



<u>Committee and Date</u>	<u>Item</u>
Audit Committee	
30 th July 2021	
10:00 am	<u>Public</u>

ANNUAL REVIEW OF INTERNAL AUDIT: QUALITY ASSURANCE AND IMPROVEMENT PROGRAMME (QAIP) 2021/22

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1. This report confirms, following a self-assessment quality assurance review (QAIP) , that Internal Audit complies with the Public Sector Internal Audit Standards (PSIAS) and where there is some limited partial conformance, this is normal in local government environments and not significant enough for escalation in the Annual Governance Statement. An external assessment is also planned for the current year, in compliance with the PSIAS.

2. Executive Summary

- 2.1 The Accounts and Audit Regulations 2015 (5) require the Council to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, considering Public Sector Internal Auditing Standards (PSIAS) or guidance.
- 2.2 As part of the Service's Quality Assurance and Improvement Programme (QAIP), this report provides the results of a self-assessment of the Internal Audit Service against the requirements of the Public Sector Internal Audit Standards. Compliance with these standards demonstrates an effective Internal Audit Service. Audit Committee is required to review this report and its findings.
- 2.3 This review should be read in conjunction with the Annual Internal Audit report, found elsewhere on this agenda. When read together the two reports demonstrate the effectiveness of internal audit. The update of the self-assessment has confirmed that the Council continues to operate an effective Internal Audit function. There are no areas where the Internal Audit function is not complying with the Code and, whilst there are areas of partial compliance, these are not considered significant and do not compromise compliance with the code.

2.4 The Public Sector Internal Audit Standards (PSIAS), also contain the requirement for an external assessment of the Internal Audit function once every five years. The Council needs to ensure that the next assessment is undertaken by 31st March 2022. This report sets out the considerations of the Section 151 Officer in agreeing the approach with the Chairman of the Audit Committee and the Head of Audit.

3. Decisions

The Committee is asked to consider and endorse, with appropriate comment,

- 3.1. The conclusion that the Council employs an effective internal audit to evaluate its risk management, control and governance processes that complies with the principles of the Public Sector Internal Audit Standards and has planned improvement activities to work towards full compliance where appropriate.
- 3.2. The approach adopted for the external assessment and agree that the final details of the assessment are agreed by the Section 151 Officer and Head of Audit in consultation with the Chairman of the Audit Committee.

REPORT

4. Risk Assessment and Opportunities Appraisal

- 4.1 The Accounts and Audit Regulations 2015 (section 5) require a relevant authority to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, considering public sector internal auditing standards (PSIAS) or guidance.
- 4.2 Under the PSIAS, Internal Audit's mission is, 'to enhance and protect organisational value by providing risk-based and objective assurance, advice and insight.' Internal auditing is 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. Thereby providing assurances on the Council's internal control systems by identifying areas for improvement or potential weaknesses and engaging with

management to address these in respect of current systems and during system design. Internal Audit will also continue to align its work with the Strategic Risk Register.

- 4.3 The use of a consistent framework for internal audit across the UK public sector has benefits for both partnership working and for internal auditors who work across different parts of the public sector. The standards are designed to drive improvement and lead to better public finance arrangements. Under 1310 of the PSIAS there is a requirement for Internal assessments which include:
- Ongoing monitoring of the performance of the internal audit activity; and
 - Periodic self-assessments or assessments by other persons within the organisation with enough knowledge of internal audit practices.
- 4.4 Ongoing monitoring is an integral part of the day-to-day supervision, review and measurement of the internal audit activity and is incorporated into the routine policies and practices used to manage the activity. It uses processes, tools and information considered necessary to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics and the Standards.
- 4.5 This Report provides Members with details of an annual assessment conducted to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics and the Standards. It is completed by the Head of Audit and discussed with the Section 151 Officer before the results and improvement plan are reported to Audit Committee.
- 4.6 Under 1312 of the PSIAS there is a requirement for External assessments every five years which include:
- The form and frequency of external assessment.
 - The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.
- An independent external assessment must be completed by a body independent to the organisation qualified in the practice of internal auditing. Independence for these reviews is critical to ensure an objective external assessment will demonstrate to the Audit Committee compliance with the PSIAS and the improvement plan will show actions to close any gaps.
- 4.7 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998. There are no direct environmental or equalities consequences of this proposal.

5. Financial Implications

- 5.1. The Internal Audit service is provided within approved budgets.
- 5.2. There may be a small cost to enable an external assessment of Internal Audit's conformance with the PSIAS. The Chairman, Section 151 Officer and the Head of Audit have delegated authority to consider the approach/scope of the assessment and agree this with an external assessor and report back to the Committee.
- 5.3. Funding for an external assessment will be met from an approved corporate budget

6. Climate Change Appraisal

- 6.1. Energy and Fuel Consumption – This report does not directly make decisions on energy and fuel consumption. Therefore, no effect.
- 6.2. Renewable Energy Generation – This report does not directly make decisions on renewable energy generation. Therefore, no effect.
- 6.3. Carbon offsetting or mitigation – This report does not directly make decisions on carbon offsetting or mitigation. Therefore, no effect.
- 6.4. Climate Change Adaption – This report does not directly make decisions on climate change adaption. Therefore, no effect.

7. Background

Internal QAIP

- 7.1. The Public Sector Internal Audit Standards (PSIAS) are mandatory for all principal local authorities and were updated in 2017. They consist of:
 - Mission of Internal Audit;
 - Definition of Internal Auditing;
 - Core Principles for the Professional Practice of Internal Auditing;
 - Code of Ethics; and
 - Standards for the Professional Practice of Internal Auditing.
- 7.2. The 'Mission' of Internal Audit is, 'to enhance and protect organisational value by providing risk based and objective assurance, advice and insight'. Internal Audit's effectiveness is demonstrated when the following principles are present and operating effectively.
 - Demonstrates integrity
 - Demonstrates competence and due professional care
 - Is objective and free from undue influence
 - Aligns with the strategies, objectives, and risks of the organisation
 - Is appropriately positioned and adequately resourced

- Demonstrates quality and continuous improvement
- Communicates effectively
- Provides risk-based assurance
- Is insightful, proactive and future focused
- Promotes organisational improvement.

7.3. Internal Audit is reviewed using CIPFA's updated Local Government Application Note for the United Kingdom Public Sector Internal Audit Standards (April 2019) for compliance with the Standards, the results of which are summarised in **Appendix A**.

7.4. The PSIAS aim to promote further improvement in the professionalism, quality and effectiveness of internal audit across both the public and private sectors. They reaffirm the importance of robust, independent and objective internal audit arrangements to provide the Executive Director of Resources (the Section 151 Officer) with the key assurances he needs in both managing the financial affairs of the Council and producing the annual governance statement.

7.5. In complying with the PSIAS, Shropshire Council can provide assurances to Internal Audit's external customers of the teams' professionalism, quality and effectiveness.

7.6. **Appendix A** provides an update against the previously approved improvement plan. Most standards are complied with totally. Where there are areas of partial conformance these are detailed below for members to consider further. Members should note that there are no new areas of none or partial compliance. Where further improvements have been identified in areas of compliance these, along with the actions outlined below, appear in the improvement plan within the appendix, to ensure continuing conformance to the standards.

External QAIP

7.7. The last external assessment report was conducted by CIPFA¹ and reported to the February 2017 Audit Committee, it is now time for a repeat review.

7.8. In 2017 it was agreed that the procurement be completed through the Staffordshire Chief Auditors Group, this option is not currently available.

7.9. Options this year include:

¹ Chartered Institute of Public Finance Accountancy

- Establishing interest in a peer review
- Procuring the services of an external self-assessor directly

7.10. A peer review would involve the participating authorities undertaking a review of another authority. Considerations would include:

- (a) Due to the different management arrangements for the audit teams across other authorities, there is a danger of inconsistency.
- (b) As authorities regularly support each other in the development of documents/ processes via networking events, there is a risk that a peer review would not be objective.
- (c) To undertake the reviews in-house would have a significant impact on Shropshire's internal resources. The work would include specification, completion of Shropshire's self-assessment and collating the necessary documentary evidence. This would be a considerable task but would also require at least three days undertaking an assessment at another authority plus additional days for feedback, compiling a report and presentation to the Audit Committee. The team is currently supporting vacancies and recovering from the impact of Covid and therefore under pressure.
- (d) There is also a strong view by those involved in this arrangement that to undertake the reviews in this way would not give a true independent assessment as required by the Standards.

7.11. Procurement of the assessment from a standard setter, such as CIPFA or the Institute of Internal Auditors (IIA) would ensure that the quality of the assessment is at the highest level sending a clear message to all on the service. The assessment is expected to be a low value contract; therefore, two written quotations will be sought as a minimum.

7.12. Audit Committee are asked to endorse the decision to go out to market for quotations from an external assessor. The outcome of which will be reported back to the Committee.

8. Additional Information

Internal Assessment: Areas of potential non-conformance

8.1. There is no change to the areas of potential conflict from previous years, the details of which are repeated here:

8.2. **Code of Ethics - Objectivity Standard:** Do internal auditors display objectivity by not taking part in any activity or relationship that may impair or be presumed to impair their unbiased assessment?

Finding: It is felt important that internal audit is consulted during system, policy or procedure development. Auditors have been assigned to business review projects where there is a possibility that internal control systems will be affected. This is an opportunity for internal audit to add value and strengthen internal control arrangements. Where specific auditors have been involved in providing system advice, they will be excluded from carrying out the audit as far as possible i.e. another auditor would be allocated to the audit. If this is not possible, it is felt the benefit of using the experience of developing controls and procedures outweighs concerns of independence and the review process will help to ensure that the review and report remain objective and evidenced based.

Where auditors have been involved in supporting service areas in response to COVID, different auditors will conduct any system reviews initially in these areas.

There is therefore **partial** conformance. This is not considered to be to the detriment of the principles of auditing and the independent review process helps to mitigate any risks, therefore no actions are proposed.

- 8.3. **1100 Independence and Objectivity Standard:** Does the Chief Audit Executive (CAE) confirm to the board, at least annually, that the internal audit activity is organisationally independent? The following examples **can be** used by the CAE when assessing the organisational independence of the internal audit activity: The board:

Approves the internal audit budget and resources plan.

Finding: It is the responsibility of the Section 151 Officer to ensure that the budget and resources allocated to internal audit are sufficient to ensure delivery of the plan and to report any concerns to the Audit Committee.

Approves decisions relating to the appointment and removal of the CAE

Finding: It is the responsibility of the Section 151 Officer to ensure that the budget and resources allocated to internal audit are sufficient to ensure delivery of the plan, including the appointment and removal of the CAE, and to report any concerns to the Audit Committee.

Therefore, **partial** conformance: Governance requirements in the UK public sector would not generally involve the board approving the

CAE's remuneration specifically. The underlying principle is that the independence of the CAE is safeguarded by ensuring that their remuneration or performance assessment is not inappropriately influenced by those subject to audit. In the UK public sector, CIPFA advise that this can be achieved by ensuring that the Chief Executive (or equivalent) undertakes, countersigns, contributes feedback to or reviews the performance appraisal of the CAE and that feedback is also sought from the Chair of the Audit Committee, this is completed for Shropshire Council.

The Section 151 Officer also seeks, as he deems appropriate, opinions from the Chairs of externally serviced Audit Committees and their key officers on the Head of Audit's performance for use in her appraisal.

8.4. *The above are not considered significant variations in respect of the principles of the PSIAS to require specific mention in the Annual Governance statement.*

8.5. In addition to the internal assessment, an external assessment was conducted on and reported by CIPFA in February 2017. The opinion of CIPFA was that Shropshire Council Audit Services, 'generally conforms to the requirements of the Public Sector Internal Audit Standards and to the requirements of the Local Government Application Note'. All recommended improvements agreed following the external assessment, which were of a minor nature, were adopted within the agreed timeframes. An external assessment is now due as reported earlier in this report.

9. Conclusions

- 9.1. Following an updated self-assessment, the Internal Audit Team generally confirm to the PSIAS, there are some ongoing improvements planned and underway.
- 9.2. An external assessment review approach is to be considered and agreed to by the Audit Committee for procurement.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

- Accounts and Audit Regulations 2015
- Public Sector Internal Audit Standards 2017
- Local government application notes for the UK Public Sector Internal Audit Standards CIPFA 2019
- Completed Conformance Checklist 2019/20 and supporting evidence

- Internal Audit Quality Assurance Improvement Programme – External assessment report, Audit Committee, February 2017.

Cabinet Member (Portfolio Holder)

Lezley Picton, Leader of the Council and Brian Williams, Chairman of Audit Committee

Local Member

N/A

Appendices

Appendix A: Public Sector Internal Audit Standards conformance assessment and improvement plan

Appendix A

Public Sector Internal Audit Standards July 2021 conformance assessment and improvement plan

Standard	Conform	Observations and actions proposed
Mission	Yes	
Definition of Internal Audit		
Code of Ethics		
Integrity		4.1 Plan ongoing compliance updates with PSIAS at team meetings. Quarterly Head of Audit
Objectivity	Partially	Internal audit is consulted during system, policy or procedure development. Auditors have been assigned to business review projects where there is a possibility that internal control systems will be affected. This is an opportunity for internal audit to add value and strengthen internal control arrangements. Where specific auditors have been involved in providing system advice, they will be excluded from carrying out the audit as far as possible i.e. another auditor would be allocated to the audit. If this is not possible, it is felt the benefit of using the experience of developing controls and procedures outweighs concerns of independence and the review process will help to ensure that the review and report remain objective and evidenced based. Where auditors have been involved in supporting service areas in response to COVID, different auditors will conduct any system reviews initially in these areas.
Confidentiality		4.3 Ensure all filing conforms with retention guidelines. 4.3 Review Audit manual documents and contents are up to date Ongoing Principal Auditors
Competency		4.4 Set dates for appraisals. Autumn 2021 Principal Auditors

Standard	Conform	Observations and actions proposed
Attribute Standards		
1100 Independence and Objectivity		
1110 Organisational Independence	Partially	It is the responsibility of the Section 151 Officer to ensure that the budget and resources allocated to internal audit are sufficient to ensure delivery of the plan; including the appointment and removal of the CAE and to report any concerns to the Audit Committee.
1111 Direct Interaction with the Board		
1120 Individual Objectivity		
1130 Impairment to Independence or Objectivity		
1210 Proficiency		<p>5.3.5 When fully staffed internal audit collectively possess the skills, knowledge and other competencies required to deliver. Recruitment is currently underway to fill vacancies. October 2021 Head of Audit</p> <p>5.3.8 Ongoing continuous development of IT skills across the audit team and move the type of audit review conducted by auditors to a more technical one to reflect digital transformation plans and to reflect new systems. March 2022 Principal Auditor (IT)</p> <p>5.3.9 Continue to embed the data analytics approach to appropriate audits March 2022 Principal Auditor</p>
1220 Due Professional Care		
1230 Continuing Professional Development		

Standard	Conform	Observations and actions proposed
1300 Quality Assurance and Improvement Programme		<p>5.4.1.1 Ongoing review of the Audit manual and the quality review processes to ensure complete compliance with the standards and suitable guidance for staff. March 2022 Head of Audit</p> <p>5.4.1.2 Complete this assessment and continue to report to Audit Committee annually along with a high-level improvement programme. June 2022 Principal Auditor</p>
1310 Requirements of the Quality Assurance and Improvement Programme		<p>5.4.5 Report to Audit Committee on selection of external assessor Sept 2021 Head of Audit</p>
1311 Internal Assessments		
1312 External Assessments		<p>5.4.18 Report to Audit Committee on selection of external assessor Sept 2021 Head of Audit</p>
1320 Reporting on the Quality Assurance and Improvement Programme		<p>5.4.23 Report to future Audit Committee on outcome of proposed external assessment Spring 2022 Head of Audit</p>
1321 Use of 'Conforms with the International Standards for the Professional Practice of Internal Auditing'		<p>5.4.25 Report outcome of this assessment to June Audit Committee on compliance with the standards and a resulting QIAP. June 2022 Head of Audit</p>
1322 Disclosure of Non-conformance		<p>5.4.26 Report outcome of self-assessment against PSIAS and the resulting external assessment. July 2022 Head of Audit</p>

Standard	Conform	Observations and actions proposed
2000 Managing the Internal Audit Activity		
2010 Planning		
2020 Communication and Approval		
2030 Resource Management		
2040 Policies and Procedures		6.1.25 Continue to review policies and procedures Ongoing Head of Audit
2050 Coordination		
2060 Reporting to Senior Management and the Board		6.1.30 Continue to ensure senior managers are informed of changes in the internal control environment. Quarterly throughout the year Head of Audit
2070 External Service Provider and Organisational Responsibility for Internal Auditing		
2110 Governance		
2120 Risk Management		6.2.6. Refresh risk assessments and look to place on Sharepoint site for updating and knowledge awareness Autumn 2021 Head of Audit Interim report on the Fraud pilot Nov 2021 Head of Audit
2130 Control		
2210 Engagement Objectives		
2220 Engagement Scope		
2230 Engagement Resource Allocation		

Standard	Conform	Observations and actions proposed
2240 Engagement Work Programme		
2300 Performing the Engagement		
2310 Identifying Information		
2320 Analysis and Evaluation		
2330 Documenting Information		
2340 Engagement Supervision		
2410 Criteria for Communicating		
2420 Quality of Communications		
2421 Errors and Omissions		
2430 Use of 'Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing'		
2431 Engagement Disclosure of Non-conformance		
2440 Disseminating Results		
2450 Overall Opinion		