TITLE   Effectiveness of Internal Audit and Counter Fraud
                 Arrangements Report

FOR CONSIDERATION BY   Audit Committee on 1 July 2014

WARD   None Specific

DIRECTOR   Julie Holland, Service Manager, Business
                    Improvement (and Head of Internal Audit)

OUTCOME / BENEFITS TO THE COMMUNITY

Internal Audit conducts an in-house annual review which assesses the effectiveness of the Internal Audit function and provides assurance over its compliance with the Public Sector Internal Audit Standards (PSIAS). This annual assessment is mandatory for all Public Bodies governed by the Accounts and Audit Regulations.

This year we incorporated an assessment of the counter fraud service which is delivered by the Investigations team. They aim to promote an anti-fraud and anti-corruption culture and investigate allegations of fraud, corruption and malpractice as defined in its business objectives. In the course of their duties the team must comply with the relevant legislation, codes of practice and council policies.

RECOMMENDATION

That the Audit Committee note the Effectiveness of Internal Audit and Counter Fraud Arrangements report (see attached).

SUMMARY OF REPORT

The review was conducted by an Internal Audit contractor and reported directly to the Head of Internal Audit.

This review is an assessment of Internal Audit's compliance against the Public Sector Internal Audit Standards (PSIAS) and of the controls in place for the prevention, detection and investigation of fraud and corruption.

The review highlighted that:

The council's Internal Audit (IA) unit was, with the exception of Standard 2050, broadly complying with the Public Sector Internal Audit Standards (PSIAS) and satisfying the professional standards laid down by the Chartered Institute of Internal Auditors.

Standard 2050 relates to coordination of activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimise duplication of efforts. The review did however identify a strong relationship with the External Auditor.

There were also two areas where, because of factors obtaining at the time of the review, compliance could not be confirmed. The first related to the role specifications for the

audit manager and team members being revised, and the review therefore had no definitive role specifications to evaluate against the Standards.

Also at the time of this review the team's "IT Lead" auditor had recently left. However, there was an adequate body of evidence to support the 2013-14 Internal Audit Assurance over the council's IT-related risks. This had been provided by the verification process (including over data and network security) the Council had had to satisfy prior to connection to the Public Services Network.

The arrangements of the council's Investigations unit to ensure that its work complies with all relevant legislation were effective; and, based on the evidence of those of its clients we contacted, its work was meeting the standards of rigor and reliability expected by its clients and users within and outside the council.

Background

Internal Audit aims to provide an 'independent and objective opinion to the organisation on the control environment comprising risk management, control and governance by evaluating its effectiveness in achieving the organisations objectives.'

The Investigations team 'is responsible for providing a comprehensive investigation service to all stakeholders, in order to prevent, detect and take appropriate action to all internal and external fraud, theft and error and to drive improvements in performance across the council.'

This audit was thought to add more value to the organisation if the effectiveness of Internal Audit and the counter fraud arrangements were reviewed together.

Analysis of Issues

This audit report provides the committee with assurance over Internal Audits compliance with the PSIAS. Furthermore, there is assurance that the controls in place for the prevention, detection and investigation of fraud and corruption are working effectively.

The committee can be assured that the audit was conducted in a professional manner and in compliance with the following IIA Standards to ensure independence and objectivity were being maintained. These are:

- 1100 Independence and Objectivity – The internal audit activity must be independent, and internal auditors must be objective in performing their work.
- 1120 Individual Objectivity – Internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest; and
- 1200 Proficiency and Due Professional Care – Engagements must be performed with proficiency and due professional care.

FINANCIAL IMPLICATIONS OF THE RECOMMENDATION
The Council faces severe financial challenges over the coming years as a result of the austerity measures implemented by the Government and subsequent reductions to public sector funding. It is estimated that Wokingham Borough

Council will be required to make budget reductions in excess of £20m over the next three years and all Executive decisions should be made in this context.

	How much will it Cost/ (Save)	Is there sufficient funding – if not quantify the Shortfall	Revenue or Capital?
Current Financial Year (Year 1)	N/A	Yes	N/A
Next Financial Year (Year 2)	N/A	Yes	N/A
Following Financial Year (Year 3)	N/A	Yes	N/A

Other financial information relevant to the Recommendation/Decision

N/A

Cross-Council Implications

N/A

Reasons for considering the report in Part 2

N/A

List of Background Papers

N/A

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Date 5 June	**Version No.** 2.0

2013-14 Review of the Effectiveness of Business Assurance - Report

Introduction

1. This review was conducted in March 2014 for Wokingham Borough Council, and was sponsored by the Service Manager - Business Improvement.

2. The review covered the Investigations and the Internal Audit components of the "Business Improvement" remit. On the Internal Audit side it met the Service Manager's in-year responsibility under **IIA Standard 1310**[1] and PSIAS, which requires her to have a Quality Assurance and Improvement Programme for the Internal Audit Unit. The Standard states: "The quality assurance and improvement programme must include both internal and external assessments. **Standard 1311** adds: "Internal assessments must include:
   - Ongoing monitoring of the performance of the internal audit activity; and
   - Periodic self-assessments or assessments by other persons within the organisation with sufficient knowledge of internal audit practices."

3. The review was conducted by Jeremy Opie, CMIIA who was engaged as an internal auditor for the council on a fixed term contract. As such, he satisfied the criterion set out in the second bullet of Standard 1311.

4. The review's Terms of Reference are at Annex A.

Summary of findings

5. The council's Internal Audit (IA) unit was, with the exception set out in paragraphs 7 and 8 below, broadly complying with the Public Sector Internal Audit Standards (PSIAS) and satisfying the professional standards laid down by the Chartered Institute of Internal Auditors. There were also two areas (including that covered by item 1b of the ToR) where, because of factors obtaining at the time of the review, compliance could not be confirmed (see paragraphs 12 – 16). An assurance can be given for all ToR items 1 c-i.

6. The arrangements of the council's Investigations unit to ensure that its work complies with all relevant legislation were effective; and, based on the evidence of those of its clients we contacted, its work was meeting the standards of rigour and reliability expected by its clients and users within and outside the council. An assurance can be given for ToR items 2 a and b.

Area of non-Compliance by the IA Unit

7. **Standard 2050** says: "The [service manager] should share information and coordinate activities with other internal and external providers of assurance and

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[1] The "Standards" are the Global Standards of the Institute of Internal Auditors. These are the Standards on which the Public Sector Internal Audit Standards (PSIAS) are based. See PSIAS "Introduction", paragraph 3.

consulting services to ensure proper coverage and minimise duplication of efforts."

8. At the time of this review the IA unit did not have an up-to-date and comprehensive account of all the sources of assurance available to the council. Hence there was no basis on which to plan the overall coordination of assurance activities or sharing of information. **To this extent, the IA unit was not able to comply with Standard 2050.**

9. The IA Manager acknowledged this shortcoming. He planned to address it in the first instance by requesting all directors to submit details of their 3rd party assurance providers.

10. This review suggests that the unit should conduct an outline risk evaluation of the risks for the council of not effectively assessing the scale, resource costs and effectiveness of its assurance "system". If the identified risks are material, they could be addressed in a future internal audit.

11. In one important aspect of coordination and information sharing, the IA unit was already effective: namely, with the council's external auditor. In operational areas where both parties had an interest, such as in "Key Financials", the IA unit's substantive testing was designed to meet external audit's specification. This minimised the potential duplication of effort for the council's operational staff; and the fact that the external auditors took assurance from the IA team's work meant that their fee to the council was lower than it would have been had they had to perform all the work themselves.

Areas where Compliance by the IA Unit could not be confirmed

Proficiency and Due Professional Care

12. **Standard 1200** covers **Proficiency and Due Professional Care. Standard 2030**, covering **Resource Management**, states: "The [service manager] must ensure that internal audit resources are appropriate, sufficient and effectively deployed to achieve the approved plan."

13. At the time of this review the IA unit was being reorganised to enhance its efficiency; aiming at a "flatter" structure which devolved more responsibility for assignment quality assurance from the manager to the audit team members. Accordingly the role specifications for the audit manager and team members were being revised, and the review therefore had no definitive role specifications to evaluate against the Standards.

14. The Internal Audit Manager told the review that new job descriptions were being developed which would provide the basis of each member's proficiency specification. These would then allow the unit to define each member's supervision and training and development requirements.

IT Auditing

15. **Standard 1210-A3** sets out the unit's IT auditing competency requirement. It states: "Internal auditors must have sufficient knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work. However, not all internal auditors are expected to have the expertise of an internal auditor whose primary responsibility is information technology auditing."

16. At the time of this review the team's "IT Lead" auditor had recently left, while, as noted at paragraph 8 above, the role of the IA Manager himself, who had an adequate level of IT audit proficiency, was under review. However, there was an adequate body of evidence to support the 2013-14 Internal Audit Assurance over the council's IT-related risks. This had been provided by the verification process (including over data and network security) the Council had had to satisfy prior to connection to the Public Services Network. Beyond this, the unit's need for IT auditing proficiency would be addressed by the new job descriptions being developed (see paragraph 9 above) and by recruitment of new staff.

Areas of Good Practice

Transition to, and promotion of, risk-based auditing

17. **Standard 2010.A1** says: "The internal audit activity's plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process."

18. The IA Unit's 2014-15 audit plan proposed that eight out of around 70 audits would address risks on the council's Corporate Risk Register (CRR). The CRR currently contained 13 risks. Hence, under this approach the management of over half of the council's paramount risks would be evaluated.

19. This review concluded that if the planned approach were successfully implemented it would serve to demonstrate that the IA unit's resources were being deployed efficiently: because they were scrutinising the council's perceived greatest risks. But this degree of concentration on the council's top-level risks would also optimise the unit's ability to evaluate – as it must do to inform its end-of-year report - the effectiveness of the council's risk management arrangements.

Whole-Team Commitment to Professionalism

20. The IA Manager informed the review that he would henceforth be requiring IA team members to confirm annually that they had (re-)familiarised themselves with the PSIAS and IIA Code of Ethics.

21. The review commends this initiative as an example of good practice in demonstrating and promoting the IA unit's commitment to professionalism.

<u>The Investigations Unit</u>

22. The maintenance arrangements for the inventory of legislation and regulations to be complied with worked effectively, to the satisfaction of the Senior Investigations Officers.

23. The risk that the unit could be "caught out" by a change in the governing legislation was considered low, because the relevant legislation governing the gathering of evidence has, in the experience of the team, changed only occasionally, and the changes have been well-publicised.

24. A representative of Shared Legal Services informed the review that throughout his experience of using the Investigations team's evidence, the quality of that evidence had always been sufficient, and had never, in itself, jeopardised the outcome of a case.

2013-14 Independent Assessment of Effectiveness of Business Assurance

Assignment Specification

Date: 28-2-2014

1. Examine the work of the IA unit to provide an assurance:
   a) that the team's policies and process specifications – including its Quality Management System – enable it to satisfy the professional standards laid down by the Chartered Institute of Internal Auditors, and comply with Public Sector Internal Audit Standards (PSIAS);
   b) that the team's roles and responsibilities are set out comprehensively and clearly, and, given the scope of the team's remit as defined in the Audit Charter, that all necessary roles are covered;
   c) that the team has the professionally-certified competence to undertake and/or supervise all the assignments in the annual programme;
   d) that the plans and arrangements to ensure the team's medium-term competency requirements are met are effective;
   e) that the arrangements for providing any identified short-term missing competencies required by the programme are effective;
   f) that the team is fully equipped to adhere to its policies and processes;
   g) that the team makes effective use of all relevant policies and processes in each assignment;
   h) that the team's clients, including executives and the Audit Committee, are enabled and encouraged to provide meaningful and measurable feedback on the effectiveness and value of the team's work;
   i) that clients' feedback is evaluated by IA management and lessons learned;
   j) and to make recommendations for remedying any inadequacies or aspects of non-compliance identified.
2. Examine the work of the Investigations unit to provide an assurance that its work:
   a) complies with all relevant legislation;
   b) is meeting the standards of rigour and reliability expected by its clients and users within and outside the council.
3. The IA review will examine the current policies and processes, the work of members of the IA team, and samples of client feedback. The Investigations review will seek evidence from the team's users, including Shared Legal Solutions.
4. The review will report to the Interim Head of Business Assurance (and Head of Internal Audit).