

CORPORATE GOVERNANCE COMMITTEE – 26 NOVEMBER 2012**REPORT OF THE DIRECTOR OF CORPORATE RESOURCES****ANNUAL REVIEW OF THE EFFECTIVENESS OF THE SYSTEM
OF INTERNAL AUDIT****Purpose of report**

1. The purpose of this report is to demonstrate the effectiveness of the system of internal audit in the County Council. This is in compliance with the Accounts and Audit (England) Regulations 2011 (the Regulations) which require the County Council to conduct an annual review of the effectiveness of its internal audit and for the Corporate Governance Committee to review its findings. This review must be considered as part of the system of internal control and informs the Annual Governance Statement.

Background

2. Part 2 of the Regulations relate to financial management and internal control and for the purposes of the Regulations, the County Council is designated a 'larger' relevant body.
3. Under Regulation 6(1) ('Internal audit'), "A relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control, in accordance with the proper practices in relation to internal control." The system of internal audit should therefore be viewed as one component of the wider issue of the County Council's internal control arrangements.
4. In addition to the above, Regulation 6(3) states that "A 'larger' relevant body must, at least once in each year, conduct a review of the effectiveness of its internal audit." This requirement is linked to the relevant body's responsibility for financial management contained in Regulation 4, which also requires a relevant body to review, at least once a year, the effectiveness of its system of internal control and to approve an annual governance statement.

5. Regulation 6(4) requires for the findings of the review on the effectiveness of the system of internal audit to be considered by members, meeting as a whole or as a committee, as part of its wider consideration of the system of internal control required under Regulation 4. In Leicestershire County Council, this responsibility falls within the remit of the Corporate Governance Committee.
6. As reported in the 2011/12 Annual Governance Statement, the annual review into the effectiveness of the system of internal audit planned to be reported in November 2011 was deferred, due to the service undergoing changes to both its service delivery approach and the pending implementation of new mandatory standards, (the Public Sector Internal Auditing Standards (PSIAS) detailed below).

Review of the Effectiveness of the System of Internal Audit

7. There is no prescriptive guidance to conducting an effectiveness review. There are a multitude of approaches and organisations are offered an opportunity to find their own solutions in order to meet the requirements of the Regulations. Nevertheless, guidance accompanying the Accounts and Audit Regulations 2003 (which over time have become the 2011 Regulations), offered that proper practices in relation to internal audit activities for principal authorities may be found in the 'Code of Practice for Internal Audit in Local Government in the United Kingdom' (the Code), issued by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Code was last updated and reissued in 2006.
8. A self assessment of compliance against the Code is a major part of the evidence used by the Head of Internal Audit Service (HoIAS) to evaluate the effectiveness of the system of internal audit. The most recent self assessment is shown in Appendix 1 and it confirms that overall, the Council continues to undertake an effective internal audit function and internal audit continues to be an effective part of the internal control process.
9. There are a small number of areas where the internal audit function is (at times or to varying degrees) not currently either fully or substantially complying with the Code. Any areas where there is currently 'partial' compliance will be improved, both through the implementation of process and structure changes following the service review, and the adoption of, and conformance to, the aforementioned mandatory PSIAS being introduced from April 2013. Should Members wish to discuss these further the HoIAS would be willing to give further explanation.
10. It is considered that the Code self assessment sheet (Appendix 1) provides Members with a useful means of supplementing their knowledge of the system of internal audit and will assist them in taking a view on its effectiveness.

Public Sector Internal Audit Standards

11. UK public sector organisations are currently covered by different internal audit standards. In the central government and health (NHS) sectors, the standards are based on those issued by the Institute of Internal Auditors (IIA). Other sectors, such as higher education and charity, apply the IIA Standards directly. The local government sector uses the aforementioned CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 (the Code).
12. As organisations work more closely together in formal partnerships and by other informal arrangements, and internal auditors work across the public sector, the following weaknesses in the current situation have become apparent:
 - A lack of consistency across the UK public sector and inconsistent up to date processes for the standards in use;
 - Different guidance for different, but related, sectors;
 - No structure to articulate public sector needs and influence best practice development.
13. A collaboration to develop the internal auditing profession was announced by CIPFA and the IIA in May 2011 and this has led to an agreement between the Relevant Internal Audit Standard Setters¹ to develop a set of internal audit standards. These will be applicable to all areas of the UK public sector and based on the mandatory elements of the Institute of Internal Auditors (IIA) and the International Professional Practices Framework (IPPF). The new standards will be known as ‘the Public Sector Internal Audit Standards’ (PSIAS) and should come into force from 1 April 2013 for all sectors. They will provide a:
 - Coherent and consistent public sector internal audit framework;
 - Coordinated update process; and
 - Public sector voice in IIA standard setting.
14. It is evident that the PSIAS further strengthen the roles and responsibilities of internal audit within governance forums. Adoption of, and compliance with the PSIAS will affect how the HoIAS reports to the Corporate Governance Committee and how effectiveness is proved. For example, the HoIAS will have to develop and maintain a quality assurance and improvement programme to enable the Service to be measured against PSIAS, and to include that external assessments must be undertaken at least once every five years.

¹ The PSIAS - The Relevant Internal Audit Standard Setters are: - HM Treasury in respect of central government; - the Scottish Government, the Department of Finance and Personnel Northern Ireland and the Welsh Government in respect of central government and the health sector in their administrations; - the Department of Health in respect of the health sector in England (excluding Foundation Trusts); - the Chartered Institute of Public Finance and Accountancy in respect of local government across the UK.

15. Detail on the PSIAS, the effects it will have on the system of internal audit and the role and responsibilities of this Committee will be reported to the February meeting.

Resource Implications

16. There are no resource implications arising from this report.

Equal Opportunities Implications

17. There are no resource implications arising from this report.

Recommendation

18. That the Committee notes the contents of this report and uses it as information to assist it in reviewing the effectiveness of the system of internal audit.

Background Papers

Accounts and Audit (England) Regulations 2011
Guidance on the Accounts and Audit Regulations 2003 – issued by Dept for Communities and Local Government 18th August 2006
The CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006
The Constitution of Leicestershire County Council
The Internal Audit Service Statement of Aims and Objectives Revised 2010
The Annual Governance Statement 2011/12

Circulation under Sensitive Issues Procedure

None

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Appendices

- Appendix - HoIAS self assessment of compliance with the CIPFA Code of Practice: November 2012