purpose of the Report

- 1 To present to Members the annual review of the system of Internal Audit for consideration and comment.

Executive Summary

- 2 This report sets out the outcome of the annual review of the effectiveness of the internal audit service. In undertaking the review, a number of key elements were assessed in order to inform a judgement over whether the service is fulfilling its responsibilities. This included:
 - (a) The structure and resourcing level, including qualifications and experience of the audit team;
 - (b) The extent of conformance with the Public Sector Internal Audit Standards (PSIAS);
 - (c) Ensuring audit work was successfully delivered in the most appropriate areas on a prioritised (risk) basis;
 - (d) The overall performance of the internal audit service.
- 3 The review found that the structure and resourcing level, including qualifications and experience of the audit team, are satisfactory.
- 4 Internal Audit has completed a self-assessment against the key elements of the Public Sector Internal Audit Standards (PSIAS) and CIPFA Local Government Application Note during 2022/23 which demonstrated that the service was **conforming** with the requirements.
- 5 It is a requirement for the service to be externally assessed once every five years. The last external assessment, carried out by the Chartered Institute of Public and Finance and Accountancy (CIPFA), in February 2022, concluded that 'Durham County Council's Internal Audit Service's self-assessment is accurate and as such we conclude that they FULLY

CONFORM to the requirements of the Public Sector Internal Audit Standards and the CIPFA Local Government Application Note’.

- 6 Further to the onset of the COVID-19 pandemic in March 2020, in conjunction with staffing recruitment and retention challenges, it was considered unrealistic at the start of the Internal Audit Year for a detailed 12-month Internal Audit Plan to be compiled due to the need to direct available resources to continue to deliver outstanding client reviews to support the annual assurance opinions for the Internal Audit Year 2021/22, along with continuing to provide assurance work relating to COVID related payments.
- 7 Therefore, an emergent Internal Audit Plan for the period from April 2022 to March 2023 which consisted of an initial six-month plan for the period 01 April 2022 to 30 September 2022 and an indicative plan for the second six-month period, from 01 October 2022 to 31 March 2023 was provided to the Audit Committee in February 2023. It is considered that the 2022/23 plan represented a reasonable view of critical areas for audit review and assurance needs when it was constructed and agreed with Senior Management and the Audit Committee.
- 8 The plan was based on reasonable estimates of available resources and incorporated management requests and referrals, and it was acknowledged that the Internal Audit Plan must continue to be sufficiently flexible to enable assurance to be obtained over current as well as emerging risks, as well as those risks yet to be identified. The final Internal Audit Plan for 2022/23 was presented to Audit Committee for review and approval on 01 July 2022 and was reassessed in September 2022 to take account of current working arrangements, government legislation and available staffing resources.
- 9 Performance management of the Section and for individual auditors is focused on deployment of auditor time to best effect. This has three main elements related to how much time is spent auditing, completion of audits within set timescales and effectiveness of time deployed. The key deliverable for the Section is the completion of the Internal Audit Plan within the year.
- 10 Performance and progress are monitored through Key Performance Indicators (KPIs). These are agreed with the Audit Committee as part of the Internal Audit Charter and allow for benchmarking to assess effectiveness. Performance is monitored throughout the year and although the number of productive days available during the year was below the profiled target, this was a result of ongoing recruitment and retention issues which resulted in only 88% of the planned staffing level being in post through the year. In addition to this, there has also been a long-term sickness absence within the service.

- 11 As a result of the challenges facing the service, it was necessary to reprioritise activities to be delivered within the 2022/23 plan, though importantly this did not require the Chief Internal Auditor and Corporate Fraud Manager to provide any formal Limitation on the Opinion to be provided.
- 12 The service continues to build on its strengths and enhance its reputation. Service delivery remains a key priority in support of the Council's priorities and to help identify and address any risks to the delivery of corporate objectives.
- 13 The service has delivered a reasonable plan of work for the year and it is considered that it has a sound base for carrying out its audit activities and meeting its objectives to provide audit assurance and advisory support to the Council.

Recommendation

- 14 Members are asked to:
 - (a) Note the findings and conclusions of the 2022/23 review of the effectiveness of the system of Internal Audit contained within this report.

Background

- 15 The Accounts and Audit Regulations 2015 Regulation 3 states that –
- ‘A relevant authority must ensure that it has a sound system of internal control which –*
- (a) Facilitates the effective exercise of its functions and the achievement of its aims and objectives;*
 - (b) Ensures that the financial and operational management of the authority is effective; and*
 - (c) Includes effective arrangements for the management of risk.’*
- 16 The Accounts and Audit Regulations 2015 Regulation 6 states that –
- ‘A relevant authority must, each financial year conduct a review of the effectiveness of the system of internal control as required by Regulation 3’.*
- 17 Internal Audit is defined as the means by which the Council assesses its governance and assurance requirements, ensuring that an effective internal control system is in place. Outcomes from the current governance process are evaluated and reported in the Annual Governance Statement.
- 18 To address the Accounts and Audit Regulations requirement, an assessment of Internal Audit has been carried out and is presented for consideration by those charged with governance.

Detailed Review

- 19 A dedicated Internal Audit Service forms part of the system of Internal Audit in the Council. The Service is part of the Resources Service Grouping. It is led by the Chief Internal Auditor and Corporate Fraud Manager. It has strong links with the Risk, Insurance Claims and Corporate Fraud areas and works closely with others across the Council tasked with governance, assurance and risk management. Whilst part of a wider service, it retains its own identity as Internal Audit for the Council.

- 20 The Chief Internal Auditor and Corporate Fraud Manager reports directly to the Corporate Director of Resources but also has direct access to the Chief Executive and the members of the Audit Committee.
- 21 At the start of 2022/23, the team comprised of 17 approved posts (15.35FTE) as well as the Interim Chief Internal Auditor and Corporate Fraud Manager and one apprentice post. This team delivered work for the Council as well as work for a range of external clients including the Pension Fund, Durham Constabulary, County Durham and Darlington Fire and Rescue Authority, New College Durham, Durham and Mountsett Crematoria, Peterlee Town Council, Spennymoor Town Council, Great Aycliffe Town Council, Horden Parish Council, Shotton Parish Council, Monk Hesleden Parish Council and Trimdon Parish Council.
- 22 During the year, three employees retired from the service; namely, one Audit Manager, one Principal Auditor and a part time Senior Auditor. In addition, two full time Senior Auditors left the employment of the council for promotion opportunities available at other neighbouring local authorities.
- 23 A replacement Audit Manager commenced employment in May 2023 and one part time Senior Auditor agreed to continue to work additional hours during 2022/23 to support the delivery of the Internal Audit Plan.
- 24 Following various recruitment campaigns taking place throughout the year, one Senior Auditor commenced employment in April 2022 and another Senior Auditor joined the service in November 2022. At the end of the 2022/23 Audit Year, one Senior Auditor post remained vacant on the staffing establishment and had been re-advertised due to the candidate who was previously selected for the post not taking up the appointment.
- 25 The service has continued to face staffing and operational challenges throughout the year and following the above recruitments taking place, a change to the establishment structure took place during quarter three of the Audit Year, which resulted in one Principal Auditor post and 1.5 Senior Auditor posts being removed from the establishment. These posts were replaced with one Graduate Trainee ICT Auditor post and two Audit Assistant posts and all the new postholders commenced employment after the end of the 2022/23 Audit Year.
- 26 The Vision and Strategy for Internal Audit is described in the Annual Internal Audit Plan and Strategy, the Internal Audit Service Terms of Reference (TOR) within the Internal Audit Charter and it outlines the status of the Section in context with the organisation and defines the principles of how the service operates. The TOR provides appropriate

arrangements to ensure that the Service is sufficiently independent and objective and that there is access to all information and people required to discharge its responsibilities. The requirements of the Public Sector Internal Audit Standards (PSIAS) are reflected in the Internal Audit Charter.

- 27 Arrangements for investigation work are defined in the Council's policies and procedures for Counter Fraud and Confidential Reporting (Whistleblowing) and these are reported to Corporate Management Team and the Audit Committee in the Protecting the Public Purse update reports. The Council's Corporate Fraud Team conduct this work.

Resourcing, Qualifications and Experience

- 28 Audit work was actively managed within the resource available and progress toward delivery reviewed regularly. The focus was maintained on clear scoping and coverage for assurance activity; timing of work and availability of clients; and control over the allocation of resources for in-year requests for support. Alternative means for gaining assurance were assessed and used where appropriate to support audit opinions. Progress and outcomes were regularly reported to Clients, Service Grouping Management Teams, Corporate Management Team and to the Audit Committee.
- 29 The structure of the service reflects the configuration of the Council at Corporate Director level and allows for close client liaison during the year. It is the intention that auditors continue to develop knowledge and client relationships. Where possible auditors will continue to work with similar service groupings to that of 2022/23 in order to offer an element of continuity for clients with whom we have built constructive relationships. We consider this approach continues to be successful in building a better understanding of the Council and its business needs and objectives and the service continues to receive positive feedback from management on this approach. There has been a need for employee rotation for development purposes and to maintain objectivity, this is continually reviewed.
- 30 The service enables the objectives of Internal Audit to be more clearly articulated through the service planning process and is demonstrated in service plans. Key priorities, options for development and service delivery, service objectives assessments of performance and workforce plans are encapsulated in the annual Internal Audit Plan.

- 31 The training and development within the division encourages development through the Chartered Institute of Public Finance and Accountancy (CIPFA), the Institute of Internal Auditors (IIA), the Association of Accounting Technicians (AAT) and Continuing Professional Development (CPD).
- 32 During the year, one auditor further progressed their IIA studies and all other employees hold at least one relevant audit qualification. For CPD, all employees have access to and attended events selected from internal and external training events. Formal internal CPD sessions are held for all employees with individuals keeping records of their CPD based on their professional requirements.
- 33 The following information about qualifications and experience of employees available for audit work as at 31 March 2023 demonstrates the experience and qualification mix.

Experience 2022/23

Auditing Experience	No	%	Public Sector Auditing	%
Up to 1 Year	1	6.7	1	6.7
1 to 5 Years	1	6.7	1	6.7
5 to 10 Years	1	6.7	1	6.7
Over 10 Years	12	80	12	80
Total Employees	15	100	15	100

Qualifications

Accountants (CCAB)	4
Institute of Internal Auditors	2
Institute of Internal Auditors – Training	1
Certified Information System Auditor	1
Association of Accounting Technicians	6
Association of Accounting Technicians – Training	1
Total	15

- 34 The level of experience of audit employees and skills level available remained high based on the substantial number of employees with over 10 years' experience and competencies in specific areas.
- 35 At 31 March 2023, the Service had three vacant posts.

Conformance with UK Public Sector Internal Audit Standards (PSIAS)

- 36 Internal Audit has completed a self-assessment against the key elements of the Public Sector Internal Audit Standards (PSIAS) and CIPFA Local Government Application Note during 2022/23 which demonstrated that the service was conforming with the requirements.
- 37 It is a requirement for the service to be externally assessed once every five years. The last external assessment carried out by the Chartered Institute of Public and Finance and Accountancy (CIPFA) in February 2022 concluded that 'Durham County Council's Internal Audit Service's self-assessment is accurate and as such we conclude that they FULLY CONFORM to the requirements of the Public Sector Internal Audit Standards and the CIPFA Local Government Application Note'.
- 38 The service must be externally assessed once every five years, with the next external review being due in the Internal Audit Year 2026/27.
- 39 All employees comply with the ethics requirements (as described in PSIAS) in relation to the professional role of an auditor. All employees provided an annual declaration of interests for consideration to enable management to ensure that there was enough information to address any potential conflicts of interest which arise during audit activities. Employees are obliged to raise any conflicts or issues with management during the year. Records are maintained for this.
- 40 Quality of audit work was actively managed in year and the achievement of quality standards enabled the Chief Internal Auditor and Corporate Fraud Manager to confirm work has been completed in conformance with PSIAS. Individual audits had an agreed and clear scope; activity was reviewed and assessed for its effectiveness and quality during and after completion of work; and customer feedback was received from post audit questionnaires.
- 41 Liaison with the External Auditor in year was productive and the two services continue to share information and to use this to inform risk assessments and to direct audit activity.

Ensuring the Effective Prioritisation of Internal Audit Work

- 42 Prioritisation of the work of the Service is achieved by the development and delivery of an annual risk-based audit plan. This describes the assurance plans for the Service and includes capacity for flexibility to adjust to changing circumstances and for demand led and urgent work if appropriate. The plan is based on a mix of different types of audit work to ensure that assurance over the systems of governance, risk management and internal control is obtained from a number of different directions and sources.

- 43 The Service’s methodology for establishing audit priorities is aligned with governance and risk management systems. Audit plans are developed through an assessment of risk and assurance needs and are linked to the Council’s overall objectives.
- 44 It is considered that the 2022/23 Internal Audit Plan represented a reasonable view of critical areas for audit review and assurance needs when it was constructed and agreed with Senior Management and the Audit Committee. It was based on reasonable estimates of available resources and with management requests and referrals. An emergent Internal Audit Plan was provided to the Audit Committee in February 2022 and the final internal Audit Plan for 2022/23 was presented to Audit Committee on 24 May 2022.

Performance Measures

- 45 Performance Management of the Section and for individual auditors is focused on deployment of auditor time to best effect. This has three main elements related to how much time is spent auditing, completion of audits within set timescales and effectiveness of time deployed. The key deliverable for the Section is the completion of the Internal Audit Plan within the year.
- 46 Performance and progress are monitored through Key Performance Indicators (KPIs). These are agreed with the Audit Committee as part of the Internal Audit Charter and are used for benchmarking to assess effectiveness. Comparative figures are used to consider areas for closer review.
- 47 Key performance measures for the Section over the last 12 months are:

KPI	Measure of Assessment	Target	Actual as at 31 March 2023
<i>Efficiency Measure - to provide maximum assurance to inform the annual assurance opinion</i>			
Productive audit time achieved	% of planned productive time from original approved plan completed as at 31 st March.	90%	80%
Timeliness of Draft Reports	% of draft reports issued within 20 working days of end of fieldwork/closure	100%	96% (72 out of 75)
Timeliness of Final Reports	% of final reports issued within 10 working days of receipt of management response	100%	96% (73 out of 76)

KPI	Measure of Assessment	Target	Actual as at 31 March 2023
Quarterly Progress Reports	Quarterly progress reports issued to Corporate Directors within one month of end of period	100%	100%
<i>Quality Measure – To ensure the service is effective and adding value</i>			
Recommendations agreed	% of Recommendations made compared with recommendations accepted	95%	100%
Post Audit Customer Surveys	% of customers scoring audit service satisfactory or above (3 out of 5) where 1 is poor and 5 is very good	100%	98% (64 out of 65) Av. score of 4.7
Customers providing feedback responses	% of customers returning satisfaction returns	70%	83%

- 48 Throughout the year the service faced ongoing staffing shortages and operational challenges which have continued to impact on the delivery of the overall plan. These challenges have included vacant posts (resulting in only 88% of the planned staffing level being in post through the year). Over and above this, there has also been a long-term sickness absence, of a Senior Auditor, from late September 2022 to early March 2023.
- 49 This has resulted in a reduction in the number of productive days available during 2022/23, which were originally estimated to be 3,241, however, as at 31 March 2023, the service had delivered 2,595 productive days, representing 80% of the total estimated planned days for the year. The target to the end of March was for 90% to have been delivered, therefore performance was below the profiled target.
- 50 This was a result of the challenges facing the service which included vacant posts on the staffing establishment which resulted in only 88% of the planned staffing level being in post through the year.
- 51 As such, the service regularly reviewed the content of the plan to ensure that the audits included in the plan are prioritised on a risk basis and to ensure that all key financial systems and high-risk areas of activity are reviewed on an annual basis. As at 31 March, approximately 79% of the audits in the revised plan had been delivered and the Chief Internal Auditor is able to issue an assurance opinion on the adequacy of the internal control environment in place.

- 52 The issuing of draft reports is an assessment of the timeliness of the audit activity from the completion of a piece of work to the issuing of a draft report for consideration and response. The issuing of final reports is a measure of the receipt of the requirement management responses to audit recommendations raised and agreed, to the issuing of final reports to the relevant individuals.
- 53 Performance for the issuing of reports fell slightly short of the profiled target as a result of the ongoing recruitment and retention challenges posed throughout the year, coupled with an Audit Manager's sickness absence which resulted in three reports been issued later than the target timescales.
- 54 Progress reports were issued to Corporate Directors within the required timescales and in turn, quarterly progress reports are presented to Audit Committee.
- 55 There continues to be a positive response to customer satisfaction returns and positive feedback on a number of specific assignments, which is reflected in the customer satisfaction questionnaires.
- 56 No concerns have been raised in relation to the application of professional standards for audit work and there have been no formal complaints.

Implementation of Recommendations

- 57 The process for monitoring the implementation of recommendations continues to work well and there are good levels of engagement from all services across the Council. Working closely with managers allowed for greater understanding of the challenges faced and in ensuring practical recommendations were made and alternative solutions considered in order to address risk.
- 58 Internal Audit continues to engage with the Council's quarterly reporting process and deliver regular quarterly reports to Service Grouping Management Teams and to the Corporate Management Team/Senior Officer Group. This process has ensured that time is targeted on key issues and that appropriate support and advice is offered at the right time.
- 59 The Audit Committee is provided with regular updates from the Service during the year and have the opportunity to challenge progress and outcomes. This includes asking senior managers to provide updates as necessary where there is felt of be a significant risk or concern. This process has provided an effective method for obtaining assurance during 2022/23.

Audit Committee

- 60 The system of Internal Audit includes the role of the Audit Committee and in particular its role in the receipt and evaluation of audit reports, both in terms of assurance opinions and in the ensuring that appropriate arrangements are in place for the delivery of an effective service.
- 61 Further to the Local Government elections, new Audit Committee Members were elected in May 2021. As part of the Member induction, Members received comprehensive training on the role of Audit Committee members in June 2021 and they also received Risk Management training in July 2021. The arrangements for the Audit Committee remained the same during 2022/23. A review of the effectiveness of Audit Committee will be carried out during 2023.
- 62 Audit Committee request reports from management in response to issues raised in within Internal Audit reports, demonstrating the positive steps being taken by the Committee to seek assurance over actions being taken to respond to concerns.

Summary and Key Priorities

- 63 The service continues to build on its strengths and enhance its reputation. Service delivery remains a key priority in support of the Council's priorities and to help identify and address any risks to the delivery of corporate objectives. The service delivered a reasonable plan for the year and it is considered that it has a sound base for carrying out its audit activities and meeting its objectives to provide audit assurance and advisory support to the Council.

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Appendix 1: Implications

Legal Implications

The Accounts and Audit Regulation 2015 (Part 2, Section 5) states a relevant authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal audit standards or guidance.

Completion of the review of the effectiveness of internal audit ensures compliance with both the Public Sector Internal Audit Standards 2017 and the Accounts and Audit Regulations 2015

Furthermore, Internal Audit assists the Corporate Director of Resources in fulfilling their duties under Section 151 of the Local Government Act 1972 which requires each Local Authority to make arrangements for the proper administration of their financial affairs.

Finance

There are no direct financial implications associated with this report.

Internal Audit work has clear and direct effects, through recommendations made, to assist in improving value for money obtained, the probity and propriety of financial administration, and / or the management of operational risks.

Consultation

All Corporate Directors and Heads of Service.

Equality and Diversity / Public Sector Equality Duty

There are no equality and diversity / public sector equality duty implications as a result of this report.

Climate Change

There are no climate change implications as a result of this report.

Human Rights

There are no human rights implications as a result of this report.

Crime and Disorder

There are no crime and disorder implications as a result of this report.

Staffing

The report presents the internal audit services 16.35 FTE (18 posts) and the relevant experience within the service.

Accommodation

There are no accommodation implications as a result of this report.

Risk

The key risk is that the internal audit service is not effective. To mitigate this risk, a defined process exists within the Service to carry out effective performance management and as such assurance is reflected in reports to the Audit Committee. Any issues with performance would be reported to the Audit Committee where further action would be agreed and overseen. To provide further assurance an external assessment is required every five years with the last external review being completed in 2022 which delivered a positive outcome.

Procurement

There are no procurement implications as a result of this report.