

Report to Audit Committee

Review of the System of Internal Audit by the Audit Committee

Portfolio Holder: Audit Committee

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Ext. 4783

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Reason for Decision

To update Members of the Audit Committee, following the external and internal assessments of the system for Internal Audit within the Council, for the financial year 2017/18.

The external assessment was conducted by the Chartered Institute of Finance and Accountancy (CIPFA) in September 2017 and the internal assessment, conducted by the Head of Corporate Governance. It is based on a “Balanced Scorecard” approach scoring certain aspects of the overall Corporate Governance Service against specific criteria from the Public Sector Internal Audit Standards (PSIAS) using a Red, Amber/Red, Amber/Green and Green scoring system as agreed by the previous Audit Committee.

Executive Summary

The 2017/18 internal assessment of the Corporate Governance team (Internal Audit, Counter Fraud, Risk and Insurance) via the Balanced Scorecard Report concludes that the service is good. The assessment has concluded that the following criteria are assessed as Amber/Red and will require management attention in 2017/18 around the wider system of Internal Audit and Control:

- Scorecard 1.10: Internal Audit: This is assessed as Red and relates to the use of automated audit software. There have been some delays to the implementation of an appropriate cost effective solution. The team has worked with Business Intelligence and ICT colleagues to capture business requirements and market engagement has commenced to secure a cost effective solution, via the Council’s procurement process.

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- Scorecard 2.8: Corporate Initiatives and Monitoring: This relates to the criteria “Payroll System has adequate opinion”, which reflects the on-going challenges around improving the audit opinion on this Fundamental Financial System, which have been reported to this Committee elsewhere on the Agenda.

Some of the issues reported in the Balanced Scorecard are wider internal control issues rather than specific to the System of Internal Audit. However, it is proposed to keep this reporting methodology, as it represents a pragmatic way to provide an overview of the overall control environment of the Council supported by professional best practice.

The external assessment by CIPFA concluded that the Audit and Counter Fraud service operates in accordance with best practice.

Recommendation

The Audit Committee note the self-assessment of the Head of Corporate Governance that the overall system of Internal Audit has been fit for purpose in 2017/18.

Review of the System of Internal Audit by the Audit Committee

1 Background

- 1.1 The Accounts and Audit Regulations and Public Sector Internal Audit Standards clarify that the body charged with governance, which for Oldham Council is the Audit Committee, should undertake an annual review of the effectiveness of its system of Internal Audit.
- 1.2 In previous years, the Head of Corporate Governance has submitted this report to this Audit Committee based on the review of the Internal Audit services against criteria set out in the “Balanced Scorecard” methodology. The Head of Corporate Governance bases this internal assessment on the criteria set out in the Public Sector Internal Audit Standards (PSIAS).
- 1.3 In September 2017, an external independent inspection of the Internal Audit function was conducted by the Chartered Institute of Public Finance and Accountancy (CIPFA). This inspection is required by PSIAS every five years. The outcome of this review was reported to the Audit Committee on 11 January 2018.
- 1.4 Going forward, if the Committee wished to adopt an alternative internal assessment methodology, it would be required to do so by developing a new system. In the past, the Committee has set up a working group of Members to undertake this task. The next external assessment is due by 31 March 2023.
- 1.5 This report sets out the findings from the internal assessment by the Head of Corporate Governance and the external assessment by CIPFA.

2 Current Position – External Assessment

- 2.1 **Appendix 1** sets out the Final agreed report arising from the CIPFA External Review. In summary, the review concluded that the service “Generally Conforms” to the standards. In addition, the review reported that Internal Audit is a “well respected service, which follows best practice”.
- 2.2 The report contains four recommendations, which have been fully implemented by the Head of Corporate Governance. The changes relate to the Audit Charter, the Annual Report and the 2018/19 Audit and Counter Fraud Plan. These are:
 - Replace the section entitled “Role and Purpose of Internal Audit” in the Audit Charter with the “Mission of Internal Audit”.
 - Incorporate a statement to the Audit Charter to confirm whether the Service has sufficient resources to deliver an effective internal audit service to the Council.
 - Review the 2018/19 Audit Plan to incorporate audits of the risk management and annual governance statement processes.
 - Expand the Head of Corporate Governance’s annual opinion to include the risk management and governance arrangements.
- 2.3 The CIPFA review also identified some suggestions for change for the service to consider. These suggestions have also been agreed by the Head of Corporate Governance and they will also be implemented in 2018/19. The suggestions are:

- Evaluate the specialist computerised audit management systems that are available and obtain the one that best meets the current and future needs of the Service.
 - Expand the Audit Plan Report to set out how the overall internal audit service and specific types of audits will be delivered.
 - Evaluate the specialist data interrogation and analysis software applications that are available and obtain the one that best meets the needs of the service.
- 2.4 The 2017/18 Year End Report by the Head of Corporate Governance is being considered as part of another agenda item by this Audit Committee meeting and this sets out how the above actions, and suggestions, are being implemented. The report highlights that the review of cost effective alternatives for a replacement audit management software are underway and, in accordance with the Council's Contract Procedure Rules, market engagement has commenced. The opportunity to determine the options for the specialist data interrogation and analysis software applications available will be assessed as part of this review.

3. Current Position – Internal Assessment

- 3.1 **Appendix 2** details the internal assessment for 2017/18 by the Head of Corporate Governance, the conclusions of which are reported using the Balanced Scorecard.
- 3.2 The Balanced Scorecard has been developed to give this Committee the assurance on a number of matters that the service supervised by the Head of Corporate Governance is operating effectively.
- 3.3 The Team's performance against the following key criteria is:
- *Internal Audit (Scorecard Section 1)*: in line with the CIPFA external assessment, the performance of the system for Internal Audit is assessed as "green". The team has worked in professional collaboration with key service managers where additional support is required and has also provided proactive professional advice prior to system and processes changes. However, in line with the external assessment, action is required to resolve the on-going performance issues caused by the current Audit Management Software. Market engagement is underway at the time of writing this report.
 - *Corporate Initiatives and Monitoring (Scorecard Section 2)*: This is overall assessed as "amber/green", due to the requirement to improve controls in the Payroll system, and the need to update the Council's Financial Procedure Rules.
 - *Risk Management and Insurance (Scorecard Section 3)*: This is overall assessed as "green".
 - *Public Sector Internal Audit Standards (Scorecard Section 4)*: Overall the skills of the team are effective and have continued to develop in 2017/18. In line with the CIPFA assessment, the team operates in line with PSIAS but should review all documentation to ensure that the role of team is defined in line with the professional standards. However, the external assessment concluded the requirement to review the options for a replacement Audit Management System, which is also reported as "red" in the internal assessment.

4 Conclusions

- 4.1 Following the external independent inspection by CIPFA in September 2017 and the internal assessment by the Head of Corporate Governance, the overall system of Internal Audit remains good in 2017/18 and that firm plans are in place to continue this progress in 2018/19.

5 Options/Alternatives

- 5.1 The Audit Committee consider this report in conjunction with the 2017/18 Annual Report and the Annual Governance Statement.
- 5.2 The Audit Committee suggests an alternative internal assessment methodology.

6 Preferred Option

- 6.1 The preferred option is that the Audit Committee accepts and notes the Review of the System of Internal Audit.

7 Consultation

- 7.1 N/A.

8 Financial Implications

- 8.1 N/A.

9 Legal Services Comments

- 9.1 N/A.

10 Cooperative Agenda

- 10.1 N/A.

11 Human Resources Comments

- 11.1 N/A

12 Risk Assessments

- 12.1 Should the Audit Committee not consider a report reviewing the system of Internal Audit on an annual basis then it could be argued it has not complied with the Accounts and Audit Regulations (Mark Stenson)

13 IT Implications

- 13.1 N/A

14 Property Implications

- 14.1 N/A

- 15 **Procurement Implications**

15.1 N/A

16 **Environmental and Health & Safety Implications**

16.1 N/A

17 **Equality, community cohesion and crime implications**

17.1 N/A

18 **Equality Impact Assessment Completed?**

18.1 None

19 **Key Decision**

19.1 N/A

20 **Forward Plan Reference**

20.1 N/A

21 **Background Papers**

21.1 The following is a list of background papers on which this report is based in accordance with the requirements of Section 100(1) of the Local Government Act 1972. It does not include documents which would disclose exempt or confidential information as defined by the Act:

File Ref: Background papers are included in the Appendices
Officer Name: Mark Stenson
Contact No: 0161 770 4783

22 **Appendices**

22.1 The following Appendices are available to support this Report:

 - **Appendix 1:** CIPFA: External Quality Assessment - Validation of Client's Self-Assessment of Conformance to the Public Sector Internal Audit Standards, Oldham Metropolitan Borough Council's Internal Audit Service: Final Report, 24 October 2017.
 - **Appendix 2:** Oldham Council Corporate Governance Balanced Scorecard Summary 2017/18.

Appendix 1

This Appendix sets out the External Quality Assessment - Validation of Client's Self-Assessment of Conformance to the Public Sector Internal Audit Standards

Oldham Metropolitan Borough Council's Internal Audit Service

Final Report

External Quality Assessment - Validation of Client's Self-Assessment of Conformance to the Public Sector Internal Audit Standards

**Oldham Metropolitan Borough Council's
Internal Audit Service**

Final Report

Lead Associate: Ray Gard, CPFA, FCCA, CFIIA, DMS

**Internal QA: Technical Manager, CIPFA, Professional Standards &
Guidance**

24 October 2017

Self-Assessment Validation of Oldham Metropolitan Borough Council's Internal Audit Service – 4th and 5th September 2017

1. Introduction

Internal audit within the public sector in the United Kingdom is governed by the Public Sector Internal Audit Standards (PSIAS), which have been in place since 1st April 2013 (revised 2016 and 2017). Public sector internal audit services are required to measure how well they are conforming to the standards. This can be achieved through undertaking periodic self-assessments, external quality assessments, or a combination of both methods. However, an external reviewer must undertake a full assessment or validate the service's own self-assessment at least once in a five year period.

2. Background

Oldham Metropolitan Borough Council's (OMBC) Internal Audit Service is based at the Civic Centre in Oldham and currently provides internal audit services to Oldham Metropolitan Borough Council and the Greater Manchester Waste Disposal Authority. The Internal Audit and Counter Fraud Service comprises twelve staff in total at various levels (including the Head of Governance) and includes four qualified accountants and three part qualified accountants or technicians. Included in the twelve are two experienced counter-fraud specialists, and three 'individual budget' auditors.

The Service has been operating under PSIAS for over four years, so this was deemed a good time for their first external review against the standards and the local government application note (LAGN) produced by CIPFA.

3 Validation Process

The self-assessment validation comprises a combination of desktop and actual on-site review and cannot reasonably consider all elements of the PSIAS and LGAN self-assessment in the time available. The desktop period of the review focussed on determining the strengths and weaknesses of the Internal Audit Service, and formed the key lines of enquiry used during the on-site stage, in order that the review itself is risk-based, timely and adds real value to the organisation. The key lines of enquiry assessed the Service against the four broad themes of Purpose and Positioning; Structure and Resources; Audit Execution; and Impact.

The Service provided a comprehensive range of documents that they used as evidence to support their self-assessment and these were available for examination prior to and during this validation review. These documents included:-

- the self-assessment against the standards and the LGAN;
- the QAIP;
- the audit charter and audit strategy;
- Head of Internal Audit's annual report and opinion;
- audit plan and covering report to the Audit committee;
- audit manual;
- reports to the Audit committee;
- individual audit reports and working papers; and
- staff training and development records.

The on-site stage of the validation process involved interviews with the head of internal audit, the audit team, and a sample of key stakeholders, together with a review of a sample of audit reports and working papers. A questionnaire was also sent to the key stakeholders and the results analysed during the review.

4. Conclusion and Opinion

The Council has a professional and well-respected internal audit service that is effective and follows best practice. The validation process has not revealed any areas of non-compliance, or any significant areas of partial non-compliance, with the standards that the Service has not already identified during their self-assessment and included in their quality assurance and improvement plan (QAIP).

The validation process identified some minor areas of partial conformance with the standards, together with some recommendations (R) and suggestions (S) to rectify these. The process also identified some opportunities for the Service to enhance its operations, and we have made some suggestions (S) for the Service to consider. These are all set out in the tables at section 5 of this report, and the action plan at Appendix 1.

On this basis it is our opinion that the self-assessment is a good reflection of Internal Audit's practices and its contribution to the organisation, and as such the Service GENERALLY CONFORMS to the requirements of the Public Sector Internal Audit Standards and the Local Government Application Note.

The co-operation of the Head of Governance, the Audit and Counter Fraud manager, the members of the internal audit team in providing all of the information asked for, and those stakeholders that made themselves available for interview, was much appreciated.

Ray Gard, CPFA, FCCA, FCIIA, DMS

5. Summary of observations, recommendations and suggestions

Standard	Compliance	Observations	Recommendations and Suggestions	No
Mission of Internal Audit	Partially Conforms	<p>Minor Observation</p> <p>The audit charter sets out the role and purpose of the Internal Audit Service in three places but does not use the specific Mission Statement as set out in the Public Sector Internal Audit Standards (PSIAS).</p>	Replace one of the 'role and purpose of internal audit statements' in the Audit Charter with the Mission Statement from the PSIAS at the next revision	R1
Core principles of internal audit	Generally Conforms			
Code of Ethics	Generally Conforms			
Attribute Standards				
1000 Purpose, authority and responsibility	Generally Conforms			
1100 Independence and objectivity	Generally Conforms			
1200 Proficiency and due professional care	Generally Conforms	<p>Opportunity to Enhance Services</p> <p>There are opportunities for the Service to perform internal audits by expanding their use of computer assisted audit techniques (CAATs). At present this type of audit work is delivered</p>	Evaluate the specialist data interrogation and analysis software applications that are available and obtain the one that best meets the	S1

Standard	Compliance	Observations	Recommendations and Suggestions	No
		through an arrangement with Salford City Council, however the Service now has the appropriate skills to carry out this work in-house but has yet to obtain a suitable interrogation application to use. Obtaining such an application would not only enable the service to test a greater number of transactions within specific systems but will also enable the Service to redirect auditors to work on audits that are better performed through manual processes.	needs of the Service.	
1300 Quality assurance and improvement programme	Generally Conforms			
Performance Standards				
2000 Managing the internal audit activity	Generally Conforms	<p>Minor Observations</p> <p>The audit charter does not specifically mention whether the Head of Governance believes he has sufficient resources to deliver an effective internal audit service to the Council.</p> <p>The Service does not have a strategic statement on internal audit setting out how the overall service and specific types of audits will be delivered. This can be a separate stand alone document, or the statement can be incorporated into another document such as the audit charter or, more commonly, the audit plan report where more detail can be provided</p>	<p>Add a statement to the audit charter to confirm whether the Service has sufficient resources to deliver an effective internal audit service to the Council.</p> <p>Expand the audit plan report to set out how the overall internal audit service and specific types of audits will be delivered.</p>	R2 S2

Standard	Compliance	Observations	Recommendations and Suggestions	No
		on how the various types of audit will be delivered.		
2100 Nature of work	Generally Conforms	<p>Minor Observation</p> <p>Although risk management and governance are covered in the various audits undertaken, the Service has not undertaken specific audits on the overall risk management processes or the processes for producing the annual governance statement. These should be incorporated into the audit plan with sufficient safeguards in place as both activities come under the responsibility of the Head of Governance</p>	Include audits of the risk management and annual governance statement processes in future audit plans	R3
2200 Engagement planning	Generally Conforms			
2300 Performing the engagement	Generally Conforms	<p>Opportunity to Enhance Services</p> <p>The Service's current electronic audit management system (AMS) is now past its useful life and cannot cope with the volume or complexity of the audits. Consequently, the Service has reverted to manual processes to overcome the shortcomings, which although effective is not enabling the Service to make best use of their auditor resources.</p> <p>Approval has recently been given for the Service to obtain a replacement AMS and they now need to press on with exploring and evaluating the products that are on the market, including ensuring that any application obtained will meet the long term needs of the</p>	Evaluate the specialist computerised audit management systems that are available and obtain the one that best meets the current and future needs of the Service.	S3

Standard	Compliance	Observations	Recommendations and Suggestions	No
		Service.		
2400 Communicating the results	Generally Conforms	<p>Minor Observation</p> <p>The Head of Governance's annual report includes narrative on the processes that have been used to inform the audit opinion which include effectiveness of the system of internal controls, the risk management, and the governance arrangements.</p> <p>However, the actual opinion in the annual report only refers to the system of internal control and does not mention risk management or governance. This needs to be expanded to include the risk management and governance arrangements.</p>	Expand the Head of Governance's annual opinion to include the risk management and governance arrangements	R4
2500 Monitoring progress	Generally Conforms			
2600 Communicating the acceptance of risks	Generally Conforms			

Appendix 1: Action Plan

Recommendations

No	Recommendation	Response	Responsible Person	Action date
R1	Replace one of the 'role and purpose of internal audit statements' in the Audit Charter with the Mission Statement from the PSIAS at the next revision	Agreed – this will amendment will be made to the Internal Audit Charter and presented to the Council's Audit Committee for approval.	Head of Corporate Governance	30 th March 2018
R2	Add a statement to the audit charter to confirm whether the Service has sufficient resources to deliver an effective internal audit service to the Council.	Agreed – this will amendment will be made to the Internal Audit Charter and presented to the Council's Audit Committee for approval.	Head of Corporate Governance	30th March 2018
R3	Include audits of the risk management and annual governance statement processes in future audit plans.	Agreed – these will be fully considered during the preparation of the 2018/19 Audit and Counter Fraud Plan and suitable arrangements made to audit using a risk based approach.	Head of Corporate Governance	30 th March 2018 (plan approval). Audits to be delivered in accordance with agreed Plan.
R4	Expand the Head of Governance's annual opinion to include the risk management and governance arrangements.	Agreed – the 2017/19 Annual Opinion will set out the opinion for these criteria and will be presented to the Council's Audit Committee for approval.	Head of Corporate Governance	30th May 2018

Suggestions

No	Suggestion	Response	Responsible Person	Action date
S1	Evaluate the specialist data interrogation and analysis software application that are available and obtain the one that best meets the needs of the Service.	Agreed. This will commence with an options appraisal for review by the Head of Corporate Governance; and it will ensure that any solutions are considered as part of the development of requirements for the implementation of the new Audit Management System	Audit and Counter Fraud Manager	24 th December 2017
S2	Expand the audit plan report to set out how the overall internal audit service and specific types of audits will be delivered.	Agreed. This will clearly set out in the 2018/19 Audit and Counter Fraud Plan.	Head of Corporate Governance	30 th May 2018
S3	Evaluate the specialist computerised audit management systems that are available and obtain the one that best meets the current and future needs of the Service.	Agreed. The IT Project Manager has been assigned to the project and technical requirements will be finalised by 30 th September 2017 for implementation by 1 st April 2018.	Audit and Counter Fraud Manager	31 st March 2018

Appendix 2: Interviewees and Questionnaires

Person	Position	Organisation
Interviewees		
Mark Stenson	Head of Governance	Oldham Metropolitan Borough Council
Jane Whyatt	Audit and Counter Fraud Manager	Oldham Metropolitan Borough Council
Anne Ryans	Director of Finance & S151 Officer	Oldham Metropolitan Borough Council
Ray Ward	Executive Director of Corporate and Commercial Services	Oldham Metropolitan Borough Council
Clr Javid Iqbar	Audit Committee Member and Past Chair	Oldham Metropolitan Borough Council
Audit Team Members	Assistance Managers, Senior Auditors, Auditors, Counter Fraud Investigator, IB Auditors	Oldham Metropolitan Borough Council
Cathy Butterworth	Assistant Director of People	Oldham Metropolitan Borough Council
Questionnaires		
Carolyn Wilkins	Chief Executive	Oldham Metropolitan Borough Council
Colin Brittain	Assistant Borough Solicitor	Oldham Metropolitan Borough Council
Mark Warren	Director of Adults	Oldham Metropolitan Borough Council
Neil Consterdine	Head of Service – Public Health and leisure	Oldham Metropolitan Borough Council

Appendix 2

Oldham Council Corporate Governance: 2017/18 Internal Assessment

Oldham Corporate Governance Scorecard Summary 2017-18					
Internal Audit	Risk	Components	Corporate Initiatives and Monitoring	Risk	Components
1.1 Compliance with 2013 Public Sector Internal Audit Standards		G	2.1 Corporate Governance Framework incl Annual Governance Statement		G
1.2 Work on Fundamental Financial Systems		G	2.2 External Audit Fees		G
1.3 Reporting to Audit Committee of Internal Control Matters		G	2.3 Counter Fraud Policy Framework		G
1.4 Completion of the 2015/16 Internal Audit Plan		G	2.4 Project Risk Monitoring		G
1.5 Detailed undertaking and reporting of internal audit work		G	2.5 Corporate Risk Management Approach		G
1.6 Relationship with External Audit		G	2.6 Partnership Governance Monitoring		G
1.7 Internal Audit Planning Process		G	2.7 Finance Procedure Rules fit for purpose		AG
1.8 Liaison with Directorates		A/G	2.8 Payroll System adequate controls		R
1.9 Findings from the work		G	2.9 Compliance within Council on Procedure Rules		A/G
1.10 Use of Automated Software		R	2.10 Overall Control environment of Council		A/G
Risk Management/Insurance	Risk	Components	Counter Fraud and Staffing Issues	Risk	Components
3.1 Level of Insurance Claims in Council		G	4.1 Level of Fraud Within Council		G
3.2 Achievement of Insurance Savings		G	4.2 Transparency Agenda		AG
3.3 Insurance incl Renewals Arranged		G	4.3 Counter Fraud Strategy		G
3.4 MMI		G	4.4 Systems to prevent fraud in 2017/18		G
3.5 Development of Financial Information on Insurance		G	4.5 NFI		AG
3.6 Risk Management Strategy		G	4.6 Develop training on Internal Control and Risk of Fraud		AG
3.7 Fraud Prevention on Insurance		G	4.7 Staffing Issues		G
3.8 Success at Litigation		G	4.8 Mid Year Performance Appraisals		G
3.9 Member involvement on Insurance/Risk Management		G	4.9 Equal Opps & Other HR indicators		G
Key to ratings					
R	Red - Highly problematic - requires urgent and decisive action.				
A/R	Amber/Red - Problematic - requires substantial attention, some aspects need urgent attention				
A/G	Amber/Green - Mixed - aspect(s) require substantial attention, some good				
G	Good – on target, or target already achieved				
W	Objectives where measures not yet agreed				
P	Work in progress, no assessment available.				