



Welland Internal Audit Board FINAL REPORT

Welland Internal Audit Consortium : External Quality Assurance Feedback
QA review date: June 2013

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1. EXECUTIVE SUMMARY

1.1. BACKGROUND

Introduction

The Welland Internal Audit Consortium provides Internal Audit Services to five Councils who are each stakeholders in the Consortium: Rutland County Council, Corby Borough Council, Harborough District Council, East Northamptonshire Council and Melton Borough Council.

The Internal Audit team is “hosted” by Rutland County Council. However, each Council has an individual Internal Audit plan and the Internal Audit team report to an Audit Committee, or equivalent, for each Council.

The Welland Internal Audit Board, via the Interim Strategic Director for Rutland County Council, has proactively sought an external review of the Welland Internal Audit Consortium. This proactive review was to undertake an External Quality Assessment (EQA) to assess any gaps in conformance with the newly established Public Sector Internal Audit Standards (PSIAS), derived from the Institute of Internal Auditors International Professional Practices Framework (IPPF). The PSIAS were published in December 2012 and replaced the CiPFA internal auditing standards for Local Authorities from 1 April 2013.

What is an EQA?

To conform with the PSIAS, heads of internal audit must put in place a quality assurance and improvement programme to evaluate conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The programme should also assess the efficiency and effectiveness of the internal audit activity and identify opportunities for improvement. Furthermore, the standards set out that this programme should have both internal and external quality assurance elements, and that the external quality assurance element (an EQA) should be undertaken at least once every five years.

1.2. SCOPE

The Consortium Head of Internal Audit reported to each of the five councils’ Audit Committees in the Internal Audit Annual Reports for 2012/13 that the Consortium did not fully comply with the CiPFA Code of Practice for Internal Auditing (the predecessor to the PSIAS).

As such the purpose of this EQA is to provide in effect a “base line assessment” through feedback on whether the internal audit activity is as it was being delivered in 2012/13 in conformance with PSIAS

Limitations

In undertaking this review there are a number of limitations to our testing and thus our conclusion provided from this review. These are summarised below.

Whilst we have spoken to respective Audit Committee (or equivalent) Chairs where they have been available and undertaken a desk top review of the Internal Audit reports to the Committees we have not undertaken any specific work to assess the effectiveness of the individual Council Audit Committees.

We have not re-performed any internal audit testing or undertaken any testing across the eight audit assignments reviewed and therefore our view as to the general compliance with the PSIAS cannot be taken as any assurance on the strength of the control environment in those areas covered by the sampled audit assignments.

We have not undertaken comprehensive substantive testing to confirm the accuracy of the information presented or viewed when forming our conclusion and as such our work cannot be taken to give assurance on the accuracy and validity of the underlying information, for example the qualifications cited as held by the respective Audit Managers, or the performance data within the Galileo Internal Audit software.

Welland Internal Audit Consortium: External Quality Assurance Feedback

Our findings are based on a review of a sample of eight files (selected by the Board), discussions with members of Internal Auditing Team, review of internal audit reports and documentation, and discussions with each Council's S151 officer (or where more appropriate a deputy S151 officer) and the Audit Committee (or equivalent) current or former Chairs where they have been available for a call at the time of this review.

It should also be noted that this report does not include detailed findings from the sample file reviews undertaken but these findings have used to support our recommendations and opportunities for improvements. We have provided feedback to the Head of the Consortium to enable learning points to be provided to the Team.

1.3. CONCLUSION

Based on the work we have undertaken, the Internal Audit Service being provided by the Welland Internal Audit Consortium is partially in conformance with the new Public Sector Internal Audit Standards.

As part of this work eight assignments and their respective reports were subject to our review. Our view based on the desk top review of the evidence and processes applied is that for each assignment, the opinion provided by Internal Audit on the control environment tested was correctly categorised as providing either "positive" or "negative" assurance.

Our review has highlighted a number of areas where improvements should be made, the main ones being

- Internal Audit needs to use risk based auditing and move away from using expected controls in order that the actual controls being operated are evaluated.
- Internal Audit needs to be clearer in their planning and reporting on what their opinions cover, including a better structure to the scope and limitations of the review.
- Internal Audit should look to proactively seek out every opportunity to add value by providing information on "good practice" operated across the Consortium's client base or to undertake thematic reviews across the Councils.
- The Consortium should improve the transparency of reporting to the Internal Audit Board and Audit Committees with regards the time spent on each assignment and subsequent changes to internal audit plan. This will lead to more focus on outputs and outcomes instead of the current focus on internal audit resource input.

The Head of the Audit Consortium recognises that there is work that is needed to demonstrate conformance with the PSIAS and has through presentations to the respective Audit Committees and the Internal Audit progress papers to each Committee started to have the dialogue on these areas. Following the appointment of the Deputy Head of the Consortium, there are now three experienced and skilled senior team members of the Consortium who, based on our discussions with them, have a desire to deliver the improvements recommended in this report. There is no reason why the existing delivery model should not deliver the required improvements but the Board will need to ensure that leadership of the team is strong, is focused on performance improvement and delivering better outcomes and does not underestimate the extent of change required.

Whilst the recommendations and improvement opportunities are made for the Consortium Head of Internal Audit to consider and action, the Welland Internal Audit Board needs to recognise that to deliver these improvements each Council has a role to play.

It is also worth noting that currently the cost of Internal Audit is relatively low per potential internal audit available day supported by negotiated low daily rates for contractor support.

Therefore each Council will have to consider the relative cost, either direct or through reduced but focused work, in supporting and facilitating Internal Audit in changing its emphasis from expected controls to a risk based approach.

Our findings are reported on an exception basis; only points where a recommendation has been made or an opportunity for enhancement has been identified have been reported. We provide at Section 3 a list of all standards within the PSIAS, and our view of the Consortium's conformance with each.

1.4. HEADLINE FEEDBACK

The main findings for the Consortium Head of Internal Audit to consider and address to ensure conformance with the Standards are:

- **Role of internal audit:** The internal audit charter needs updating to ensure it addresses fully the requirements within the new standards. This will also support clarity over internal audit resourcing and formalise the agreement between the Consortium and each of its clients. [Attribute Standard 1000]
- **Internal audit approach and manual:** The internal audit manual needs a comprehensive update to ensure that it removes references to outdated processes and those being updated to comply with the new standards and the recommendations made in this report. [Performance Standard 2040]
- **Internal audit approach:** The approach adopted by Internal Audit has been to design testing matrices detailing "expected controls" to guide the Internal Auditor in the delivery of the review. For each of the Council's key financial systems a guiding factor in the development of these matrices has been to satisfy the external auditor and gain their reliance on the work of Internal Audit under the "managed audit approach". This approach does NOT facilitate the identification of the system's actual controls and the determination of a testing programme based on assessing the real risks within the system under review. [Performance Standards 2200 and 2300] Whilst not expressly within the scope of this review, the QA reviewer noted that the Internal Auditor by following an expected controls approach did not test areas within the work reviewed that they would have expected to have been reasonably covered in respect of potential system risks. For example, within the income audit that the risks in respect of the credit card income specifically in respect of the security of that data was not covered, albeit the scope of this review stated that it did cover the credit card income stream.
- **Internal audit scoping:** In planning each specific internal audit assignments there will realistically be limitations on the actual scope that will be undertaken. The current approach adopted by the Consortium is that these limitations are not explicitly documented in the assignment Terms of Reference or the assignment reporting itself. [Performance Standard 2200]
- **Internal audit reporting:** The progress reports to the respective audit committees, whilst reflecting specific Authority requirements, do not;-
 - draw out the potential impact on the Council's annual governance statement of the identified control deficiencies.
 - report in summary the outcomes of the specific reviews instead with reliance being made on the emailing of the full reports to Audit Committee Chairs. However these summaries are included in the Internal Audit Annual Report along with some comparison information if the opinion level is comparable to or better or worse than that given in that area in the previous review.

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- transparently report the “real” resources used to deliver each review to allow a better understanding of the real time taken to deliver the level of assurance required to inform future internal audit plans. It may also be useful to include if that variances is due to training new staff members, as this time should if the team remain stable not need to be repeated each year.

[Performance Standards 2400 and 2500]

- **Staff development:** The manager QA process applied to the work undertaken by the Auditors, or peer QA process applied to the respective three Audit Managers (who act as the Heads of Internal Audit) does not expand to the formal recording of personal development points. [Performance Standard 2300]

As part of our work we identified a number of opportunities to improve or enhance current processes

- **Internal audit testing and evidence:** there are opportunities to strengthen the evidence retained by the internal auditors, especially where element of control testing is referring to actual testing undertaken within other reviews.
- **Audit assignment planning:** there is an opportunity to redesign the current audit Terms of Reference to include a client manager / audit sponsor comments box to encourage greater engagement of clients in the scoping of internal audit reviews.
- **Internal Audit Annual Plans:-** there is an opportunity when drafting the individual Council Internal Audit Annual plans for the Consortium to consider opportunities to add extra value through potential joint reviews across some or all of the Councils.
- **Assignment reporting:** there is an opportunity for the audit team to include within many of the individual assignment reports a section benchmarking the auditors findings with those from similar reviews undertaken across the Consortium’s other clients. This could include a simple comparison of the opinion provided and number / categories of recommendations made through to more added value comparisons of different control configurations and the cost / control benefits they could bring.
- **Audit Committee training:** in many of the conversations we had with the Audit Committee representatives (current or recent chairs of the respective Committees) there was an eagerness for training to be given on the role of the Audit Committee and how they should work with and challenge / hold to account Internal Audit. In a number of the conversations there was also a recognition that in the recent months more training had been provided by Internal Audit.

Whilst the recommendations and improvement opportunities are made for the Consortium Head of Internal Audit to consider and action, the Welland Internal Audit Board needs to recognise that to deliver these they will have a role to play, especially in support they can give regarding their resource allocations to the Internal Audit Consortium and their expectations of the number of days required as they support and facilitate Internal Audit’s change of the emphasis from expected controls to a risk based approach. In making this change there is an increased opportunity for internal audit to focus on the key risks of the Councils and to add value by providing assurance to management and Audit Committees in those risk areas.

2. Feedback and EQA Findings

2.1. INTERNAL AUDIT CHARTER AND INTERNAL AUDIT MANUAL

The Standards require there to be an Internal Audit Charter, and set out a number of topics that should be included within the Charter. Whilst the Consortium has established a Charter this was written before the introduction of the new PSIAS standards in April 2013.

Also with the introduction of the new Standards there is an opportunity to update the Consortium’s Internal Audit Manual to remove outdated sections / elements covering such areas as the issuing of “none contentious” reports, the use of a “limited assurance methodology” for the fundamental financial systems to reduce the risk of confusion for junior staff when they are referring to the Manual.

Recommendation	
1	The Internal Audit Charter should be updated to address the requirements of the newly introduced Standards.
<p>Management response:</p> <p>Agreed.</p> <p><i>The IIA has produced a template which is being used to ensure that a revised Charter addresses all of the new requirements specified in the PSIAS. It should be feasible to seek Audit Committees’ endorsement of a revised Charter in the September cycle of meetings. Early adoption of a fully compliant Charter would be helpful in the context of Member training – Members would have access to a clear statement of their on-going roles and responsibilities that should help them to understand the purpose and significance of training offered.</i></p>	

Recommendation	
2	The Internal Manual should be updated to remove outdated material and also for it to reflect the new Standards. There is also scope to streamline the manual to make it more user friendly for auditors.
<p>Management response:</p> <p>Agreed.</p> <p><i>The current Manual’s design reflected a need to demonstrate clearly to External Audit the extent of compliance with the 11 Standards prescribed in the CIPFA Code of Practice. Intention is to break the revised Manual into two parts: Part 1 will deal with Attribute Standards and other issues of management responsibility; Part 2 will focus on how audit assignments are to be planned, undertaken and quality assured.</i></p> <p><i>Timescale for completing Part 2 will reflect the time needed to ensure that changed working practices deliver the desired outcomes before they are formally codified. Delivery should be feasible by 31st March 2014.</i></p>	

2.2. INTERNAL AUDIT ASSIGNMENTS

Eight assignments and their respective reports have been reviewed as part of this assessment. Our view based on the desk top review of the evidence and processes applied is that for each assignment, the opinion provided by Internal Audit on the control environment tested was correctly categorised as providing either “positive” or “negative” assurance.

There were a number of individual areas that could have been improved for each of the reviews and we have summarised below the common themes from this element of our work, these being:

- The approach adopted by Internal Audit has been to design testing matrices detailing “expected controls” to guide the Internal Auditor in the delivery of the review. For each of the Council’s key financial systems a guiding factor in the development of these matrices has been to satisfy the external audit rely on the work of Internal Audit under a “managed audit approach”. This approach does NOT facilitate the identification of the system’s actual controls and the determination of a testing programme based on assessing the real risks within the system under review.
- In planning the Audit and its subsequent reporting the limitations to the Auditors opinion and breadth of testing undertaken for the area under review are not explicitly documented. Without including this, the reader of the report and its opinion may feel that the opinion provides wider assurance than the actual testing, which is fully reported in the main body of each report, actually provides.
- There are opportunities to strengthen the evidence retained by the internal auditors, especially where testing is referring to testing undertaken in other reviews.
- Given the scope of the work undertaken by the Consortium across the five Councils there is an opportunity for the audit team to include within many of the individual assignment reports a section benchmarking the auditors findings with those from similar reviews undertaken across the Consortium’s other clients. There is also the opportunity for the Consortium to consider the potential to add value through joint reviews across some or all of the Councils.
- There is an opportunity to redesign the current audit Terms of Reference to include a client comments box to encourage greater engagement by client in the scoping of the reviews.

Recommendation	
3	The approach adopted by Internal Audit should move away from utilising “expected controls” to direct the Internal Auditor’s testing to a “risk based” approach whereby the actual controls mitigating the system risks are determined and then tested.
<p>Management response:</p> <p>Agreed.</p> <p><i>Work is in hand to change the design of matrices to direct the Auditors towards the identified risks that need to be mitigated and to require them to identify controls in place: process of redesign remains work in progress which has yet to be formally codified. The Audit Managers are providing more direct support and guidance to Auditors during field work in recognition of their limited experience. In the short-term this will have resource implications. Delivery – including codification in Manual – 31st December 2013.</i></p>	

Recommendation	
4	In planning the Audit, and its subsequent reporting, the limitations to the Auditor’s opinion and breadth of testing in the area under review should be explicitly documented.
<p>Management response:</p> <p>Agreed.</p> <p><i>Scoping exercises now seek to get the clients to identify more clearly the specific risks for which assurance is required and to agree assignments where resources available are consistent with the assurance sought. Reporting format is under review: as ongoing assignments get to draft report stage the need to clarify range and limitations is being assessed. Arrangements have yet to be formally codified and Audit Managers are liaising closely to ensure consistency as new approach is being developed. . Delivery – including codification in Manual – 31st December 2013.</i></p>	

Opportunity	
a	Where Audit testing is cross referenced to other Internal Audit work then there is an opportunity to strengthen the usefulness of this cross referral by drawing into the report the outcome of this actual testing undertaken elsewhere. This allows the reader of the report to see the full outcome of all relevant testing without have to refer to other reports to which they may not have to hand.
<p>Management response:</p> <p><i>Cross referencing was introduced as a way of avoiding repetitive testing when carrying out audits of all of a client’s key financial systems towards the end of the financial year – in line with the Managed Audit approach. It is considered unlikely that there will be a need to adopt this approach in future but if it is outcomes will be reported / summarised in all relevant reports.</i></p>	

Opportunity	
b	There is an opportunity for the audit team to include within many of the individual assignment reports a section benchmarking the auditors findings with those from similar reviews undertaken across the Consortium’s other clients. This could include a simple comparison of the opinion provided and number / categories of recommendations made through to more added value comparisons of different control configurations and the cost / control benefits they could bring.
<p>Management response:</p> <p><i>There have been discussions with relevant client officers about the scheduling of work and – more particularly – final reporting to allow for shared learning on some of the 2013/14 assignments where shared learning/shared good practice is likely to arise (Data Managing; Benefits/Welfare Reform; Local Taxation).</i></p>	

Opportunity	
c	There is an opportunity for the Consortium to consider the potential to add value through joint reviews across some or all of the Councils.
<p>Management response:</p> <p><i>As part of the process for developing Annual Audit Plans for 2014/15 and future years, clients will be offered the opportunity to commission joint reviews of areas of activity where there is a shared requirement for assurance.</i></p>	

Opportunity	
d	There is an opportunity to redesign the current audit Terms of Reference to include a client comments box to encourage greater engagement by client in the scoping of the reviews.
<p>Management response:</p> <p><i>The Terms of Reference document has now been modified to prompt clients to identify any specific issues of assurance. The effect of this change may be to highlight lower than appropriate levels of client engagement in the scoping of audit assignments.</i></p>	

2.3. REPORTING TO THE AUDIT COMMITTEE

Currently Internal Audit report to each Audit Committee their progress against the respective Internal Audit Annual Plan, performance against a number of performance indicators including resourcing issues and general information for example on conformance with what were the previous Internal Auditing Standards. The Consortium has for 2013/14 positively sought to redesign the progress report to map the specifically planned work to the Council’s risk areas (e.g. financial, IT, fraud etc). However these reports do not;-

- draw out the potential impact on the Council’s annual governance statement of the identified control deficiencies.
- report in summary the outcomes of the specific reviews instead of reliance being made on the emailing of the full reports to Audit Committee Chairs. Such summaries are included in the Internal Audit Annual Report along with some comparison information if the opinion level is comparable to or better or worse than that given in that area in the previous review which provides a structure that could be applied to an updated progress paper.
- transparently report the “real” resources used to deliver each review to allow a better understanding of the real time taken to deliver the level of assurance required to inform future internal audit plans. It may also be useful to include if that variances is due to training new staff members, as this time should if the team remain stable not need to be repeated each year.

Recommendation	
5	<p>The Audit Committee progress paper should be redesigned to include:-</p> <ul style="list-style-type: none"> - the outcomes of the work reported to management since the previous meeting - the actual resources taken to deliver the reviews to the date of the progress report - the potential impact of the assurance opinions, either individually or collectively, on the Council's Annual Governance Statement.
<p>Management response:</p> <p>Agreed.</p> <p><i>Audit Committees have now considered reports setting out the way in which assurance planned and delivered will be mapped and reported: comments received about the reporting approach have been broadly positive. No difficulties anticipated in developing a clearer linkage to the development of the AGS.</i></p> <p><i>Reporting of summary outcomes in Annual Reports for 2012/13 should have identified any site-specific reporting requirements. No difficulties anticipated in using the same reporting format in performance reports starting in September committee cycle.</i></p> <p><i>Reporting on actual time spent on audits against plan can be accommodated within reporting of Performance Indicators – again starting in September committee cycle.</i></p>	

Opportunity	
e	<p>In discussion with Audit Committee representatives (current or recent chairs of the respective Committees), a number expressed an eagerness for training to be given on the role of the Audit Committee and how they should work with and challenge / hold to account Internal Audit. This presents an opportunity for Internal Audit to expand the training they have previously provided which will also help to raise the profile and increase understanding of internal auditing.</p>
<p>Management response:</p> <p><i>Reports setting out the challenges that the PSIAS will present to Audit Committees have been presented to all clients' Committees; programmes of training have been designed; first training session has been delivered @ MBC and positively received. Discussions in hand to make training sessions at any site open to any member of a Welland Audit Committee.</i></p>	

2.4. STAFF DEVELOPMENT

The current Manager Quality Assurance process applied to the work undertaken by the individual Auditors focuses on the testing undertaken the wording within the respective report. An important aspect of any internal Quality Assurance process is to identify any staff development opportunities.

Recommendation	
6	The Head of the Consortium should design a process that captures staff development opportunities identified as part of the Quality Assurance process. These should inform both the Consortium's Quality Assurance and Improvement Programme as well as the personal development plans of individual team members.
Management response: Agreed. <i>Review of assignments is currently undertaken using (and evidenced via) Galileo System. Investigations in hand to establish whether Galileo can analyse resolved review points by Auditor and/or Learning Point or whether there will be a requirement to introduce an alternative means of information capture.</i> <i>Arrangements will be in place – and codified in the Manual - by 31st December 2013.</i>	

3. SUMMARY OF CONFORMANCE WITH PSIAS

ATTRIBUTE STANDARDS

1000 Purpose, Authority, and Responsibility

1010 Recognition of the Definition of Internal Auditing

Generally Conforms	Partially Conforms	Does Not Conform
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GC	PC	DNC
----	----	-----

1100 Independence and Objectivity

1110 Organizational Independence

GC	PC	DNC
----	----	-----

1111 Direct Interaction with the Board

GC	PC	DNC
----	----	-----

1120 Individual Objectivity

GC	PC	DNC
----	----	-----

1130 Impairments to Independence or Objectivity

GC	PC	DNC
----	----	-----

1200 Proficiency and Due Professional Care

1210 Proficiency

GC	PC	DNC
----	----	-----

1220 Due Professional Care

GC	PC	DNC
----	----	-----

1230 Continuing Professional Development

GC	PC	DNC
----	----	-----

1300 Quality Assurance and Improvement Program

1310 Requirements of the Quality Assurance and Improvement Program

GC	PC	DNC
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1311 Internal Assessments

GC	PC	DNC
----	----	-----

1312 External Assessments

GC	PC	DNC
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1320 Reporting on the Quality Assurance and Improvement Program

GC	PC	DNC
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1321 Use of "Conforms with the International Standards for the Professional Practice of Internal Auditing"

Not applicable		
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1322 Disclosure of Nonconformance

GC	PC	DNC
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Note 1

PERFORMANCE STANDARDS

2000 Managing the Internal Audit Activity

2010 Planning

GC	PC	DNC
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2020 Communication and Approval

GC	PC	DNC
----	----	-----

2030 Resource Management

GC	PC	DNC
----	----	-----

2040 Policies and Procedures

GC	PC	DNC
----	----	-----

2050 Coordination

GC	PC	DNC
----	----	-----

2060 Reporting to Senior Management and the Board

GC	PC	DNC
----	----	-----

2070 External Service Provider and Organizational Responsibility for Internal Auditing

Not applicable		
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Note 1

2100 Nature of Work

2110 Governance

GC	PC	DNC
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2120 Risk Management

GC	PC	DNC
----	----	-----

2130 Control

GC	PC	DNC
----	----	-----

2200 Engagement Planning

2201 Planning Considerations

GC	PC	DNC
----	----	-----

2210 Engagement Objectives

GC	PC	DNC
----	----	-----

2220 Engagement Scope

GC	PC	DNC
----	----	-----

2230 Engagement Resource Allocation

GC	PC	DNC
----	----	-----

2240 Engagement Work Program

GC	PC	DNC
----	----	-----

Note 1

2300 Performing the Engagement

2310 Identifying Information

GC	PC	DNC
----	----	-----

2320 Analysis and Evaluation

GC	PC	DNC
----	----	-----

2330 Documenting Information

GC	PC	DNC
----	----	-----

2340 Engagement Supervision

GC	PC	DNC
----	----	-----

2400 Communicating Results

2410 Criteria for Communicating

GC	PC	DNC
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2420 Quality of Communications

GC	PC	DNC
----	----	-----

2421 Errors and Omissions

GC	PC	DNC
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2430 Use of "Conducted in conformance with the International Standards for the Professional Practice of Internal Auditing"

Not applicable		
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2431 Engagement Disclosure of Nonconformance

GC	PC	DNC
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2440 Disseminating Results

GC	PC	DNC
----	----	-----

2450 Overall Opinions

GC	PC	DNC
----	----	-----

2500 Monitoring Progress

GC	PC	DNC
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2600 Resolution of Senior Management's Acceptance of Risks

GC	PC	DNC
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Note 1

In 2012/13 the Consortium Head of Internal Audit has reported resourcing issues that lead to none comply with the previous CiPFA standards. Recruitment has now been made BUT a review of the resources needed will be required to implement the recommended change to the current approach for systems evaluation and the development of appropriate testing strategies.