

Internal Audit: Charter and Strategy 2019

Background

The purpose of this Internal Audit Charter and Strategy is to define internal audit's purpose, authority and responsibility, in accordance with the UK Public Sector Internal Audit Standards (PSIAS). It establishes internal audit's position within the Councils and reporting lines; authorises access to records, personnel and physical property relevant to the performance of audit work; and, defines the scope of internal audit activities.

This Charter and Strategy also covers the role of the Head of Assurance and internal audit staff, and identifies the nature of professionalism, skills and experience required.

Statutory requirements for an Internal Audit function

The role of internal audit is underpinned by the statutory requirement. This is set out in the Accounts and Audit Regulations, which states that every local authority "must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance".

The statutory requirement is also within Section 151 of the Local Government Act 1972. This states that every authority in England and Wales should "make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs" in that it should include "compliance with statutory requirement for accounting and audit".

The CIPFA statement on the Role of the Chief Financial Officer in Local Government states that the chief financial officer (CFO) must:

- Ensure that an effective internal audit function is resourced and maintained;
- Ensure that the authority has put in place effective arrangements for internal audit of the control environment;
- Support the authority's internal audit arrangements; and
- Ensure that the Audit Board/Committee receives the necessary advice and information, so that both functions can operate effectively.

In a local authority, internal audit provides independent and objective assurance to the Council, its Members, the Corporate Leadership/Management Team and in particular to the CFO, assisting the CFO in discharging his/her responsibilities under S151 of the Local Government Act 1972, relating to the proper administration of the Councils' financial affairs.

The Public Sector Internal Audit Standards (PSIAS) require that the Internal Audit Charter defines the terms ‘board’ and ‘senior management’ in relation to the work of internal audit. For the purposes of internal audit work, the ‘board’ refers to the Councils’ Audit Board / Committee, which oversees the work of internal audit. Senior management is defined as the Corporate Leadership/ Management Team.

Definition of Internal Audit

Internal audit is defined by the Chartered Institute of Internal Auditors’ International Professional Practices Framework as “an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.”

Applicable Standards that must be complied with

The internal audit function is required to comply with Public Sector Internal Audit Standards (PSIAS). The relevant internal audit standard setters, which include the Chartered Institute of Public Finance and Accountancy (CIPFA) in respect of local government, originally adopted PSIAS from 1 April 2013. PSIAS was subsequently revised and updated in 2017. The Standards encompass the mandatory elements of the Chartered Institute of Internal Auditors (CIIA) International Professional Practices Framework (IPPF). Compliance with these Standards is subject to a quality assurance and improvement programme in line with PSIAS.

The PSIAS incorporate a code of ethics to promote an ethical and professional culture. Auditors are required to comply with this code, as well as any code of ethics from other professional bodies they belong to and any code of ethics required by the partner Councils.

Responsibility of Internal Audit

The Head of Assurance must deliver an annual internal audit opinion and report that can be used by the partner organisations to inform its annual governance statement. The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and control. This is the ‘assurance role’ for internal audit. In order to achieve this, the internal audit function has the following objectives:

- To provide a quality, independent and objective risk-based audit service that effectively meets the Councils’ needs, adds value, improves operations and helps protect public resources.

- To provide assurance to management that the Councils' operations are being conducted in accordance with external regulations, legislation, internal policies and procedures.
- To provide a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, internal control and governance processes.
- To provide advice and support to management to enable an effective control environment to be maintained.
- To promote an anti-fraud, anti-bribery and anti-corruption culture within partner Councils, to aid the prevention and detection of fraud.
- To investigate allegations of fraud, bribery and corruption via the counter fraud team.

Responsibility of the Councils

Councils are responsible for ensuring that internal audit is provided with all necessary assistance and support to ensure that it meets the required standards.

The Councils' Financial Regulations are specific about the role of the Chief Financial Officer in relation to internal audit, setting out access rights, independence and support for resources sufficient to provide an opinion and support managers to prevent and detect fraud.

Financial Regulations specify the responsibilities of the Directors in terms of access, explanations, reporting of allegations of fraud and engaging with the audit process.

The respective roles of managers in relation to internal audit are also set out in Financial Regulations. In addition, there is a straightforward assurance framework, which assists in understanding the role of internal audit in the overall risk management and internal control processes in the Councils. This framework is commonly referred to as the 'three lines of defence' model.

Operational management is responsible for ensuring that systems of internal control are in place, good business practices are implemented and followed in all areas, compliance is maintained, risks, including fraud risks, are identified and mitigated, and effective governance is established. This is the 'first line' of defence.

The second line of defence is performed by those responsible for oversight functions, generally the policy / system owner. They set boundaries by drafting and implementing policies and procedures. They are also responsible for guidance and directions for implementing their policies and for monitoring their proper execution. They therefore provide oversight over business processes and risks.

The Council's third line of defence includes internal audit, which should provide independent assurance to senior management and the Audit Board / Committee on how effectively the first and second lines of defence have been operating.

Notwithstanding the above, the internal audit service may, on occasion, be required to undertake a range of reviews which, through volume testing, identify and examine the levels of organisational compliance with council policies, procedures, financial regulations and legislation. As a result of these reviews, an assessment can be provided on the degree of compliance across the councils and can help services to improve their systems to facilitate greater compliance in the future.

The individual topics of work undertaken by the internal audit service include:

- Audit planning
- Risk-based audit reviews
- By exception, compliance reviews
- Investigating issues and concerns raised by services
- Auditing grant claims
- Follow up audit reviews
- Consultancy advice on controls and system development

Each individual audit assignment is governed by a specific terms of reference for that piece of work, detailing the scope of the audit and elements that will be covered, and if appropriate, the resources to be applied and the timeframe.

There is a separate terms of engagement covering counter fraud work, setting out in detail the respective responsibilities of the counter fraud team and managers, such as:

- Independent investigation function
- Advice around whether it is a fraud issue
- Fraud awareness.

This is supplemented by Council Policies which include:

1. The Anti-Fraud and Corruption response plan/Strategy
2. The Anti-Money Laundering response plan/Policies
3. Anti-Bribery Policies

These provide detailed guidance on what to do if a manager discovers fraud, corruption, money laundering or has an allegation reported to them.

Head of Assurance

The Head of Assurance is the Chief Audit Executive as referred to in the Public Sector Internal Audit Standards (PSIAS). They will have sufficient skill, experience and competencies to work with the leadership team and the Audit Board/Committee, influencing risk management, governance and the internal control environment of each Council. The Head of Assurance will hold a full, professional qualification, defined as CCAB, CMIIA or equivalent professional membership, and adhere to professional values and the Code of Ethics.

The Head of Assurance is responsible for ensuring that there is access to the full range of knowledge, skills, qualifications and experience to deliver the audit plan and meet the requirements of the PSIAS. In addition to internal audit skills, the Head of Assurance will specify any other professional skills that may be needed by the internal audit team.

Independence of Internal Audit

Managers and staff within internal audit are required to make annual declarations of interest and declarations must be made, if required, by all other staff, in accordance with each Council's declaration's policy. Everyone is reminded of the need to make annual declarations of interest. Declarations made are reviewed by management and, if required, appropriate control measures are put in place to prevent conflicts of interest.

Where appropriate, internal audit may provide advice and support, regarding risk and controls, during the design and implementation of new systems. In such cases, independence is preserved by ensuring that the person providing this support takes no part in any subsequent audit.

Audit assignments are distributed in such a way as to ensure that independence is maintained and objective opinions can be given. Auditors work on a wide range of assignments and do not focus on any particular area of the Council's business.

When auditors are recruited from within the Council, they cannot audit the area where they previously worked for at least six months, to preserve the auditor's independence.

Relationships

The Head of Assurance reports directly to the S151 Officer of each Council, and the Director of Finance for oneSource.

The Head of Assurance has direct access to the Head of Paid Service (Chief Executive or equivalent), all levels of management and elected members, as set out in each Council's financial regulations.

The Head of Assurance can meet separately with the Chair of the Audit Board/Committee, if required.

The Head of Assurance, or an appropriate representative of the internal audit team, attends meetings of the Audit Board/Committee.

The Head of Assurance, or an appropriate representative, attends meetings of the partner Councils' senior management teams to discuss the audit plan, following consultation over the proposals with Directors.

Scope of Internal Audit

Responsibility

Even sound systems of internal control can only provide reasonable and not absolute assurance and may not be proof against collusive fraud. Internal audit procedures are designed to focus on areas identified by the organisation as being of greatest risk and significance and rely on management to provide full access to accounting records and transactions for the purposes of audit work and to ensure the authenticity of these documents.

Due Professional Care

The internal audit function is bound by the following standards:

- Institute of Internal Auditor's International Code of Ethics
- Seven Principles of Public Life (Nolan Principles)
- UK Public Sector Internal Audit Standards.
- All Council policies and procedures
- All relevant legislation
- Any code of ethics prescribed by an accounting or audit body to which an auditor is a member of.

Internal audit is subject to a Quality Assurance and Improvement Programme that covers all aspects of internal audit activity. This consists of an annual self-assessment of the service and its compliance with the UK Public Sector Internal Audit Standards, ongoing performance monitoring and an external assessment at least once every five years by a suitably qualified, independent assessor.

Opinion work

The PSIAS state that the Head of Assurance is responsible for developing a risk-based plan. This takes into account the organisation's risk management framework, including using risk appetite levels set by management for the different activities or parts of the organisation. If a framework does not exist, the Head of Assurance uses his/her own judgment of risks, after consideration of input from senior management and the board. The Head of Assurance must review and adjust the plan, as necessary, in response to changes in the organisation's business, risks, operations, programs, systems, and controls.

The risk-based plan must take into account the requirement to produce an annual internal audit opinion and the assurance framework. It must incorporate or be linked to a strategic or high-level statement of how the internal audit service will be delivered and developed in accordance with the Internal Audit Charter and how it links to the organisational objectives and priorities.

For each audit assignment, terms of reference are developed and agreed with the client setting out the scope of the audit. At the completion of the audit, a report is produced which provides an audit opinion on the control environment in place.

The risk based plan is a live document and subject to reviews in year to take account of changes in the risk environment and internal factors within each Council.

Outcomes from audit reports are submitted to the Audit Board/Committee for information and discussion.

Non-opinion work

From time to time, the internal audit service will undertake work which does not contribute explicitly to the overall audit opinion. These will be probity or regularity audits in response to investigations, certification of grant claims or limited consultancy exercises in the form of support for new systems being developed.

Where such work is undertaken, this is set out as part of the Head of Assurance's annual report. The risk, for which the work is providing assurance, is also specified.

Prior to accepting any consultancy work, due consideration is given to its potential impact on the independence of internal audit and the impact on the ability of the section to provide sufficient assurance to provide an opinion on the Council's overall control framework.

Fraud

Managing the risk of fraud is the responsibility of line management; however the Section 151 Officer retains specific responsibilities in relation to the detection and investigation of fraud.

The wider internal audit service supports the Pro-Active Audit & Counter Fraud Team to provide a counter fraud function to support the Section 151 officer in the discharge of his/her responsibilities.

Fraud risks are also considered as part of the scope for audit assignments and specific testing takes place to ensure that there are adequate controls in place to prevent and detect fraud, errors and omissions, as part of the opinion work.

The oneSource Counter Fraud team is trained to deal with cases to a criminal standard and adhere to a range of legislative requirements to enable cases to be prosecuted, where necessary.

The Counter Fraud team undertakes work of a proactive nature through various data matching exercises. The aim is to try to identify potential frauds at an early stage, assess the controls against the risks and enable identified fraud to be dealt with whilst giving a level of assurance over Council data.

The Counter Fraud team also responds reactively to allegations of fraud from both internal and external sources, aiming to investigate cases where appropriate to a criminal standard. Council policies require that the Assurance Service is notified of all suspected or detected fraud and corruption.

The Counter Fraud team maintains and updates each Council's Counter Fraud policies, including:

- Anti-fraud and corruption policy statement
- Anti-fraud and corruption publicity policy
- Anti-fraud and corruption prosecution policy
- Anti-bribery policy
- Anti-money laundering policy
- Policy for the use of the confiscation regime within the Proceeds of Crime Act 2002.

The team also maintains specific, detailed guidance for managers to help them to deal with situations that they may be unfamiliar with the:

- Anti-fraud and corruption response plan/Strategy
- Anti-money laundering response plan/Policy

They also provide training and resources to enable officers to identify and prevent fraud in the design and control of their systems.

Work carried out by the Counter Fraud team is reported to Members and contributes to the Head of Assurance's annual opinion.

Reporting

The UK Public Sector Internal Audit Standards require the Head of Assurance to report to the top of the organisation and this is done in the following ways:

- The Internal Audit Charter and any amendments are reported to senior management team and the Audit Board/Committee. The annual Internal Audit Plan is compiled by the Head of Assurance, taking account of the risk framework and after input from directors and heads of service. It is then presented to the senior management team, the oneSource Management team and Audit Board/Committee, annually, for noting and comment.
- The adequacy, or otherwise, of the level of internal audit resources (as determined by the Head of Assurance) and the independence of internal audit will be reported annually to the Audit Board/Committee. Performance against the Internal Audit Plan and any significant risk exposures and control issues arising from audit work are reported regularly to Audit Board/Committee.
- Any significant consulting activity not already included in the audit plan and which might affect the level of assurance work undertaken will be reported to the Audit Board/Committee.
- Any instances of non-conformance with the Public Sector Internal Audit Standards will be included in the annual Head of Assurance report. If there is significant non-conformance, this may be included in the partner Council's Annual Governance Statement.

Internal Audit Access Rights

Internal audit has unrestricted access to all records and information, both manual and computerised, cash, stores and other property or assets it considers necessary to fulfil its responsibilities. Audit may enter a property and has unrestricted access to all locations and officers where necessary, on demand, and without prior notice. Right of access to other bodies funded by the Council should be set out in the conditions of funding.

Internal Audit Resources

Internal audit must have sufficient resources in terms of numbers, grades, qualifications, levels of experience, having regard to its objectives and to the Public Sector Internal Audit Standards.

The Head of Assurance is responsible for ensuring that the resources of the Internal Audit Service are sufficient to meet its responsibilities. If a situation arose whereby resources were insufficient this will be reported to the Directors of Finance, the Section 151 Officers and, if not resolved, Audit Board/Committees.