

Leicestershire County Council Internal Audit Service Annual Report 2013-14



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Statutory requirement for an internal audit function

The Chief Financial Officer is responsible for arranging a continuous internal audit

Leicestershire County Council's (LCC) Constitution (Financial Procedure Rule 2) states that the Chief Financial Officer (CFO) is responsible for the proper administration of the County Council's financial affairs under the requirements of Section 151 of the Local Government Act 1972 and Section 114 of the Local Government Finance Act 1988.

The Accounts and Audit Regulations (England) 2011 state that a relevant body (such as LCC) 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.

Financial Procedure Rule 15 states responsibility for arranging a continuous internal audit of LCC's financial management arrangements will be delegated to the CFO.

Leicestershire County Council Internal Audit Service provides the continuous audit

During 2013-14 Leicestershire County Council's Internal Audit Service (LCCIAS) led by the Head of Internal Audit Service (HoIAS), provided internal audit for LCC, the Pension Fund and Bradgate Park Trust. LCCIAS adopted the principles of the Public Sector Internal Audit Standards 2013 (the PSIAS). LCCIAS works closely with the external auditor PricewaterhouseCoopers (PwC) to minimise duplication.

Internal Audit Standards and their application to Local Government

New internal audit standards since 2013

The Public Sector Internal Audit Standards (PSIAS – the Standards) were introduced in 2013. The PSIAS and the Local Government Application Note (the Application Note) together supersede the 2006 CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom (the 2006 Code). The Application Note has been developed as the sector specific requirements for local government organisations.

Specific requirements for an annual report with mandatory inclusions

The Standards require the HoIAS to provide an annual report to the board timed to support the annual governance statement. This must include: -

- an annual internal audit opinion on the overall adequacy and effectiveness of the organisation's governance, risk and control framework (i.e. the control environment)
- a summary of the audit work from which the opinion is derived
- a statement on conformance with the PSIAS and the results of the internal audit Quality Assurance and Improvement Programme (QAIP).

Approach to internal audit work

Responsibility in respect of the control environment

It is the Corporate Management Team's (CMT) responsibility to design, install and operate adequate arrangements for governance, risk management and control within appropriate constitutional frameworks; and to identify, assess and manage risks that are significant to the achievement of LCC's objectives.

The Internal Audit Service's task is to carry out independent and objective 'assurance' type audits of the adequacy and effectiveness of how risks are managed including controls and, if necessary, highlight weaknesses and recommend improvements.

'Consulting' type audits add value by allowing the auditor to give early commentary on management's planned design of controls in say a new system or process.

Standards require risk based plans

The Standards state that the HoIAS must establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organisation's goals. The risk-based plan must take into account the requirement to produce an annual internal audit opinion

How LCCIAS plans its work

Much internal audit work can be planned. To this end an annual plan is produced, detailing the main areas of proposed work. The plan for 2013-14 was produced from a combination of: -

- Consultation about emerging risks, planned changes and potential problems with senior management across departments
- Evaluation of governance arrangements e.g. plans, risk registers and governance statements,
- Comparisons and 'horizon scanning' new and emerging risks affecting similar organisations

A continuing improvement in LCC's risk management (based upon specific audits of the risk management framework) and governance arrangements, allowed the HoIAS to utilise the information above, to mostly form the 2013-14 plan.

Risk based auditing

LCCIAS uses a number of techniques to reach its opinions on what level of assurance can be provided that risks are being identified, evaluated and managed. Much work will be based around a "risk based" audit. With this technique key risks (based on likelihood and impact) are identified and agreed at the start of the audit. The quality and application of controls established to mitigate the risks is then tested

“Joint audit” work with PwC	Part of the plan requires that LCCIAS conducts annual audits on key elements of the general ledger and IT systems. These audits are undertaken in consultation with LCC's External Auditors (PWC) to assist in their responsibility to form an opinion that LCC's financial accounts are not materially misstated. PWC determines that the quality and scope of LCCIAS work is sufficient to contribute positively to LCC's overall control environment and to allow them to place reliance on LCCIAS work.
Maintained schools and other site visits	Whilst a high proportion of Leicestershire schools have converted to Academy status, LCCIAS continues to audit remaining 'maintained' schools, children's care homes and children and family centres on a cyclical basis.
Investigations	Occasionally LCCIAS is commissioned to investigate suspected theft and fraud or specific problems that require an independent objective viewpoint.
Advisory	Quite often LCCIAS is asked to provide ad-hoc advice on governance, risk and internal financial control matters. Occasionally these are escalated to more formal 'consulting' engagements.
The number and type of recommendations form the 'opinion'	Internal Audit Service reports may contain recommendations for improvements. The number, type and importance of recommendations affects how the auditor reaches an opinion on the level of assurance that can be given that controls are suitably designed and applied effectively, and that material risks will likely not arise. The combined sum of individual audit opinions and other assurances gained, allows the HoIAS to form the annual internal audit opinion on the overall adequacy and effectiveness of the Council's governance, risk and control framework (i.e. the control environment).
High importance (HI) recommendations	<p>Following audit testing, if (using LCC methodology) risk is considered to remain significant (i.e. controls are poorly designed or are not being applied as planned), then recommendations are designated as High Importance (HI). Action taken to implement the HI recommendation is always re-tested by LCCIAS before being 'signed off' by the HoIAS.</p> <p>8 new HI recommendations were made in relation to 2013-14 audits. This was a slight increase on the previous year, but it was also noticeable that allowing extensions to originally agreed implementation dates is more prevalent.</p>
LCC member involvement	The Corporate Governance Committee receives audit reports i.e. annual plan, quarterly progress against the plan (including progress against implementing HI recommendations) and the annual report (including the HoIAS opinion).

Corporate functions	The HoIAS attends Corporate Governance Committee, various management teams, supplies performance data for corporate governance dashboards and acts as co-ordinator for both the Audit Commission's annual Fraud and Corruption Survey and the bi-annual National Fraud Initiative, an extensive biennial data matching exercise.
National Fraud Initiative	Payments to members' have to be included in the bi-annual submission of data to the Audit Commission.
Non audit duties	On rare occasions, LCCIAS may provide resource to assist with urgent operational requirements. Examples are validating the accuracy and completeness of outputs through a newly established payables system. Wherever this occurs, the auditors involved would be excluded from auditing that particular part of the system for at least one year, to retain the principles of independence and objectivity.

Head of Internal Audit Service Annual Opinion

Issue relating to payments to providers system	<p>During 2013-14 there was an issue with a system relating to payments to providers.</p> <p>The issue was caused by changes to staffing 'hierarchies' after service reviews not being reflected in the payables system. When automatic approval of invoices went live, the 'mismatches' meant messages asking for approvals were directed to the wrong persons and/or 'stacked up' thereby delaying payments.</p> <p>The issue was quickly identified and immediately addressed. Good governance and transparency was displayed in that management promptly brought the issue to the HoIAS attention and actively sought LCCIAS involvement in both 'approving' plans for the immediate workaround solutions (involving resources independent to the 'business' areas where the problems had occurred) and reviewing and testing the implementation of additional controls to avoid repetitions. LCCIAS 'walk-through' tests proved satisfactory and further audits will occur in 2014-15.</p>
Small increase in the number of HI recommendations indicating pressures and strains	Over the year, there was a small increase in the number of key risk audits that returned only 'partial' assurance ratings. This applied to governance, risk management and internal control functions. This is most likely an indicator of the increasing pressures and strains on staff, processes and systems during a time of unprecedented change, since all but one of the audits were in areas of new development or transition and hence controls and practices hadn't fully bedded down. Whilst management without failure accepted the need for remedial action, there has been slippage in implementing some 'high importance' recommendations.

There will be a need to monitor improvements to these areas as they move to 'business as usual', so that they do not slip off the radar behind further transformation. Nevertheless, the governance and level of attention paid by members and management to such issues is a comfort.

HolAS opinion on the overall adequacy and effectiveness of the organisation's governance, risk and control framework (i.e. the control environment)

Taking the above into consideration, based on the evidence of audits completed and other relevant work undertaken (appendix 3) and the HolAS observations of governance and risk management processes, on the whole reasonable assurance can be given that the Council's control environment is sound and that governance, risk and control frameworks are adequate and effective.

Summary of work undertaken 2013-14

Work undertaken in 2013-14

Work undertaken during 2013-14 is contained in appendix 3. Audits incomplete at 31st March show the opinion given at final report stage in 2014-15.

Conformance with the PSIAS

PSIAS requirement to report conformance (or disclose non-conformance)

There is a requirement for the annual report to contain a statement by the HolAS of conformance (or a disclosure of non-conformance) with the Standards.

Self-assessment revealed conformance with 'Performance' Standards

The HolAS has undertaken a self-assessment and evaluation of the internal audit activity, and the results (including areas for improvement) have been shared with the Chief Financial Officer (CFO). The exercise has revealed that on the whole the 'Performance' Standards (managing the activity; nature of work; planning and performing engagements; communicating results and monitoring progress) are being met.

However, two specific parts of the 'Attribute' Standards are not yet in place

However, within the 'Attribute' Standards there are two specific requirements that must be in place before the HolAS can formally state that LCCIAS, 'Conforms with the International Standards for the Professional Practice of Internal Auditing'. These are the development and approval by this Committee of both: -

- an internal audit Charter which mandates the purpose, authority and responsibility of the County Council's internal audit activity
- a Quality Assurance and Improvement Programme (QAIP) which formalises the evaluation of the internal audit activity's conformance with the Standards. The QAIP also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement

Neither of the documents above is yet in place.

**Current ‘alternatives’
to a Charter and QAIP**

Regarding the implementation of an Audit Charter, LCCIAS has a ‘Statement of Aims and Objectives’ and ‘Audit Strategy’ (both last updated and reported to this Committee in November 2010). Whilst the documents are not too dissimilar to what is required in a Charter, they do not contain all of the requirements of the 2013 Standards, and do not include recently inherited responsibilities for administering the Authority’s risk management framework and the Annual Governance Statement. Regarding the QAIP, whilst LCCIAS has always and continues to undertake quality reviews, evaluate effectiveness and seek continuous improvement, once again these are not formalised into a QAIP.

**Disclosing non-
conformance**

As such, the lack of a formal Charter and QAIP are to be reported as ‘non-conformance with the PSIAS’. The disclosures of ‘non-conformance’ are not considered a significant deviation from the PSIAS. For the time being the HoIAS is stating that ‘LCCIAS is abiding by the principles of the PSIAS’.

**Recorded as a key
improvement area in
the AGS**

The HoIAS has reported the non-conformance in the ‘weaknesses/areas for improvement’ column of Principle B of the Annual Governance Statement and within both Section 5 ‘The Effectiveness of the Internal Audit Service’ and Section 6 ‘Key Improvement Areas 2014/15’. The CFO has tasked the HoIAS to develop and implement both a Charter and QAIP by the end of December.

Person to Contact about this Report

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