# Sunderland City Council

## Public Sector Internal Audit Standards Compliance Review

June 2014

MAZARS

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# 01 Introduction

An effective, objective and independent internal audit service (IAS) is the cornerstone of good governance in all public sector bodies.  Internal audit plays a pivotal role in providing assurance to officers and members that the system of internal control within their organisation is operating effectively and to recommend how that system of internal control can be strengthened.  This is a fundamental requirement enshrined in the Accounts and Audit (England) Regulations 2011.

## Public Sector Internal Audit Standards

From 1 April 2013, a new set of internal audit standards for the public sector, the 'Public Sector Internal Audit Standards' (PSIAS) have been in effect. These standards replaced the 'Code of Practice for Internal Audit in Local Government in the United Kingdom' which was last revised in 2006.  The PSIAS adopt the principle requirements of the Institute of Internal Auditors Professional Practices Framework and adapt these to ensure they are relevant and appropriate for the UK public sector.

They are mandatory for all authorities who are required to comply with the 2011 regulations.

The overall objective of the PSIAS is to provide a high level overarching framework applicable to all of the public sector.  In summary, they:

- 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.[1]

## Local Government Application Note and 'proper practices'

The Chartered Institute of Public Finance and Accountancy (CIPFA) recognised the potential significance of the changes resulting from the adoption of the PSIAS and has provided guidance to internal auditors in the form of an Application Note. The Application Note and PSIAS combined constitute 'proper practices' in internal control as set out in the Accounts and Audit Regulations.

## External assessment

The PSIAS and Application Note require that every local government IAS is subject to an external assessment of its work against the requirements of the standards, regardless of whether the IAS is provided by an in-house or external team.  This external assessment is required to be carried out at least once every five years, and this report sets out our assessment of the IAS provided to Sunderland City Council.

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[1] Public Sector Internal Audit Standards

# 02 Our Approach

## Methodology

Our assessment has been wide-ranging and we have considered evidence to inform our conclusions and recommendations from a number of sources. The main phases of our methodology are set out below.

**Review of self-assessment**

The CIPFA Application Note provides a framework within which every IAS is expected to carry out a self-assessment against the requirements of the PSIAS. The Council's IAS carried out this self-assessment and we critically evaluated the findings, sought evidence to support the results and reached our own judgement as to whether the self-assessment was accurate.

**File reviews**

To inform our review of the self-assessment we carried out a detailed review of a sample of internal audit files. Each file reviewed was considered against the requirements of the PSIAS and the CIPFA Application Note.

The five files selected for review were:

- Accounts Payable
- Council Tax
- Revenue Procurement
- Sunderland Aquatic Centre
- Sunderland Live Contract Management

In addition to the activities above we also considered our detailed knowledge of the IAS gathered from our experience as the Council's external auditor for a number of years. This, together with the work outlined above, place us in an unrivalled position to provide an informed external assessment of the Council's IAS against the requirements of the PSIAS. It also enables us to provide recommendations on where the service can potentially be improved.

# 03 Our assessment

## Overall conclusion

We conclude that the IAS is **compliant** with the requirements of the Public Sector Internal Audit Standards and the CIPFA Application Note.

Some minor improvement points were identified during our detailed file reviews and these have been discussed with the Head of Assurance, Procurement and Projects (HoAPP) and the Audit, Risk and Assurance Manager (ARAM).

## Identified Good Practice

Our review noted areas where the IAS is demonstrating good practice in the way it carries out its functions.

### Assurance Framework

The use of the Integrated Assurance Framework and placing IAS as 'the last line of defence' has allowed audit work to focus on key risk areas for the Council which gives targeted assurance, making the most of the resources available to the IAS. This process is becoming increasingly embedded in the Council's approach to assurance.

### Officer feedback

Questionnaires are sent to all service managers after the completion of the audit, in order to give service managers the opportunity to provide feedback. The Audit Manager reviews and reports the findings of all questionnaires and uses the information obtained to help ensure further improvements in the service provided.

### Audit manual and audit programmes

A detailed audit manual sets the framework within which all internal audit assignments delivered by the IAS are to be provided. This audit manual is compliant with the PSIAS and, when followed, should ensure that all individual audit assignments meet the requirements of the PSIAS.

The IAS also has standardised audit programmes in place where appropriate which are designed to ensure work is completed in line with PSIAS requirements.

# 04 Detailed findings

## Review of compliance with the PSIAS and CIPFA Application Note

Our detailed findings in respect of compliance with the PSIAS and the CIPFA Application Note are provided below. These are based on our review of both the IAS self-assessment and a sample of internal audit files. Professional standards for Internal Audit are contained in the PSIAS and cover the following key areas:

- Purpose, Authority and Responsibility
- Independence and Objectivity
- Proficiency and Due Professional Care
- Quality Assurance and Improvement Programme
- Managing the Internal Audit Activity
- Nature of Work
- Engagement Planning
- Performing the Engagement
- Communicating Results
- Monitoring Progress

**Purpose, Authority and Responsibility**

The formally approved Audit Charter sets out the purpose, authority and responsibility of IAS. The charter was updated in 2013/14 to reflect the changes in the IAS following the establishment of the Assurance Framework and Risk and Assurance Team.

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 HoAPP is to be notified of all suspected or detected fraud, corruption or financial impropriety.

Two areas were identified where additional information should be incorporated into the Audit Charter:

Definition of 'the Board' and 'management'

For the purposes of the IAS, it is the Audit and Governance Committee (Those Charged With Governance) who are defined as 'the Board', and the Executive Director of Commercial and Corporate Services and Chief Officers who are 'management'. This is not explicitly stated within the Audit Charter as recommended in the PSIAS (public sector requirement 1000). Although we agree that reporting lines are clearly laid out, we suggest that the wording of the Charter is expanded when it is next reviewed.

We note that a change may also be needed to the Charter in respect of the roles of the Executive Director of Commercial and Corporate Services and Head of Financial Resources, where precise roles will change in the future.

Assurances to external parties

The PSIAS (1000.A1) sets out that if assurances are to be provided to parties outside the Council, the nature of these assurances must also be defined in the internal audit charter. We agree that proper arrangements are in place for external assurances, but given the increasing number of such assurances, for example, as alternative models of service delivery are introduced and audited by the Council's IAS, it would be helpful to update the Charter to be explicit about these when it is next reviewed.

**Independence and Objectivity**

The Audit Charter sets the standard for IAS' independence.

The Audit Manual clearly sets out the reporting lines of IAS and confirm the independence of the HoAPP.

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

- the Audit Charter specifies that IAS will not have any  responsibilities for operations other than providing recommendations and advice to management on risks and controls; and
- the HoAPP reports directly to the Executive Director of Commercial and Corporate Services and has the freedom to report to Members and officers.

The Audit Manual clearly sets out auditor responsibilities in relation to independence and objectivity. For example, requirements for staff rotation are set out:

- an assignment should not be undertaken by the same individual more than twice in succession; 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 is 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.

**Proficiency and Due Professional Care**

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. Staff Performance Statements are completed for each piece of work to aid development of staff and drive improvement in the section.

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

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. A separate budget exists to fund such work, and this arrangement provides comfort that the function of IAS will not be impaired.

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

No areas of non-compliance with the PSIAS were identified.

## Quality Assurance and Improvement Programme

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.

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 Audit and Governance Committee (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.

IAS continues to score highly in client post-audit questionnaires, with an average in 2013/14 to date of 1 (1 = good, 4 = poor).

External validation of IAS's self-assessment is sought to meet the requirement of the PSIAS.

No areas of non-compliance with the PSIAS were identified.

## Managing the Internal Audit Activity

The work of IAS is part of the Integrated Assurance Framework, and drives the annual internal audit opinion.

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

The HoAPP 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. This feeds into the Corporate Assurance Map which helps set Internal Audit's work programme.

The external auditor meets regularly with the HoAPP and ARAM, and has an effective working relationship with IAS.

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.

No areas of non-compliance with the PSIAS were identified.

## Nature of Work

The IAS annual work programme is based on the risk assessment of the whole Council, and is produced in consultation with Heads of Services. The use of the IAF and Corporate Assurance Map means that the work of IAS can be clearly linked to the assurance needs of the Council.

A Fraud Risk Assessment is used to determine the level of risk in each area of the Council. Risk scoring is used to determine the potential impact on the Council and helps focus the work of IAS.

No areas on non-compliance with the PSIAS were identified.

## Engagement Planning

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 PSIAS and include an explanation of:

- how the HoAPP 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.

Directors and Heads of Service are consulted on the areas to be covered as part of the annual audit planning process to ensure that management concerns can be built into the Audit Plan as appropriate.

The HoAPP 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 PSIAS were identified.

## Performing the Engagement

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 Audit Manual 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 HoAPP.  These areas did not prevent us from assessing this area as complying with the PSIAS.

## Communicating Results

The Audit Manual contains 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, significant, medium, low and observation).

Documented escalation procedures are applied for late responses to reports.

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

- an opinion on the effectiveness of the Council's framework of governance, risk management and control
- a summary of work undertaken, from which the opinion was drawn;
- a statement on conformance with the PSIAS; and
- the results of the quality assurance and improvement programme.

No areas of non-compliance with the PSIAS were identified.

**Monitoring Progress**

There is a formal follow-up procedure where audit recommendations are made.

The acceptance of risk without compensating controls by management would be fed into the Corporate Assurance Map to reflect the impact of the risk of the Council.

There is a high implementation rate of IAS recommendations, and this is reported to AGC as part of the performance monitoring of IAS.

No areas of non-compliance with the PSIAS were identified.