

## **Review of the Effectiveness of Internal Audit 2011/12**

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### **Summary**

- 1 This report advises Members of the process and the outcomes of the 2011/12 review of the effectiveness of the council's internal audit arrangements.

### **Background**

- 2 The Accounts and Audit Regulations 2011 require the council to conduct, at least once a year, a review of the effectiveness of its internal audit arrangements, and to report the findings of this review to an appropriate committee. The process is intended to form part of the wider review of the effectiveness of the system of internal control which is necessary to prepare the Annual Governance Statement (which is a separate item on this Agenda).
- 3 The Regulations require that the council must undertake an adequate and effective internal audit of its accounting records and of its system of internal control. Previous guidance has stated that the proper practices for internal audit are those contained within the CIPFA Code of Practice for Internal Audit in Local Government 2006 (the Code of Practice).

### **Defining Internal Audit**

- 4 In the Code of Practice, internal audit is defined as:

*“an assurance function that provides an independent and objective opinion to the organisation on the control environment, by evaluating its effectiveness in achieving the*

*organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources."*

As such internal audit forms an essential part of the council's corporate governance arrangements.

- 5 Since April 2009, internal audit has been provided under contract by Veritau Ltd, a company wholly owned by the council and North Yorkshire County Council, with the service being provided under a formal "shared service" arrangement. This review takes full account of this framework for the provision of the service.
- 6 The principal functions of internal audit are to:
  - (a) provide assurance to Members, chief officers, other key stakeholders and the wider community on the effectiveness of the governance arrangements and internal controls at the council;
  - (b) provide advice and make recommendations to improve controls and/or address the poor or inappropriate use of the council's resources;
  - (c) examine and evaluate the probity, legality and value for money of the council's activities;
  - (d) act as a visible deterrent against all fraudulent activity, corruption and other wrong doing;
  - (e) respond to and investigate any instances of suspected fraud or corruption
  - (f) provide assistance to the Audit and Governance Committee in the performance of its functions as set out in its terms of reference.
- 7 The Code of Practice sets out eleven standards (or principles) for the establishment of a professional service. Each principle is supported by detailed guidance. The principles cover the following areas:
  - (a) scope of internal audit (terms of reference and scope of work);
  - (b) independence;

- (c) ethics for internal auditors;
  - (d) audit committees (including internal audit's relationship with the audit committee);
  - (e) relationships (with management, elected members and other auditors, regulators and inspectors);
  - (f) staffing, training and continuing professional development;
  - (g) audit strategy and planning;
  - (h) undertaking audit work;
  - (i) due professional care;
  - (j) reporting;
  - (k) performance, quality and effectiveness.
- 8 The best practice guidance states that the review of the effectiveness of internal audit should also include consideration of the effectiveness of the audit committee itself (to the extent that its work relates to internal audit) as well as the performance of the audit provider. A separate review of the Audit and Governance Committee's effectiveness is currently being undertaken. It is expected that the results of this review will be reported to the September meeting of this Committee.

### **Who Should Undertake the Review?**

- 9 The Regulations require either the council itself, or an appropriate committee of the council, to review the system of internal audit. The council has delegated this to the Audit and Governance Committee. The main reasons why the Audit and Governance Committee is considered as "an appropriate means through which to carry out the review of Internal Audit" are:
- (a) it is a core responsibility of the Audit and Governance Committee to approve internal audit plans and monitor the work of the service;
  - (b) the Audit and Governance Committee is independent of the management of the council;
  - (c) the annual report and the opinion of the Head of Internal Audit are considered by the Audit and Governance Committee;

- (d) the external auditor reports to the Audit and Governance Committee and is therefore readily available to give an opinion on the work of internal audit;
  - (e) the review of the effectiveness of internal audit feeds into the Annual Governance Statement which is also considered by the Committee.
- 10 A key point is that it is the responsibility of the council to conduct the annual review; it is not a review that is carried out by the external auditor as part of their annual audit. External audit review elements of internal audit's work to assess what reliance can be placed upon it for other purposes and the audit of the council's accounts. However, this review work does not cover all the elements of the system of internal audit and, therefore cannot be relied upon to properly fulfil the requirements of the Regulations.
- 11 The review of the effectiveness of internal audit has been undertaken jointly with North Yorkshire County Council by the Shared Service Contract Board (SSCB) and in consultation with the respective Audit Committee Chairs, in accordance with the process agreed by this Committee in December 2011. The SSCB comprises the respective client officers from the council and North Yorkshire County Council, and Veritau's Head of Internal Audit. Meetings of the SSCB are held quarterly and performance indicators and changes in working practices are discussed.
- 12 Using the SSCB as the focus for this annual review ensures consistency and avoids unnecessary duplication of work by the two client officers. The opinions reflected in this report reflect the shared view of the two client officers arrived at during the review. It should be noted that the statistics in this report are, of course, just in respect of the service provided to the council.

### **Scope of the Review**

- 13 The review is primarily about effectiveness, not process. In essence the need for the review is to ensure that the opinion contained in the Annual Report provided by the Head of Internal Audit may be relied upon as a key source of evidence in the Annual Governance Statement. The focus of the review has, therefore, concentrated on the delivery of the internal

audit function to the required professional standards in order to produce the required outcome i.e. a reliable assurance on internal control and the management of risks in the council, rather than an assessment of value for money.

- 14 Other sources of assurance that the Committee receives, from which it can take a view on the effectiveness of the service include:
- (a) regular monitoring reports on internal audit work and related performance measures;
  - (b) the Internal Audit Annual Report (which is a separate item on this Agenda);
  - (c) the Internal Audit Plan (the 2012/13 Plan was approved at the April 2012 meeting of this Committee);
  - (d) regular reports on the implementation of internal audit recommendations.

### **2011/12 REVIEW OF THE EFFECTIVENESS OF INTERNAL AUDIT**

- 15 For the purposes of this review, the following work has been completed:
- (a) the Code of Practice self assessment checklist has been refreshed so as to identify any significant changes in the degree of compliance against the Code
  - (b) an overview of customer survey results has been undertaken
  - (c) the opinion of external audit has been considered
  - (d) other issues regarding the quality and cost effectiveness of the service have been considered as appropriate
- 16 In previous years, the results of the latest benchmarking data available from CIPFA have been used to provide some indication of how cost-effective the service was compared to internal audit provision within other councils. Given that the service is now a shared service provided by an external body, albeit owned by the two councils involved, suitable benchmarking data has been more difficult to obtain. Alternative sources of information have therefore been used to provide evidence of the continued cost effectiveness of the current arrangements. This information supports the view that

the service remains cost effective. See paragraph 34 below for further details.

### **Update of Code of Practice Self Assessment Checklist**

- 17 The self assessment checklist has been reviewed and updated for 2011/12. This has been reviewed in the SSCB and is considered by the SSCB as a fair reflection of the priorities that need to be progressed at this time.
- 18 As previously reported to this Committee, considerable work has been undertaken to integrate working practices and systems across the shared service and to select best practice from both partners' organisations. A specific priority in 2011/12 has been the development of a more proactive approach to the identification of fraud risks, particularly within housing and adult social care services. The majority of fraud investigations are now being undertaken by Veritau's dedicated counter fraud team based at York. This has allowed a number of new tools and techniques to be deployed to combat suspected fraud within the council.
- 19 In respect of the delivery of the service for the council, it is the view of the Assistant Director – Finance, Asset Management and Procurement (who acts as the lead client for the council), that whilst there have been some changes in operational arrangements, adherence with the professional standards set out in the Code of Practice has been maintained or enhanced.
- 20 Those aspects of the current internal audit arrangements which have been identified as not complying fully with the Code of Practice are listed in Annex 1. Where changes and/or improvements to working practices are considered necessary then these have been included in the Veritau Business Plan for 2012/13, and are reflected in paragraphs 22 - 23 below.
- 21 There were a number of areas for development which were identified as part of last year's self assessment. These are listed below, with information on progress made in the year, as follows:
  - (a) **continued rotation of internal audit staff between teams and across sites to minimise the number of**

## **occasions where systems or services are subject to audit by the same member of staff**

Cross site working has been continued through 2011/12. This has produced efficiencies and allowed best practice to be more easily shared between the two councils. It has also helped to reduce the number of occasions where the audit of a specific system or area has been undertaken by the same person for a number of years. Examples of successful cross site working during the year have included the audits of:

- the Carbon Reduction Commitment submission
- personalisation in social care
- contracting and charges for social care
- workforce planning

A single schools audit team has also been created covering both councils. This has meant that staff resources can be more easily managed and has reduced travelling times. Staff rotation, however, has to be balanced with the need to maintain a level of continuity and to ensure that the knowledge gained by auditors of each system or service area is used effectively.

### **(b) Audit and Governance Committee to conduct a review of it's own effectiveness**

The Committee has established a working group to undertake this review. A self assessment questionnaire has also been completed by all the members of the Committee. The results of the review are expected to be reported to this Committee in September.

### **(c) development of a formal protocol to support joint working with other internal auditors**

The principal area which has been identified for joint working is with health. Good working relationships exist between Veritau and the NHS internal audit provider in York and North Yorkshire. Regular liaison meetings are

held and a joint audit was completed during the year to assess the baseline financial information prior to the transfer of public health responsibilities to the council (and North Yorkshire). Further joint audit work is planned in 2012/13. A memorandum of understanding has been agreed between the two audit providers and this will be further developed in 2012/13. Internal protocols exist within Veritau for work involving the council and the group's other clients (including the North Yorkshire Fire and Rescue Service and the five district council members of Veritau North Yorkshire). A standard protocol will be prepared for other potential joint working situations, for example with neighbouring authorities, North Yorkshire Police or significant partnerships in which the council has an interest.

(d) **development of a clearer methodology for determining the overall opinion of the Head of Internal Audit**

This has been completed. A new audit report format has also been developed which incorporates a clearer assessment of the probability of identified risks occurring and their likely impact.

22 The self assessment exercise has been reviewed in the light of progress made over the last year. It remains the case that whilst the service is not wholly compliant in all aspects of the code, the approach taken is considered to be appropriate in the circumstances of the service provided to the council, with the exception of two areas that continue to require further development in 2012/13, which are as follows:

- (a) As noted in paragraph 18 above, further work is required to fully embed the updated counter fraud arrangements.
- (b) As noted in paragraph 21 above, further work is required to establish a clear framework for obtaining assurance from other partner organisations.

23 In addition, reports from the Head of Internal Audit to the Audit and Governance Committee have previously been in the name of the council's client officer. It is proposed that this should change in the future with all internal audit related reports issued in the name of the Head of Internal Audit.



## **Customer Satisfaction Surveys**

- 24 In accordance with the CIPFA Code, Veritau carries out customer survey reviews as a normal part of the audit process. As part of the work to support this review of effectiveness, other surveys are also undertaken to provide further assurance. These are dealt with in turn below.
- 25 At the close of each audit, the responsible Manager of the area being audited is asked for feedback on that audit. In response to the question “Considering the audit overall, would you say that you were more satisfied than dissatisfied with the service received?” 100% assessed the audit as being satisfactory. The equivalent satisfaction score for 2010/11 was 100%.
- 26 An overall customer satisfaction survey was sent to relevant senior officers in May 2012. Five replies were received.
- 27 A summary of the questions, and the range of assessments made for the main audit service is attached as Annex 2. The majority of the assessments give an opinion of good or better. Only one “poor” assessment was made, relating to the time taken to issue audit reports. More generally, the spread of assessments for this question (1.14) suggests that this is an area for improvement, and this has been discussed with the Head of Internal Audit.
- 28 It will be noted that no responses were received for question 1.17, which relates specifically to the specialist IT audit service provided on behalf of Veritau by PWC. This service mostly relates to North Yorkshire County Council.
- 29 As well as the main internal audit service, Veritau also provides counter fraud and information governance services to the council, and the survey also covered this aspect of the Veritau work. Whilst not strictly covered by the scope of this effectiveness review, it is pleasing to note that the overall assessment of these services was mainly ‘good’ and there were no ‘poor’ responses.

## **External Audit Opinions expressed during 2011/12**

- 30 No matters of concern have been raised with the S151 Officer or the Audit and Governance Committee by the external

auditor regarding internal audit matters during 2011/12. There were also no matters raised regarding internal audit arrangements in the Audit Commission's Annual Audit Letter 2010/11, which was reported to this Committee in December 2011

- 31 The external auditor was asked for specific feedback on the work of the internal audit service during 2011/12. A copy of the letter received is attached at Annex 3.
- 32 In respect of the service provided to North Yorkshire County Council, the external auditor is Deloittes. The following response was received from Deloittes:
  - (a) We maintain an open dialogue with internal audit that allows us to share areas of concern between internal and external audit;
  - (b) Internal audit work constructively with external audit;
  - (c) We have not indentified any significant areas of concerns based on our review of the reports produced by internal audit that are relevant to the financial statement audit

**Other Issues identified regarding the quality and cost effectiveness of the service**

- 33 During 2011/12, and relevant to the overall quality of the staffing available to the internal audit service, it is appropriate to note that Veritau achieved IIP accreditation, and a number of staff completed their training, leading to membership of the Chartered Institute of Internal Auditors, hence strengthening experience and the knowledge base of the team.
- 34 In previous reviews, consideration has been given to the availability of benchmarking data with other internal audit services providers. Previously, benchmarking data was available through membership of the relevant CIPFA benchmarking club. Because of the shared service arrangement, and the fact that it is provided through an external company, it has been concluded that membership of this benchmarking club is of limited value. In terms of evidence available in relation to cost effectiveness, Veritau were involved in two tender exercises during the year. Neither were mainstream local government bodies. In both cases, the Veritau bid represented the lowest cost, although in neither

case was the contract awarded to them. This was because of issues relating to the range of skills and services that the team was able to make available, which did not meet in full the requirements of the bodies concerned. In both cases the winning tenders were submitted by large accountancy firms.

## **CONCLUSION**

- 35 Based on the results of this review, the council's internal audit arrangements are considered to be operating in accordance with accepted professional best practice, and remain effective. The Committee can therefore continue to place reliance on the internal audit arrangements operating within the council when considering the draft Annual Governance Statement for 2011/12.

## **Consultation**

- 36 This review has been undertaken jointly with the Assistant Director – Central Finance at North Yorkshire County Council and in consultation with the Chair of the Audit and Governance Committee as recommended and agreed by this Committee in December 2011.

## **Options**

- 37 Not relevant for the purpose of the report.

## **Analysis**

- 38 Not relevant for the purpose of the report.

## **Council Plan**

- 39 This report contributes to the council's overall aims and priorities by helping to ensure probity, integrity and honesty in everything it does and by helping to make the council a more effective organisation.

## **Implications**

- 40 There are no implications to this report in relation to:

- **Finance**
- **Human Resources (HR)**

- **Equalities**
- **Legal**
- **Crime and Disorder**
- **Information Technology (IT)**
- **Property**

### **Risk Management Assessment**

- 41 The council will fail to comply with the Accounts and Audit Regulations 2011 if it does not undertake a proper review of the effectiveness of internal audit as part of the wider review of the effectiveness of the system of internal control.

### **Recommendation**

- 42 Members are asked to:

- (a) Note the results of the annual review of the effectiveness of internal audit.

#### Reason

To enable members to consider the overall adequacy and effectiveness of the council's control environment.

- (b) Approve the change in reporting arrangements in respect of reports to the Committee on internal audit matters (see paragraph 23 above).

#### Reason

To ensure the council complies with the CIPFA Code of Practice.

## Contact Details

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Report  
Approved



Date 12/6/12

### Specialist Implications Officers

Not applicable

Wards Affected: Not applicable

All



For further information please contact the author of the report

### Background Papers

None

### Annexes

Annex 1 – areas of non-compliance with the CIPFA Code of Practice

Annex 2 – customer satisfaction survey results

Annex 3 – copy of letter from Lynn Hunt, Audit Manager – Audit Commission