



**The Head of Internal Audit Service's Annual Opinion
on the overall adequacy and effectiveness
of ESPO's control environment
2019-20**

**Neil Jones CPFA, Head of Internal Audit Service,
Leicestershire County Council**

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Background

During the financial year 2019-20, Leicestershire County Council Internal Audit Service (LCCIAS) provided internal audit activity to the Eastern Shires Purchasing Organisation (ESPO). LCCIAS conforms to the Public Sector Internal Audit Standards (the PSIAS) revised with effect from April 2017. The PSIAS require the Head of Internal Audit Service (HoIAS) to give an annual opinion on the overall adequacy and effectiveness of ESPO's control environment i.e. its framework of governance, risk management and control. The PSIAS definitions of the types of audits undertaken and of the control environment are to be found at the end of this document, along with further explanation from the Institute of Internal Auditors about what an effective system of internal control facilitates.

The HoIAS annual opinion is for a specific time interval i.e. 2019-20 and combines: -

- an objective assessment based on the results of individual audits undertaken and actions taken by management thereafter. Individual audit opinions on what level of assurance can be given as to whether risk is being identified and adequately managed, are formed by applying systematic grading to remove any elements of subjectivity. An explanation of the ratings applied is also to be found in the definitions at the end of this document. The results of audits undertaken during 2019-20 are reported in **Annex 2**
- the professional judgement of the HoIAS based on his evaluation of other related activities e.g. attendance at Committees.
- Specifically for 2019-20, the HoIAS' views on ESPO management's responses to the coronavirus during the months of February and March 2020.

The results of the above, when combined, form the basis for the overall opinion on ESPO's control environment. Individual audits are assigned a rating because it is possible to gather and test evidence for a specific audit topic. The overall opinion reflects that it isn't possible to provide audit coverage over all systems and processes. The caveat at the very end of this document explains what internal control cannot do. i.e., no system of internal control can provide absolute assurance against material misstatement or loss, nor can LCCIAS give absolute assurance, especially given its limited resource. The work of LCCIAS is intended only to provide assurance on the adequacy of the control environment based on the work undertaken and known facts.

Governance related internal audit work

An opinion on whether good governance principles have been applied is based on the results of an audit of Annual Governance Statement compilation and observation of the project governance arrangements for the new website development.

The HoIAS and the designated Audit Manager attend the Finance and Audit Subcommittee and appropriate Management Committee meetings to present audit plans and reports, which enables him to gauge ESPO Member governance at first hand.

The HoIAS and the Audit Manager have regular discussions with the ESPO Director and the Leadership Team, the Consortium Treasurer, and where required the Consortium Secretary, on governance issues and related aspects of audits.

The HoIAS is part of a group comprising the ESPO Director, the Assistant Director Finance, the Consortium Treasurer, and Consortium Secretary which review the content of the draft Annual Governance Statement.

Risk management related internal audit work

Most audits planned and conducted were 'risk based' i.e. ensuring that ESPO management identifies, evaluates and manages risk to achieving its objectives i.e. ensuring controls are in place to reduce risk exposure.

Audits of the limited company risk evaluation, counter fraud, supply chain management, business growth, IT developments and health and safety, returned positive assurances.

The HoIAS monitors members engagement with ESPO's risk registers through Management Committee meetings.

Financial (and ICT) Controls related internal audit work

Several financial system audits were undertaken including those of ESPO's IT and general financial systems controls, Supply Chain and Operations Productivity Plan and the catalogue pricing routine. Findings did not suggest any fundamental weakness.

For the National Fraud Initiative exercise no instances of fraudulent activity were noted.

Two financial controls related audits (rebates income and servicing authority responsibilities) could not be completed because they would have required site visits and this was not possible with the immediate impact on workplaces of the covid-19 virus and as such opinions on the audits haven't been reached.

Planning for and managing the impact of the coronavirus

It is the HoIAS' opinion that the Director of ESPO demonstrated good governance and risk management when he first outlined plans for identifying risks and managing the impact of the coronavirus to Management Committee on 4 March 2020 and added a risk to the ESPO Corporate Risk Register. There were further updates informing Management Committee of plans and actions towards the end of March. However, the speed of escalation and lockdown instructions required ESPO management to very quickly design and install alternative ways of working with its financial and ICT systems which could have internal control and risk implications for the overall control environment. These were reported in summary to Chief Officers Group on 29 April. We will review the arrangements to ensure alternative methods retain robust controls.

Planning for and responding to the virus crisis, planning recovery, lessons learned, and future impacts are likely to be reflected in the Annual Governance Statement.

HolIAS opinion

Prior to the onset of the coronavirus, ESPO's control environment was in a steady state. The build-up and immediate impact of the virus was significant, adverse in nature and unique in character. However, no significant governance, risk management internal control failings have come to the HoIAS' attention therefore substantial assurance is given that ESPO's control environment overall has remained adequate and effective.

15th June 2020

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Definitions

The revised 2017 Public Sector Internal Audit Standards (the PSIAS) define the following: -

Assurance audit

An objective examination of evidence for the purpose of providing an independent assessment on governance, risk management and control processes for the organisation. Examples may include financial, performance, compliance, system security and due diligence engagements.

Assurance audits have four gradings: -

Outcome of the audit

Assurance rating

No (or only a few minor) recommendations

Full assurance

A number of recommendations made but none considered to have sufficient significance to be denoted as **HI** (high importance)

Substantial assurance

Includes at least one **HI** recommendation, denoting that (based upon a combination of probability and impact) a significant weakness either exists or potentially could arise and therefore the system's objectives are seriously compromised. Management should quickly address **HI** recommendations and implement an agreed action plan without delay.

Partial assurance

Alternatively, whilst individually none of the recommendations scored a HI rating, collectively they indicate that the level of risk to is sufficient to emphasise that prompt management action is required.

The number and content of the **HI** recommendations made are sufficient to seriously undermine any confidence in the controls that are currently operating.

Little or no assurance

Consulting audit

Advisory and related client service activities, the nature and scope of which are agreed with the client, are intended to add value and improve an organisation's governance, risk management and control processes without the internal auditor assuming management responsibility. Examples include counsel, advice, facilitation and training.

Control

Any action taken by management, the board and other parties to manage risk and increase the likelihood that established objectives and goals will be achieved.

Management plans, organises and directs the performance of sufficient actions to provide reasonable assurance that objectives and goals will be achieved.

Control Environment

The attitude and actions of the board and management regarding the importance of control within the organisation. The control environment provides the discipline and structure for the achievement of the primary objectives of the system of internal control.

The control environment includes the following elements: -

- Integrity and ethical values
- Management's philosophy and operating style
- Organisational structure.
- Assignment of authority and responsibility.
- Human resource policies and practices.
- Competence of personnel.

The Institute of Internal Auditors further explains that the control environment is the foundation on which an effective system of internal control is built and operated in an organisation that strives to achieve its strategic objectives, provide reliable financial reporting to internal and external stakeholders, operate its business efficiently and effectively, comply with all applicable laws and regulations, and safeguard its assets.

Caveat

The Financial Reporting Council in an Auditing Practices Board briefing paper, 'Providing Assurance on the Effectiveness of Internal Control' explains what internal control cannot do, namely: -

'A sound system of internal control reduces, but cannot eliminate, the possibility of poor judgement in decision making, human error, control processes being deliberately circumvented by employees or others, management overriding controls and the occurrence of unforeseen circumstances. A sound system of internal control therefore provides reasonable, but not absolute assurance that an organisation will not be hindered in achieving its objectives, or in the orderly and legitimate conduct of its business, by circumstances which may reasonably be foreseen. A system of internal control cannot, however, provide protection with certainty against an organisation failing to meet its objectives, or all material errors, losses, fraud or breaches of laws and regulations'.

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