MAZARS

Sunderland City Council

Review of Internal Audit

June 2013

Contents

M A Z A R S

1 Introduction

The Accounts and Audit Regulations 2011 state that 'a relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control.' These practices are defined in CIPFA's Code of Practice for Internal Audit in Local Government in the UK (the Code).

As part of the Council's governance arrangements, it reports annually on the work of Internal Audit to comply with the requirements of Regulation 6 of the Accounts and Audit Regulations 2011. This regulation requires an annual assessment of the effectiveness of Internal Audit.

This review is intended to contribute towards the assessment of the Internal Audit Service (IAS).

2 Our approach

Our review focused on arrangements for 2012/13 in two areas:

- A review of the IAS' Quality System against the professional and statutory requirements contained within the Code.
- A sample review of five IAS files that covered work in areas spread across the Council's functions.

Professional standards for Internal Audit are contained in the Code and cover the following key areas:

- Scope of Internal Audit
- Independence and ethics
- The role of the Audit Committee
- Relationships
- Staffing, training and continuous professional development (CPD)
- Audit strategy and planning
- Undertaking audit work
- Due professional care
- Reporting
- Performance, quality and effectiveness

The five files selected for review were:

- Payroll
- Benefits administration
- Corporate Attendance Management
- Corporate Legality
- St Benet's primary school

We have not reviewed IAS against the requirements of the new United Kingdom Public Sector Internal Audit Standards which came into force from 1 April 2013.

3 Main conclusions

Our review concludes that the Council's Internal Audit Service complies with the CIPFA 'Code of Practice for Internal Audit in Local Government in the UK'. Our review confirmed that IAS continues to meet its professional and statutory duties. Processes in place are driven by a Quality System. Our detailed review of files did not highlight any significant non-compliance with the Quality System or the Code. Some minor issues were discussed with officers.

IAS has been through major changes that have reduced the size and function of Internal Audit at Sunderland City Council, with Internal Audit now being viewed as part of the Council's overall Integrated Assurance Framework (IAF).

The changes that have been made are now becoming embedded, though key documents are in need of updating to reflect the new structure and processes in place. These include, but are not restricted to, the Quality Manual, the Quality Procedures Manual, the Audit Charter and the Audit Strategy. Officers are aware of this, and are currently in the process of updating the documents.

4   Detailed findings

Detailed below are our key findings against each area of the Code.

Scope of Internal Audit

Background

The CIPFA standard on the scope of Internal Audit addresses:

- Internal Audit's terms of reference;
- Its scope of work;
- Other work undertaken; and
- Its role in anti fraud and corruption work.

Findings

IAS' formally approved terms of reference and scope are clearly set out in both the Internal Audit Charter and the Council's Financial Procedure Rules and are appropriate for a council internal audit function. Whilst the principles in the Audit Charter remain valid and appropriate, it requires updating to reflect the new structure and responsibilities of IAS.

IAS' scope includes services provided in partnership and, where appropriate, access rights are written into partnership agreements.

The Audit Charter includes a requirement that the Head of Corporate Assurance and Procurement (HoCAP) is to be notified of all suspected or detected fraud, corruption or financial impropriety.

No areas of non-compliance with the CIPFA standard were identified.

The new Integrated Assurance Framework (IAF) and Corporate Assurance Map (CAM) have been in place for 2012/13 and have led to changes in the approach of IAS.

These changes have resulted in separate teams for Risk and Assurance and Internal Audit. The smaller internal audit team focuses on planned audit work and continues to meet CIPFA Code requirements. The Risk and Assurance team are able to provide advice on the design and implementation of new systems. This two-step approach ensures that Internal Audit is free from operational duties and has reduced threats to their independence through self-review.

Independence

Background

The CIPFA standard on independence considers:

- Internal Audit's principles regarding independence;
- its organisational independence;
- the status of the Head of Internal Audit;

- the independence of individual auditors and contractors; and
- declarations of interests.

Findings

The Audit Charter and Financial Procedure Rules set the standards for IAS' independence.

As noted above, the new IAF arrangements have improved the independence position of Internal Audit and reduced the threat of self-review.

Arrangements in place to provide assurance that independence is maintained include:

- the Audit Charter specifies that IAS will not have any executive responsibilities; and
- the HoCAP reports directly to the Executive Director of Commercial and Corporate Services and has the freedom to report to Members and officers.

Internal Auditors are required to sign an annual certificate of independence or declare any issues that may lead to a conflict of interest. For the financial year 2012/13 declarations were not on file for the HoCAP and the Audit Manager. Declarations were, however, available for the current financial year. Arrangements are in place to mitigate potential conflicts of interest.

Ethics for the Internal Auditor

Background

This CIPFA standard covers ethical standards for Internal Auditors in relation to:

- integrity;
- objectivity;
- competence; and
- confidentiality.

Findings

The Quality System clearly sets out auditor responsibilities in relation to integrity, objectivity, confidentiality and competence. For example, requirements for staff rotation are set out:

- an assignment should not be undertaken by the same individual more than twice; and
- audit work will not be undertaken within two years where the auditor has had previous operational responsibilities.

There are occasions where an auditor does, in practice, undertake an audit twice in succession, but this only where it can't be avoided due to the specialist nature of the work involved and the expertise of team members, or there is a length of time between the two visits. Due to the smaller size of the IAS team, this is likely to occur more often in the future but review procedures are in place to mitigate any perceived threats to independence.

Each report has a 'Strictly Private and Confidential' footer, which highlights that contents are not for reproduction, publication or disclosure to unauthorised persons without prior agreement.

Staff are regularly reminded of their obligations. Team meetings are held every six weeks where messages about quality, ethical behaviour and independence are reinforced if necessary.

The Council's Code of Conduct for Officers applies equally to IAS staff and this covers ethical conduct.

Similarly, the Council's annual appraisal process is used to identify any training needs, and staff are appropriately qualified to carry out their roles.

No areas of non-compliance with the CIPFA standard were identified.

Audit Committees

Background

This CIPFA standard covers:

- the purpose of an Audit Committee; and
- Internal Audit's relationship with the Audit Committee.

Findings

The Council has an independent Audit and Governance Committee (AGC), comprised of five elected members and two co-opted members, one of whom is the Chair.

The HoCAP submits the annual operational plan to the AGC and also, if there are any changes to it, the IAS strategy. Regular progress reports and an annual report are also presented. These plans are now part of the IAF and CAM updates.

The HoCAP has access to the Committee and Chair which provides assurance on the independence of Internal Audit. The AGC's terms of reference also stipulate that the AGC may meet privately with the HoCAP.

Our attendance at AGC meetings provide assurance that processes are robust and officers are regularly challenged.

No areas of non-compliance with the CIPFA standard were identified.

Relationships

Background

This CIPFA standard covers:

- the principles of good relationships (internal and external); and
- Internal Audit's relationship with:
    - management;
    - other internal auditors;
    - external auditors;
    - other regulators and inspectors; and

- elected members.

Findings

The HoCAP seeks to develop good working relationships with all relevant parties.

IAS continues to score highly in client post-audit questionnaires, with an average in 2012/13 to date of 1 (1 = good, 4 = poor).

The Head of Performance Improvement liaises with inspectorates, and the HoCAP is aware of inspectors' views through discussions with them as part of the Corporate Assurance Group, and through his role in the annual governance review.

The external auditor meets regularly with the HoCAP and Audit, Risk and Assurance Manager (ARAM) and has an effective working relationship with IAS.

No areas of non-compliance with the CIPFA standard were identified.

Staffing, training and CPD

Background

This CIPFA standard covers:

- Internal Audit's staffing levels; and
- training and the continuous professional development of Internal Auditors.

Findings

IAS auditors are subject to an annual Council appraisal where performance is formally assessed.

All Internal Auditors have professional qualifications and as such are required to comply with their institute's requirements for continuing professional development.

Personal development plans are in place for auditors, which are regularly monitored.

The HoCAP confirms that IAS is sufficiently resourced within the annual Internal Audit plan, which provides assurance that its scope and adherence to the Code will not be compromised.

The reduced level of staffing in IAS may mean that IAS does not have the capacity to deal with increased workloads due to any ad hoc investigations that arise. A smaller team is always more vulnerable to the effects of long-term sickness or sudden loss of experienced members of staff. Staffing levels were considered as part of the restructure of IAS, and are also considered as part of the five-year plan.

If any additional resources are required, a partnership has been entered into with PWC that means that the Council can access suitably qualified staff to assist with workload, and also provide expertise in specific areas. Whilst this is at an additional cost to the Council, this arrangement provides comfort that the function of IAS will not be impaired.

No areas of non-compliance with the CIPFA standard were identified.

Audit strategy and planning

Background

This CIPFA standard covers:

- Internal Audit's audit strategy; and
- its risk based audit plan.

Findings

The annual risk-based plan is approved by the AGC. The Audit Strategy is now part of the IAF. The documents are in line with the Code and include an explanation of:

- how the HoCAP will form and evidence his annual opinion on the control environment;
- how IAS has identified and will address significant local and national issues and risks;
- how IAS will be provided; and
- the resources and skills required to deliver the planned work.

The HoCAP and Executive Director of Commercial and Corporate Services both review and challenge the proposed audit plan before it is finalised and presented to members for approval.

No areas of non-compliance with the CIPFA standard were identified.

Undertaking audit work

Background

This CIPFA standard covers:

- Internal Audit's planning;
- the approach to undertaking audit work; and
- the recording of audit assignments.

Findings

We found that work was well planned, with clear audit briefs issued at the start of each audit. Standard documentation and the need for a thorough review are Quality System requirements that are followed in practice. Risks, controls, testing and evaluation of results are all clearly recorded within the MKI e-audit system.

The sample of audit files tested provided sufficient information to enable an understanding of the work carried out and why conclusions were reached. Findings and conclusions were adequately supported with appropriate evidence.

Some minor points for improvement were identified. These have been shared with the ARAM and the HoCAP.

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Due professional care

Background

This CIPFA standard covers:

- the responsibilities of the individual Internal Auditor; and
- the responsibilities of the Head of Internal Audit.

Findings

IAS has appropriate procedures in place to ensure due professional care. The Quality Procedures Manual contains guidance on professional standards and ethics. The review process also provides assurance that due professional care is applied throughout internal audit work.

The Council's Whistleblowing Policy sets out arrangements for the disclosure of improper conduct.

No areas of non-compliance with the CIPFA standard were identified.

Reporting

Background

This CIPFA standard covers:

- the principles of reporting;
- reporting on audit work;
- follow-up audits and reporting; and
- annual reporting and presentation of the audit opinion.

Findings

The Quality System contains comprehensive guidance on report writing. The MKI e-audit system is used to automatically feed recommendations into reports set out in the correct format. Our detailed testing highlighted that clear reports are issued in good time following the conclusion of audits. Examples of good practice include:

- clearly stating the scope of the audit;
- giving an opinion on the control environment; and
- categorisation of audit recommendations (high, medium, low and observation).

Documented escalation procedures are applied for late responses to reports.

The annual report to the Audit and Governance Committee follows Code requirements, in that it includes:

- an opinion on the control environment;
- a summary of work undertaken, from which the opinion was drawn;

- a comparison of work undertaken to that planned;
- a summary of IAS performance against targets and measures;
- commentary on compliance with the Code; and
- results of quality assurance assessments.

No areas of non-compliance with the CIPFA standard were identified.

Performance, quality and effectiveness

Background

This CIPFA standard covers:

- the principles of performance, quality and effectiveness;
- the quality assurance of audit work; and
- the performance and effectiveness of the Internal Audit service.

Findings

There is a Quality System in place within IAS, consisting of a Quality Manual and Quality Procedures Manual. This is based on procedures that were in place prior to the restructure of IAS and requires updating. At a time when there are significant changes and pressures on local government, good and up-to-date written procedures can help mitigate against loss of expertise and capacity and ensure continuation and consistency of approach.

Each audit is staffed by an appropriate skills mix and the level of supervision takes account of the experience of the auditor.

Monitoring of the audit plan is carried out throughout the year within IAS and with regular reporting to both the Executive Director of Commercial and Corporate Services and the AGC.

IAS has developed a suite of performance indicators, which are reported to each meeting of the AGC. The most recent data show that IAS is meeting its targets.

Performance is also compared against other authorities within the CIPFA benchmarking club. Review of the latest benchmarking report highlights no areas of concern that indicate that IAS may be out of line with other Internal Audit services in local authorities.

No areas of non-compliance with the CIPFA standard were identified.