



Coventry City Council

# Public report

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**Report to**

Audit and Procurement Committee

3<sup>rd</sup> August 2015

**Name of Cabinet Member:**

Cabinet Member for Strategic Finance & Resources – Councillor Damian Gannon

**Director approving submission of the report:**

Executive Director of Resources

**Ward(s) affected:**

City Wide

**Title:**

Review of the Effectiveness of the System of Internal Audit 2014-15

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**Is this a key decision?**

No

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**Executive summary:**

This report summarises the outcome of the various activities and assessments for the period 2014-15, to assist the Audit and Procurement Committee in undertaking the review of the effectiveness of the Council's System of Internal Audit, on behalf of the Council.

**Recommendations:**

Audit and Procurement Committee is recommended to:

1. Note the findings of the 2014-15 review.
2. Endorse the areas for development highlighted and agree to receive a further update in December to ensure progress is being made.

**List of Appendices included:**

Appendix One – CIPFA Suggested Terms of Reference

**Other useful background papers:**

None

**Has it or will it be considered by scrutiny?**

No other scrutiny consideration other than the Audit and Procurement Committee.

**Has it, or will it be considered by any other council committee, advisory panel or other body?**

No

**Will this report go to Council?**

No

**Report title:**

Review of the Effectiveness of the System of Internal Audit 2014-15

**1. Context (or background)**

1.1 The Accounts and Audit Regulations include a requirement for the Council to carry out an annual review of the effectiveness of its System of Internal Audit. Whilst not explicit in the guidance, the Audit and Procurement Committee is viewed as the appropriate Committee to undertake this review, given its role. In completing the review for 2014-15, the Council has again considered CIPFA guidance in determining the scope of the review, but have excluded the following:

- The area of Internal Audit will not consider:
  - The outcomes of specific audit reviews, performance indicators and the annual opinion of the Internal Audit and Risk Manager, as these have been considered in the annual Internal Audit Report that was presented to the Committee in June 2015.
  - An assessment of the role of the Council's Internal Audit and Risk Manager against the requirements stated in the CIPFA Statement on the Role of the Head of Internal Audit in Public Service Organisations (2010), as it has been determined that this should be considered on a cyclical basis given there has been no change in guidance / arrangements in the last year.
- The work of other assurance providers, as this has been considered separately in the preparation of the Annual Governance Statement that was presented to the Committee in June 2015.

1.2 The scope of the 2014-15 review has considered the following areas:

- The assessment of the Council's Internal Audit Service against the requirements of the Public Sector Internal Audit Standards.
- The results of the 2014-15 Internal Audit quality assurance review.
- An update on actions identified in last year's assessment of the Council's Audit Committee arrangement in comparison with good practice reflected in CIPFA guidance.

**2. Options considered and recommended proposal**

2.1 **Assessment of the Council's Internal Audit Service against the requirements of the Public Sector Internal Audit Standards (PSIAS)** - A professional, independent and objective internal audit service is one of the key elements of good governance, as recognised throughout the UK public sector. The PSIAS were introduced in 2013 and provided a single set of standards that underpinned Internal Audit in the public sector. The objectives of the PSIAS are to:

- Define the nature of internal auditing within the UK public sector.
- Set basic principles for carrying out internal audit in the UK public sector.
- Establish a framework for providing internal audit services, which add value to the organisation, leading to improved organisational processes and operations, and

- Establish the basis for the evaluation of internal audit performance and to drive improvement planning.

2.1.1 The PSIAS are significant in size and includes over 300 requirements. A summary of the results from our self-assessment is detailed in the table below:

Table One - Summary of Compliance against the PSIAS

Section	Standard	Compliant				Total
		Yes	Partial	No	N/A	
1	Definition of Internal Auditing	3				3
2	Code of Ethics	11	1			12
3	Attribute Standards					
3.1	Purpose, Authority and Responsibility	23				23
3.2	Independence and Objectivity	22	1		6	29
3.3	Proficiency and Due Professional Care	17	1		3	21
3.4	Quality Assurance and Improvement Programme	16	1		9	26
4	Performance Standards					
4.1	Managing the Internal Audit Activity	39	3		5	47
4.2	Nature of Work	24	2		3	29
4.3	Engagement Planning	39	2		12	53
4.4	Performing the Engagement	22				22
4.5	Communicating Results	48			5	53
4.6	Monitoring Progress	3			1	4
4.7	Communicating the Acceptance of Risks				2	2
<b>Total</b>		<b>267</b>	<b>11</b>		<b>46</b>	<b>324</b>

2.1.2 In considering the results, the following points need to be acknowledged:

- A large element of the assessment requires the assessor to make a judgement in determining compliance. In completing this assessment, the Internal Audit and Risk Manager has applied a pragmatic approach to determine compliance, as well as using his experience of the operations of the Service in reaching his judgements.
- Given that the Standard is based around a “one size fits all” approach to Internal Audit in the public sector, there are elements of the Standard which do not apply in Coventry. The majority of the 46 requirements classed as ‘N/A’ relate to the issue of consultancy services, which are not currently provided by the Internal Audit Service. Other factors include (a) requirements which have not arisen in practice and as such these are impractical to assess, and (b) where the timescale for implementation is some time away (i.e. external assessment must be carried out by March 2018) and this issue has yet to be considered. In respect of the external assessment, this will be considered in the coming months along the other developments highlighted in section 2.1.3.

2.1.3 In relation to those areas judged as partially compliant, these cover the following themes which are currently being progressed:

- 1) Continually improving the team’s proficiency, effectiveness and quality of services provided through on-going training and development.

- 2) To ensure a balance is achieved between rotating in the team around audit reviews and / or areas of responsibility whilst ensuring audits are allocated to the most appropriate auditor.
- 3) Formalising arrangements over obtaining stakeholder feedback.
- 4) To understand the range of assurance mechanisms available to the Council and to carry out an assurance mapping exercise around key Council activities as part of the development of the Internal Audit Plan.
- 5) To get a better understanding of the expectation within the standard around ethics related audits.

**2.2 Results of the Internal Audit Quality Assurance Review** - A key focus of the Performance Standards element of the PSIAS is around the delivery of audit assignments. Whilst procedures are in place to oversee such work as reflected in the self-assessment results for these areas, the PSIAS also requires Internal Audit Services to have a Quality Assurance and Improvement Programme designed to provide reasonable assurance that it:

- Performs its work in accordance with its Charter, which is consistent with the Public Sector Internal Audit Standards (PSIAS).
- Operates in an effective and efficient manner; and
- Is perceived by stakeholders as adding value and seeking to continually improve.

2.2.1 In addition to oversight provided on each audit, an annual assessment has been undertaken considering audits completed in 2014-15 along with performance data for the same period, in order to determine whether audit work is compliant with the requirements of the PSIAS. Overall, the review has found that such activity is compliant with the requirements of the PSIAS, although as part of our drive to continually improve, a number of developments have been identified. These are:

- The need for more regular dialogue with senior management to ensure changes in audit priorities are identified at an early stage so that resources can be re-allocated to other priorities without delay.
- To ensure that all reviews are completed on a timely basis and within agreed budget days. Developments include:
  - Ensuring that both budget allocations and report deadlines agreed for each assignment are underpinned by an assessment that such targets are achievable given the amount of work involved in completing the audit.
  - All work plans to support audit reviews are subject to approval at the planning stage to ensure that coverage focuses on the key risks in respect of the issue / area being audited.
- The audit report provides clearly evidenced opinions, with findings aligned to risks and recommendations that are both cost effective and solution focused. This development will be progressed through both individual and team development activity.

**2.3 Audit and Procurement Committee: The Effectiveness of the Council's Audit Committee** – CIPFA has developed a tool to assist Councils in assessing its Audit Committee arrangements against good practice. An assessment was made last year and highlighted three areas for development. Progress against these developments is detailed below:

2.3.1 To review the Audit and Procurement Committee's terms of reference in comparison with the updated CIPFA guidance - The current Audit and Procurement Committee's terms of reference was based around previous guidance issued by CIPFA. The revised CIPFA guidance includes a suggested terms of reference (Appendix One) for a local authority Audit Committee. The suggested terms of reference reflects a significant change in focus in the fact that that the number of core activities of the Committee has increased from 18 to 30.

This does not mean that there are significant gaps in the Councils current arrangements as the majority of new activity highlighted is either:

- Covered at least in part in reports already considered by the Committee.
- Reflective of the Committees current working practices.
- Are exception type issues and in the view of the Internal Audit and Risk Manager, would be considered if the issue arose.

There is, however, a need to formally update the terms of reference of the Audit and Procurement Committee to ensure it reflects current practices and in the process deciding whether the Council adopts all the suggestions made by CIPFA.

2.3.2 To undertake an assessment against the core knowledge and skills framework (CIPFA guidance) expected of an Audit Committee - All current members of the Audit and Procurement Committee have completed a self-assessment against the CIPFA framework. Whilst this has highlighted differing levels of knowledge / skills across members, overall, the assessment indicates the need to increase the knowledge of the Committee across the majority of the ten core areas that it considers. A number of delivery methods involving both internal and external training are available and a plan will be developed to progress this taking into account the views of the Committee.

2.3.2 To assess the effectiveness of the Audit and Procurement Committee - The CIPFA tool highlights a number of questions which consider the effectiveness of the Audit Committee arrangements in place. These are:

- An annual evaluation is undertaken to assess whether the committee is fulfilling its terms of reference and that adequate consideration has been given to all core areas.
- The committee obtain feedback on its performance from those interacting with the committee or relying on its work.
- The committee has evaluated whether and how it is adding value to the organisation.

This has not been progressed to date, primarily as a result of the fact that CIPFA evaluation tool is underpinned by its expectations around the terms of reference for the committee and the knowledge / skills its expects from members of the Committee. As these areas are still being progressed, the value gained from any assessment would be limited at this stage. The timing and mechanism (i.e. self-assessment, external assurance) for such a review will be considered once the other actions outlined have been implemented.

### **3. Results of consultation undertaken**

3.1 None

#### **4. Timetable for implementing this decision**

- 4.1 There is no implementation timetable associated with this report. An update report on action taken in progressing developments identified will be reported to the Audit and Procurement Committee in December 2015.

#### **5. Comments from the Executive Director Resources**

##### **5.1 Financial Implications**

There are no specific financial implications associated with this report. A key objective of the system of Internal Audit is to help improve value for money obtained, ensure the probity and propriety of financial administration, as well as assisting in the management of financial and operational risks.

##### **5.2 Legal implications**

There are no legal implications associated with this report.

#### **6. Other implications**

- 6.1 **How will this contribute to achievement of the council's key objectives / corporate priorities (corporate plan/scorecard) / organisational blueprint / LAA (or Coventry SCS)?**

The purpose of the system of Internal Audit is to provide independent assurance that the Council has an effective control environment that assists the Council in achieving the organisation's objectives. It objectively examines and evaluates the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources.

- 6.2 **How is risk being managed?**

The key risk is that failure to have effective arrangements may mean the Council does not have good corporate governance arrangements in place. This could result in an increased likelihood that the control environment would not aid the achievement of the Council's objectives.

- 6.3 **What is the impact on the organisation?**

None

- 6.4 **Equalities / EIA**

None

- 6.5 **Implications for (or impact on) the environment**

No impact

- 6.6 **Implications for partner organisations?**

None

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## **Appendix One - CIPFA Suggested Terms of Reference**

### **Statement of purpose**

1. Our audit committee is a key component of [name of authority]'s corporate governance. It provides an independent and high-level focus on the audit, assurance and reporting arrangements that underpin good governance and financial standards.
2. The purpose of our audit committee is to provide independent assurance to the members [or identify others charged with governance in your authority] of the adequacy of the risk management framework and the internal control environment. It provides independent review of [name of authority]'s governance, risk management and control frameworks and oversees the financial reporting and annual governance processes. It oversees internal audit and external audit, helping to ensure efficient and effective assurance arrangements are in place.

### **Governance and risk and control**

3. To review the council's corporate governance arrangements against the good governance framework and consider annual governance reports and assurances.
4. To review the Annual Governance Statement prior to approval and consider whether it properly reflects the risk environment and supporting assurances, taking into account internal audit's opinion on the overall adequacy and effectiveness of the council's framework of governance, risk management and control.
5. To consider the council's arrangements to secure value for money and review assurances and assessments of the risks and priorities of the council.
6. To consider the council's framework of assurance and ensure that it adequately addresses the risks and priorities of the council.
7. To monitor progress in addressing risk-related issues reported to the committee.
8. To consider reports on the effectiveness of internal controls and monitor the implementation of agreed actions.
9. To consider reports on the effectiveness of internal controls and monitor the implementation of agreed actions.
10. To review the assessment of fraud risks and potential harm to the council from fraud and corruption.
11. To monitor the counter-fraud strategy, actions and resources.

### **Internal audit**

12. To approve the internal audit charter.
13. To review proposals made in relation to the appointment of external providers of internal audit services and to make recommendations.
14. To approve the risk-based internal audit plan, including internal audit's resource requirements, the approach to using other sources of assurance and any work required to place reliance upon those other sources.

15. To approve significant interim changes to the risk-based internal audit plan and resource requirements.
16. To make appropriate enquiries of both management and the head of internal audit to determine if there are any inappropriate scope or resource limitations.
17. To consider reports from the head of internal audit on internal audit's performance during the year, including the performance of external providers of internal audit services. These will include:
  - Updates on the work of internal audit including key findings, issues of concern and action in hand as a result of internal audit work.
  - Regular reports on the results of the Quality Assurance and Improvement Programme.
  - Reports on instances where the internal audit function does not conform to the Public Sector Internal Audit Standards and Local Government Application Note, considering whether the non-conformance is significant enough that it must be included in the Annual Governance Statement.
18. To consider the head of internal audit's annual report:
  - The statement of the level of conformance with Public Sector Internal Audit Standards and Local Government Application Note and the results of the Quality Assurance and Improvement Programme that supports the statement – these will indicate the reliability of the conclusions of internal audit.
  - The opinion on the overall adequacy and effectiveness of the council's framework of governance, risk management and control together with the summary of the work supporting the opinion – these will assist the committee in reviewing the Annual Governance Statement.
19. To consider summaries of specific internal audit reports as requested.
20. To receive reports outlining the action taken where the head of internal audit has concluded that management has accepted a level of risk that may be unacceptable to the authority or there are concerns about progress with the implementation of agreed actions.
21. To contribute to the Quality Assurance and Improvement Programme and in particular, to the external quality assessment of the internal audit that takes place at least once every five years.
22. To consider a report on the effectiveness of internal audit to support the Annual Governance Statement, where required to do so by the Accounts and Audit Regulations.
23. To support the development of effective communication with the head of internal audit.

#### **External audit**

24. To consider the external auditor's annual letter, relevant reports, and the report to those in charge with governance.
25. To consider specific reports as agreed with the external auditor.
26. To comment on the scope and depth of external audit work and to ensure it gives value for money.
27. To commission work from internal and external audit.

28. To advise and recommend on the effectiveness of relationships between external and internal audit and other inspection agencies or relevant bodies.

### **Financial reporting**

29. To review the annual statement of accounts. Specifically, to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements or from the audit that need to be brought to the attention of the council.
30. To consider the external auditor's report to those charged with governance on issues arising from the audit of the accounts.

### **Accountability arrangements**

31. To report to those charged with governance on the committee's findings, conclusions and recommendations concerning the adequacy and effectiveness of their governance, risk management and internal control frameworks; financial reporting arrangements, and internal and external audit functions.
32. To report to full council on a regular basis on the committee's performance in relation to the term of reference and the effectiveness of the committee in meeting its purpose.