

Open Report on behalf of Pete Moore, Executive Director of Resources and Community Safety

Report to:	Audit Committee
Date:	11 July 2011
Subject:	Review of the Effectiveness of Internal Audit

Summary:

There exists a statutory requirement for bodies such as the County Council to review the effectiveness of internal audit once a year and for the findings of the review to be considered by an appropriate committee of the Council. This paper discharges that responsibility by reporting the findings of work undertaken by a joint officer / councillor working group. Whilst identifying a few areas for ongoing monitoring and improvement, the group concluded that the Council does have an effective system of internal audit.

Recommendation(s):

The Committee endorse the opinion of the Review Group that the County Council maintains an effective system of internal audit

Background

- 1.1 Regulation 6(3) of the Accounts and Audit (England) Regulations 2011 requires this Council to review the effectiveness of internal audit once a year and for the findings of the review to be considered by a Committee of the Council. The Audit Committee is the most appropriate one in the case of this Council. It is sensible to consider this aspect in advance of finalisation of the Annual Governance Statement of the Council as the effectiveness of the system of internal audit is a key aspect of the governance framework. The Annual Governance Statement will be considered in draft at this meeting of this Committee and will be finalised by September in time to be incorporated into the audited financial statements of the Council.
- 1.2 In this context 'internal audit' is not just restricted to the role, activity and effectiveness of the internal audit team; it also applies to the role, activity and effectiveness of this Committee itself. Aspects of risk management and health and safety are also relevant to this review. Guidance makes it clear that is not the role of the external auditor to undertake this work. It is for the authority itself to complete a review.

2. The Review Group

- 2.1 Guidance from CIPFA on this issue suggests that this review is best undertaken by a group of officers and / or members. In terms of the officer input this should not directly involve the Head of the Internal Audit service or any audit team member. The Head of Internal Audit can, however, provide material to be considered by the Review Group.
- 2.2 The following Review Group has been established to undertake this role:

Councillor Mr B Young– Chairman of the Audit Committee
Councillor Mrs C M H Farquharson – Vice Chairman of the Audit Committee
David O'Connor – Executive Director – Performance & Governance
David C Forbes – Assistant Director – Finance and Resources

3. The Review Activity

- 3.1 CIPFA have developed and issued a Code of Practice for the provision of internal audit services in the public sector. In tandem with the development of that Code, CIPFA have also published a self assessment questionnaire to assess compliance with the Code and thereby the effectiveness of the internal audit service aspect of the internal audit system. In addition CIPFA have relatively recently published a good practice note on the role of the Head of Internal Audit. The Review Group have reviewed compliance of the Lincolnshire Head of Internal Audit with that document as part of the latest review. The outcome is reported later in this report.
- 3.2 At its meeting in June 2007 the Review Group critically appraised the self assessment questionnaire completed by the Head of Internal Audit. This enabled both an overall conclusion to be drawn on the effectiveness of the service and to endorse recommendations for improvement. The Head of Internal Audit repeated a self assessment of the internal audit function during 2009/10.
- 3.3 The Audit Committee completed a self assessment of its own performance in November 2007 and reported to the Audit Committee in December 2007. Action points arising were subsequently actioned to the satisfaction of the Committee.

4. Review Findings

- 4.1 The Review Group reconsidered the findings from previous self assessments of the internal audit service as prepared by the Head of Internal Audit. The Review Group concluded this remained a fair and reasonable assessment of the internal audit service provided to the County Council.

4.2 Last year no areas of activity were identified of non-compliance with the CIPFA Code of Practice. However, the Head of Corporate Audit brought a number of issues to the attention of the Review Group. These issues together with the action taken over the year are described below.

- To undertake a self assessment of the effectiveness of the Audit Committee in light of the impact of the Autumn 2010 Spending Review upon the business of the County Council factoring into that review the refresh of the Corporate Risk Register that is planned following the Spending Review.

Action Taken:

A workshop with the Committee was held on 13th June 2011 to review effectiveness and to help shape its future work plan. The update of the corporate risk register has not yet been undertaken and is planned for October/November 2011. The outcomes of both pieces of work will help to assess how well the Committee is working and whether it's discharging its 'watchdog' role and terms of reference.

- In light of previous positive experiences, to schedule a private meeting with the external auditor to enable a full and frank exchange of views of the system of internal audit to take place.

Action Taken:

This was completed in December 2010.

- The Review Group (or Audit Committee) to assess compliance with the recently issued Cipfa good practice note on the role of the Head of Internal Audit.

Action Taken:

The Cipfa good practice guide was issued in November 2010. It covers both the role played by the Head of Internal Audit in helping steer the Council to maintain good governance arrangements and the attributes required by the individual occupying that role.

There is an expectation from Cipfa of a 'comply or explain' approach when assessing local practice. The Review Group undertook an assessment of the role and personal attributes of the Head of Internal Audit (HIA) in Lincolnshire and concluded that full compliance was achieved for the majority of the best practice points covered in the Cipfa guide.

In eight cases the Review Group felt that full compliance was not presently achieved and the detail in respect of each of these issues is given below in compliance with the guides' 'explain' principle. Six

cases relate to the governance compliance theme and two to core HIA responsibilities.

Governance Requirements

Ensure that the HIA is consulted on all proposed major projects, programmes and policy matters.

This is not automatically provided for within the key governance documents, practices, etc of the Council. However, the reality is that the HIA is aware of all major projects through a variety of means (eg. Directorate liaison meetings, participation in the Governance Group and liaison with the Programme Centre).

Where the HIA does have operational responsibilities the HIA's line manager and the Audit Committee should specifically approve the internal audit strategy for these and associated plans and reports and ensure the work is independently managed.

The Lincolnshire HIA does have non-audit operational responsibilities but these are for services that have a direct synergy with internal audit (eg. risk management, health & safety, business continuity). Historically, when such service areas have been reviewed independent resources have been employed. It is accepted that this aspect could be strengthened by having such work commissioned by, and reported directly to, the Asst Director – Finance & Resources. This will be implemented.

Establish clear lines of responsibility for those with an interest in governance (eg. Chief Executive, Chief Legal Officer, Chief Financial Officer, Audit Committee, non-executive director/elected representatives). This covers responsibilities for drawing up and reviewing key corporate strategies, statements and policies.

Whilst the HIA does not report directly to a Director or the Chief Executive (see specific point on this below), the reality in the Authority is that the HIA has unencumbered access to all senior officers (and elected members) within the authority. Good governance is clearly part of the standard remit of such officers and this is enhanced by the operation of a cross Directorate Governance Group.

Include awareness of governance in the competencies required by members of the Leadership Team.

Technically the competency framework of the County Council does not apply to the Management Board. However, governance forms a key aspect of all senior manager job descriptions and is tested as part of the recruitment process. Executive Directors and the Chief Executive are periodically questioned by the Audit Committee on this and related topics.

Ensure that the internal audit strategy is approved by the Audit Committee and endorsed by the Leadership Team.

Whilst the strategy is presently approved by the Committee it is not presented to the Management Board. This will be corrected for the future.

Ensure that where the HIA is an employee the HIA is line managed by a member of the Management Team.

The HIA does not report to a member of the Management Team but to an Asst Director. The experience to date has been that unfettered direct access to senior managers/elected members has always been available to the HIA. Structure has not been a barrier to effectiveness.

Core HIA Responsibilities

Consulting stakeholders, including senior managers and non-executive directors/elected representatives on internal audit strategy.

This has been achieved via regular Directorate liaison meetings and through consultation with the Governance Group.

Setting out how the HIA plans to rely on others for assurance on the organisation's controls and risks and taking account of any limitations in assurance given by others.

This is a key area for development and is mentioned in the next section of this report as a key mitigation factor consequent to the reduction in available internal audit resources for 2011/12 onwards. Whilst further developments are required, a recent example of this in action relates to improved liaison work with the Programme Centre. The Committee will wish to monitor progress on this aspect.

The Review Group felt adequate progress had been made in delivering the above points and that they had contributed positively towards improving the overall system of internal audit. With specific reference to the review of compliance with the Cipfa good practice guide on the role of the HIA the Review Group felt, that subject to the specific proposals mentioned above, the present situation was satisfactory.

- 4.3 In terms of the effectiveness of the internal audit service itself, the following developments over the year were noted.

As part of the Core Offer workforce change the service has had to balance 'effective assurance' arrangements with what the Council can afford – the service was required to make a 25% budget reduction.

The main impact of this has been to scale down the core internal audit function with the key elements including:

- Lincolnshire Internal Audit Plan is reduced by 17% with focus to be on strategic risks and critical systems. The service will need to leverage other assurance functions of the Council to provide assurance where direct audit work is not undertaken. The current assurance mapping exercise will help identify the councils current assurance arrangements, together with how much can be placed reliance on them and any duplication / gaps in assurance.
- The service is reviewing its risk and internal audit strategy and the tools used to obtain assurance. Management views will be obtained to help shape this and ensure the service focuses on what matters (ie strategic risks and critical systems).
- The service has reviewed roles and remit within the teams, involving the integration of operational risk management support in the audit team, the focus of the risk team on strategic and critical risks and the alignment of 'due diligence' audit work with proactive counter fraud work.
- The service will continue to deliver external work generating income of £241,500. This helps fund at least 2 posts for delivery of Lincolnshire plan.
- Counter Fraud plan increased by 12%.
- Strategic risk management capacity unchanged.
- The corporate health & safety capacity remains unchanged although the service will be seeking a cost reduction in the operational health and safety service delivered by Mouchel. The current cost of this service is £446,841. A value for money study will be undertaken in 2011/12.
- Business Continuity Capacity reduced by 25%.
- Insurance function capacity unchanged (although carrying a vacancy at present).
- The total budget reduction is £368,000.

All of the above means significant change to people, processes and how the service delivers assurance to the Council. To help implement this change a project plan is in place – where key milestones are being monitored.

Other developments include that the HIA will be providing Head of Audit Support for East Lindsey District Council. It is proposed that two staff from

East Lindsey are seconded to the County with the service having management oversight of the delivery of the East Lindsey internal audit plan. This supports the 'Audit Lincolnshire' partnership where the County works with the City of Lincoln to deliver 7 of the 8 local authority internal audit services in Lincolnshire.

The Review Group again felt that adequate progress had been made during the year.

4.4 The Review Group considered a number of actions that could be undertaken over the year ahead to enhance the system of internal audit. The Group felt that the following would be appropriate actions for the year ahead in light of their current assessment.

- The changes in practice proposed as a result of the review of the CIPFA good practice guide on the role of the HIA be implemented forthwith.
- The continued delivery of an effective internal audit service should be carefully monitored during the year to ensure that the 25% reduction in budget does not materially impact upon service quality or effectiveness.

Conclusion

The Review Group are of the opinion that the County Council has an effective system of internal audit.

Consultation

a) Policy Proofing Actions Required

n/a

Background Papers

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

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