

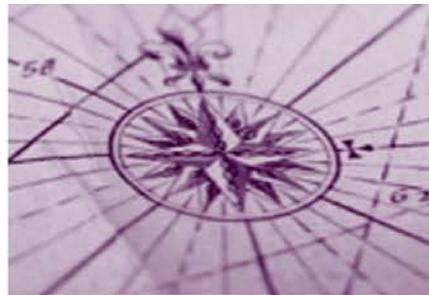


Broxbourne, Epping Forest and Harlow District  
Councils

**Internal Audit Shared Service**

**External Quality Assessment**

**November 2016**



## Purpose of assignment

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The Internal Audit service for the Local Authorities of Broxbourne, Epping Forest and Harlow District Councils is provided by a shared service arrangement which under the leadership of Sarah Marsh as Chief Internal Auditor (CIA); the team have responded to the Public Sector Internal Audit Standards and have increasingly worked to a common methodology for delivery of internal audit services. Performance against the standard has been self assessed on an annual basis and appropriate reports provided to member authority committee meetings.

The purpose of this review is to provide an external and independent quality review in accordance with standard 1312. We see this as not merely a compliance exercise and have also highlighted aspects of the service that we regard as best practice as well as summarised our thoughts as to where further development can be made to enhance the value of the service being provided.

The teams have significant experience, with a range of relevant qualifications and it has been recognised that there is a need to ensure a consistent approach to delivering assurance, as this is beneficial regarding communication with clients, working practices, reporting and therefore associated supervision and training needs. At a corporate level, this is established through the presence of an Internal Audit Charter which effectively defines the standards to which the shared service will carry out its work and is supported by a framework of standard templates and accepted processes to which the internal audit team work consistently.

The report reflects our opinion regarding the services currently provided measured against the Public Sector Internal Audit Standards (PSIAS), which we trust will be of benefit to individual staff, the team and the local authorities serviced by the Internal Audit Shared Service. Our observations and recommendations have been summarised within categories relating to the Resources, Competency, and Delivery and the team graded as being at one of three stages within each category, grades are related to our opinion as to whether the service is developing, established or excelling.

The outcome has been benchmarked against other provision in both the sector and the wider industry which shows that the team compares favourably with regard to its peers.

The internal audit shared service has responded to the merger of the three teams in recent years and has moved towards a common approach that is consistent with the PSIAS.

The significant change within the PSIAS reflects the focus on a requirement to implement a risk based internal audit approach to all aspects of internal audit work – significantly in relation to planning at a strategic and assignment level as well as in reporting. The shared service does adopt a risk based approach through the development of its own risk assessment at a strategic planning level, at an assignment level through recognition of risk register content and in testing schedules although further development would be beneficial both in terms of recognising inherent risk and in terms of reflecting wider sector risk experience of the internal audit team within Audit Planning documents and Terms of Reference.

All three authorities with which the Shared Service is involved have developing risk management strategies and associated frameworks; as a consequence, it would be beneficial for internal audit to increasingly align its processes with those of the host authority as this would promote effective communication, structure audit work on ‘what really matters’ and use risk as the basis for reporting. In this respect we have recommended that future opinions and recommendations relate directly to established risk definitions within each authority.

Increasing transparency within the Council systems regarding the inherent risks being faced and upon those assurances available would allow internal audit to clearly define risks and key mitigating controls and therefore provide a robust basis for communication with managers and with other assurance providers, although different perceptions of risk appetite exist within the Councils involved.

The internal audit shared service has benefitted from a period of stability during which staff have remained consistent, and therefore a robust internal audit standard has been maintained and delivered using an experienced team. This has allowed the **service** to demonstrate compliance with the PSIAS.

Nevertheless with increasing pressures on Council budgets, significant change to service delivery and as a result increasing risk; there is a need for the division to continue to enhance its delivery through greater awareness of the relevance of risk to both the Council and its own approach, in order to ensure that it focuses on the most appropriate areas and as a result demonstrates that it provides a service that effectively contributes towards the achievement of each Councils objectives.

## Compliance with PSIAS

- **Resources**

Business Vision and Mission, Governance arrangements, Recognition of standards, Guidance, Procedures and Supervision, Terms of Engagement, Ethics and business conduct.

- **Competency**

Charter, Internal Audit Manual, Planning and Allocation of staffing, Recruitment (Numbers and skills), Training (Professional and Technical), Appraisal and Development

- **Delivery**

Client engagement and relationship, Directed led service, Terms of Engagement (Audit/Assignment Brief), Discussion of assurance and advisory opinions, Reporting at assignment and strategic levels

# Grading of recommendations

- The grading of recommendations is intended to reflect the relative importance to the relevant standard within the Public Sector Internal Audit Standards (PSIAS).

Recommendation grading	Explanation
Enhance	The internal audit shared service must enhance its practice in order to demonstrate transparent alignment with the relevant PSIAS in order to demonstrate a contribution to the achievement of the organisations objectives in relation to risk management, governance and control.
Review	The Internal audit division should review its approach in this area to better reflect the application of the PSIAS.
Consider	The internal audit division should consider whether revision of its approach merits attention in order to improve the efficiency and effectiveness of the delivery of services

- In grading our recommendations, we have considered the wider environment within the Council in terms of both the degree of transformation that is currently taking place as well as our assessment of the level of risk maturity that currently exists as these will have a consequence for the conduct of internal audit planning as well as subsequent communication.

# Summary of good practice identified within EQA

Standard	Good practice identified	Observation
1000	An Internal Audit Charter has been established and agreed with each Authority	The Charter is comprehensive and establishes an appropriate framework against which internal audit services can be delivered.
1312	The IASS has conducted annual self assessment exercises resulting in an annual development plan which is agreed by the host authorities.	Demonstrates a process and commitment to continuous improvement.
2020	Active engagement at officer and member level	Represents the establishment of a good understanding of key issues through interaction with positive feedback from all officers and members who participated in the assessment.
2030	The IASS routinely assesses its training needs and discusses requirements with the Lead Officer Group	This represents a firm basis for the consideration of training and recruitment needs as well as the use of external support
2040	A detailed internal audit manual is in place	Provides for a consistent methodology, within the IASS this is delivered through a series of templates
2060	Reports are produced using a standard template which is consistently applied. Customer feedback is routinely obtained following conduct of an audit.	Demonstration of a consistent approach for communication which is well received by management and the Audit Committee
2300	Audits are performed using an approach which is consistently applied	This supports a view that the internal audit team understand the standard processes, receive supervision and are effectively trained.
2400	Reports are clear and express opinions in a manner that is understood by stakeholders. Reports containing more significant recommendations are presented to operational management meetings where felt appropriate	Reports are produced on a timely basis, with summaries being produced for Audit Committee attention



# Resources

Business Vision and Mission, Governance arrangements, Recognition of standards, Guidance, Procedures and Supervision, Terms of Engagement, Ethics and business conduct.

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	Issue identified	Recommended action
1	No observations	

	Issue identified	Recommended action
1	<p><b>Governance and standards</b></p> <p>The Internal Audit Shared Service does not have an Internal Audit Manual which reflects the PSIAS. Instead the service has opted for a 'Process and Standards Map' supported by a series of standard templates which must be completed as part of the audit process. It is felt that understanding and status of internal audit would be enhanced if key standards within the PSIAS were fully cross referenced to these documents.</p>	<p>Understanding of and training in the application of the PSIAS would be enhanced by cross referencing templates to specific standards or by reflecting the key standards within the document 'IA Process and Standards Map'.</p> 
2	<p><b>Internal Audit Planning</b></p> <p>Whilst internal audit planning is being increasingly based upon a risk model as required by the PSIAS, the process largely depends on an assessment devised by internal audit; rather than reflecting wider risk issues and in particular use of different definitions of risk impact to those approved within the Council risk management strategy.</p> <p>There should be a direct and identified link between the internal audit plan content discussed with Audit Committees and the risk based reasoning for inclusion of the assignment in the audit plan, in turn this should drive the preparation of the terms of reference for each assignment as recorded within the Audit Brief.</p> <p>The focus for assignments can therefore be shown to directly relate to the value of the 'control risk' and as a result an opinion based upon the robustness of the controls and assurances available to management and the Council.</p>	<p>a. Audit Plans should be constructed through using an audit needs assessment process which achieves the objectives of the service as set out in the Internal Audit Charter. The audit planning process should be designed to reflect the assurance needs of each Council through transparent alignment with the Council wide approach to risk management. </p> <p>b. The internal audit planning process should further identify other sources of assurance that are available and upon which Councils can place reliance. </p> <p>c. The starting point for the development of the Audit Brief should be a preliminary discussion with management regarding the inherent and residual risks relevant to the audit area under review. It may aid assignment planning, if the management objectives for the area under review were also identified. This should result in the formation of a direct link with the Authority's risk register and the key mitigating controls highlighted, thereby aiding the understanding and ability of members of the Audit Committee to contribute to the assurance agenda. </p>

Client engagement and relationship, Directed led service, Terms of Engagement (Audit/Assignment Brief), Discussion of assurance and advisory opinions, Reporting at assignment and strategic levels

	Issue identified	Recommended action
1.	<p><b>Assignment Planning</b></p> <p>The service currently initiates each audit through engagement with management which provides for creation of an Audit Planning Document and a Terms of Reference which is then shared with management as an agreed basis for the audit.</p> <p>The assignment is then structured around control objectives and a framework of expected controls and was previously only loosely related to the risks which have been discussed with management. In a new process from 2016/17 each control objective is supported by an analysis of risks.</p>	<p>Internal audit working papers should focus on major risks to the Council that have been identified and discussed with the auditee; this should include an assessment of the inherent risks in each area (regardless of whether these are specifically recorded with the risk management system)</p> <p>Terms of reference should be constructed based upon the principal risks identified and not control objectives. This will allow the audit to naturally reflect assurance regarding the risks identified within the 'Control Matrix'. An example template is provided at Appendix A.</p> 
2	<p><b>Focus on pre-identified controls</b></p> <p>Assignments are currently undertaken by reference to control objectives and corresponding controls; there is a tendency for these to reflect Key Lines of Enquiry (KLOE) based controls emanating from external audit practices and to a degree past audits rather than be generated to reflect the materiality of the current risk involved. The service has more recently commenced consideration of wider risk aspects relating to the area subject to review.</p> <p>.</p>	<p>The use of risk as a basis for the control matrix will allow auditors to focus on the key controls and assurances which reflect the most material control risk to the area under review.</p> <p>The service should continue to develop pre-audit communication with management to focus on significant risk and key controls.</p> 

	Issue identified	Recommended action
3.	<p><b>Control Matrix templates</b> Assignments commence with meetings with officers at which notes are recorded relating to how the system works.</p> <p>The control matrix then contains a record of the actual controls and there is a tendency for auditors to duplicate the notes referred to above and/or the controls in the section on findings.</p> <p>Further improvements to remove duplication are in place for 2016/17.</p>	<p>Recording the system in note form and the essential detail of interviews is regarded as good practice.</p> <p>When this is supported by actual controls and appropriate testing the findings column may be completed by the use of an opinion in the form of is the control adequate and effective (or not).</p> 
4	<p><b>Closing meetings</b> Whilst those files reviewed all contained reference to a closure or exit meeting it was noticed that the record of the closing/exit meeting took different forms.</p> <p>There was evidence that the closure meeting also highlights good practice and this is considered good practice.</p>	<p>A consistent approach to the recording of the details discussed at the closing meeting and any agreements reached should be introduced.</p> 
5	<p><b>File structure</b> A consistent file structure has been introduced across all areas of the Shared Service. We did observe that the reporting section was 'cluttered' and may be better organised to enable effective review and supervision.</p> <p>A file index form is used to record progress on each audit and generate the file structure.</p>	<p>It is suggested that the sub structure to the reporting file may be better organised as closing meeting, draft report and final report.</p> 

	Issue identified	Recommended action
6	<p><b>Audit Opinions - Recommendations</b></p> <p>These are currently developed and assessed by each internal auditor, and reviewed by the Supervisor prior to release of the draft report and which include a grading of the recommendations being made.</p> <p>The definitions used by internal audit to support opinions have been revised between 2015/16 and 2016/17 financial years with the later year showing better reflection with each Authority's risk appetite and the definitions of impact risk.</p> <p>The basis for grading of recommendations should normally as a result influence the overall opinion for each audit directly, for example if a risk falling into a definition of the highest category is identified (potential for death, loss greater than £500k) then the assurance level given is reduced. Any risk of this nature should automatically trigger a negative audit opinion of 'limited assurance'.</p> <p>At present the service prefers to retain a basis which provides flexibility for the CIA to determine the grading of the recommendations being made.</p>	<p>a) Risk definitions used by internal audit should be developed to reflect the risk appetite within each organisation, and the definitions of impact and likelihood used by the Council.</p> <p>It is recognised best practice to use terminology such as High, Medium and Low or Fundamental, Significant and Merits attention and perhaps support this with RAG rated colours linked to the Council's risk management system.</p> <p>These should be used by each internal auditor to grade the recommendation and discuss the level of risk to which the organisation is exposed with each auditee at the exit meeting.</p> <p>b) Consideration should be given to removing the need to include 'low' rated recommendations in formal audit reports; alternatively reflecting on these in discussion at the closure meeting and confirmed in a side letter or email to the manager. This would aid the profile of internal audit through concentrating on things that really matter in relation to significant risk as defined within risk management policies.</p>

	Issue identified	Recommended action
7	<p><b><i>Audit Opinions - Overall opinions</i></b></p> <p>These are currently based upon the personal judgement of each auditor, within the definitions specified as relating and subject to review by the supervisor and CIA of the draft report prior to release.</p> <p>Wider best practice provides for three levels of opinion being substantial, adequate or limited as this provides a clearer indication to stakeholders of the level of assurance that can be gained. This opinion can then be aligned directly with the nature of the risks being identified and the grading of those recommendations being made.</p>	<p>a) The grading of reports should be based upon the level of risk exposure identified within the review and reflect the highest ranked recommendation being reported upon.</p> <p>Best practice would reflect:</p> <ul style="list-style-type: none"> <li>- Where a fundamental risk (red) is identified that limited assurance is given.</li> <li>- Where significant risks (amber) are identified then adequate assurance is given, and</li> <li>- Where 'merits attention' (green) risks are identified these are not referred to in the report and substantial assurance is given.</li> </ul> <p>b) Reducing the levels of opinion to three at all clients would provide a clearer indication of the assurance being provided and represent a more straight-forward approach for internal audit staff to administer.</p>

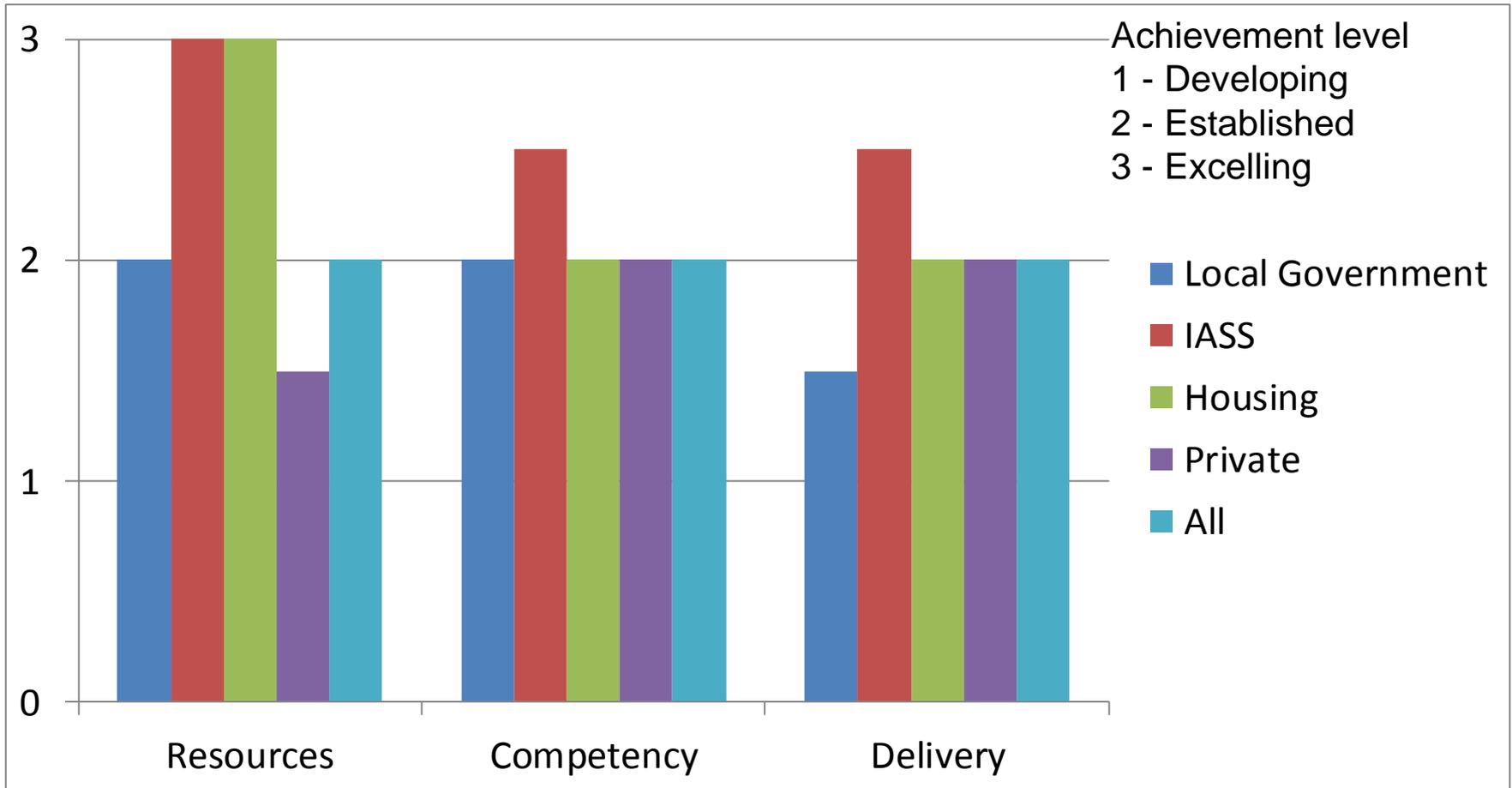
	Issue identified	Recommended action
8	<p><b>Delays in reporting</b></p> <p>The service produces a consistent quality of report albeit that internal audit reports may be considered 'lengthy' by comparison to developing practice in other sectors. In developing an increasingly risk based approach consideration could be given to moving to an exceptions based executive summary highlighting significant risks.</p> <p>We do however recognise that the section does not wish to move to an exceptions based methodology and that both Executive Management and Audit Committee reflection on current reporting is positive.</p> <p>It was observed that the time taken to deliver a final report was often extensive; this appear to relate to audit briefs being planned ahead of the commencement of fieldwork and the time taken to agree a draft report with management.</p>	<p>a) The service should consider whether focusing on risk as a basis for reporting would allow movement towards an 'executive summary' approach which highlights only significant risks.</p> <p>This may help further build the profile of internal audit and allow greater efficiency within the team through reducing the time consumed in report production and clearance; thereby reducing the overall time taken to report on assignments. </p> <p>b) Moving to reporting on significant risk may also increase ownership of draft reports by management and decrease response times; if this is not successful it is recommended that delays in response are brought to the attention of the Audit Committee. </p>

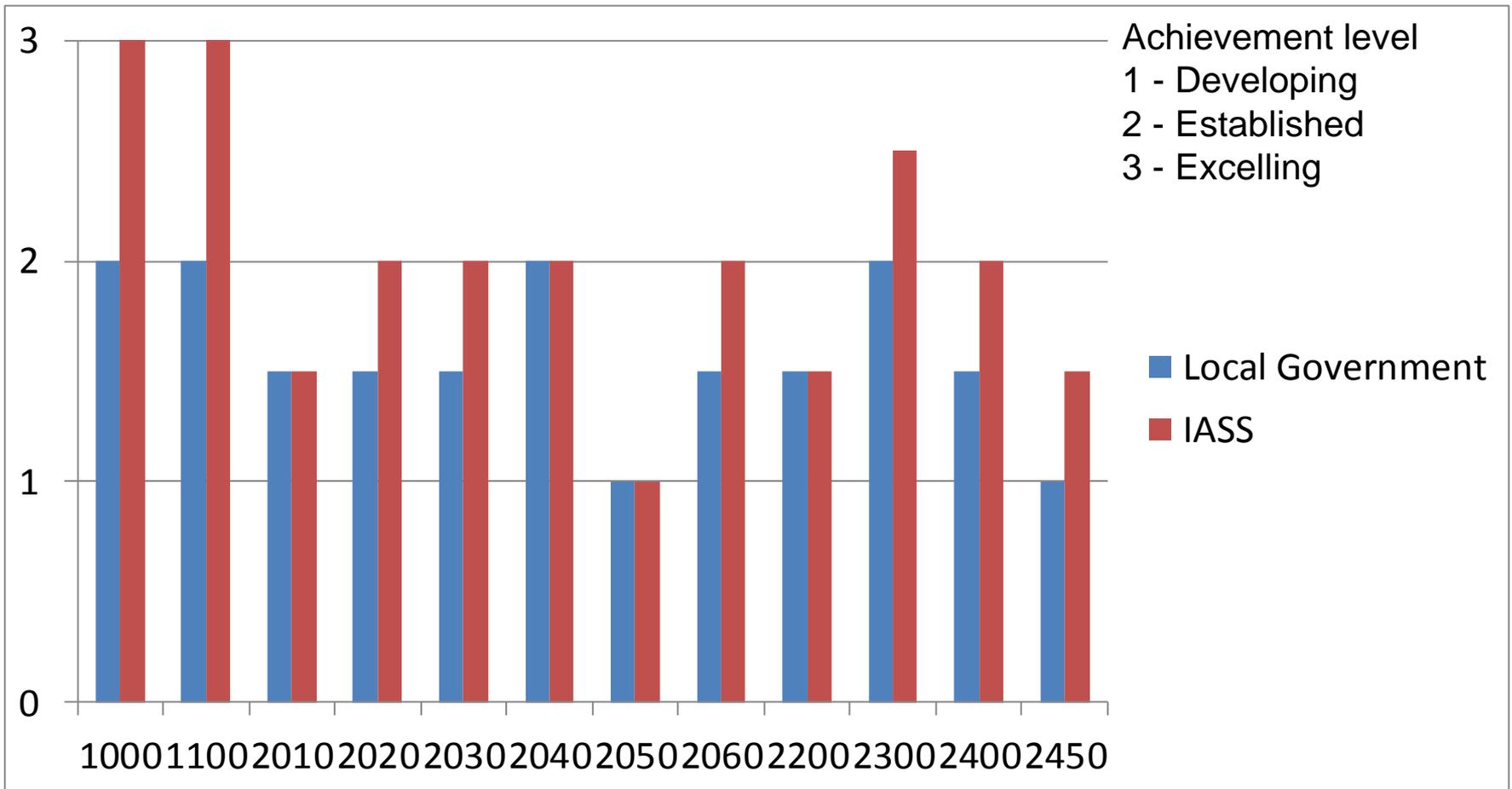
	Issue identified	Recommended action
9	<p><b>Annual Report</b></p> <p>The CIA produces an Annual Audit report which summarises the years work and includes analysis of performance. The opinion reflects</p> <p>“Based upon the results of work undertaken during the year, it is the Internal Audit Manager’s overall opinion that the Council has an adequate and effective governance, risk management and control framework”.</p> <p>The form required by the PSIAS requires a wider statement which <i>‘must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the board’</i>.</p>	<p>In alignment with recommendations made earlier, the internal audit plan should be constructed to provide an explicit link to risk and the other assurances available so that the CIA is able to provide wider assurance to each Authority in support of the governance statement.</p> <p>Best practice is that the Annual Report should also contain reference to all significant risks and therefore co-ordination with and an understanding of issues being raised by the range of assurance sources available is essential in order to meet this broader scope.</p> <p>An example of the words which may be used has been provided in Appendix B.</p> 

# Summary Audit Committee feedback

Question	A	B	C
Purpose	✓	✓	✓
Understanding of Council requirements	✓	✓	✓
Adequate assurance provided	✓	✓	✓
Independence with contact outside of meetings	✓	✓	✓
Status	✓	✓	✓
Experience, skills and effective communication	✓	✓	✓
Effective performance	✓	✓	✓
Effective planning and priorities	✓	✓	✓
Other relevant observations			
a) Councils benefit from the shared service. b) The team does well to cover the diverse range of services and therefore risks. c) Responds well to questions from Members. d) The team create good working relationships. e) Internal Audit has grasped the importance of following up recommendations to evidence implementation and regularly reports adherence to action plans. f) The shared service has improved the performance of the internal auditors and by some measure has raised their status and objectivity			

1	<b>RESOURCES</b>		<b>Excelling</b> – Processes in this area are fully embedded within every day practices and reflect best practice that is at least consistent with PSIAS expectations.
2	<b>COMPETENCY</b>		<b>Established</b> – Processes in this area are embedded within every day practices, the EQA has identified a number of areas in which further development is desirable.
3	<b>DELIVERY</b>		<b>Established</b> – Processes in this area are embedded within every day practices, the EQA has identified a number of areas in which further development is desirable.





# Key PSIAS Standards assessed

(for benchmarking purposes)

Standard		Focus
1000	Purpose, Authority and Responsibility	The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the Definition of Internal Auditing, the Code of Ethics, and the <i>Standards</i> . The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.
1100	Independence and Objectivity	The internal audit activity must be independent, and internal auditors must be objective in performing their work.
2010	Planning	The chief audit executive must establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organisation's goals.
2020	Communication and approval	The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.
2030	Resource Management	The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.
2040	Policies	The chief audit executive must establish policies and procedures to guide the internal audit activity.
2050	Co-ordination	The chief audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimize duplication of efforts.
2060	Reporting	The chief audit executive must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the board.
2200	Engagement planning	Internal auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations.
2300	Work programme	Internal auditors must identify, analyse, evaluate, and document sufficient information to achieve the engagement's objectives.
2400	Communicating results	Internal auditors must communicate the results of engagements
2450	Overall opinions	When an overall opinion is issued, it must take into account the expectations of senior management, the board, and other stakeholders and must be supported by sufficient, reliable, relevant, and useful information.

- The internal audit provision within the Councils of Broxbourne, Epping Forest and Harlow complies with the expectations of the Public Sector Internal Audit Standards.
- The introduction of the shared service has benefited the three Councils and receives positive feedback from both Audit Committee Chairs as well as Executive Management.
- There are a number of areas in which the service can be further improved in relation to the use of risk based auditing which will provide increased levels of assurance to the Councils and assist in improving its profile and the subsequent feedback that is received from clients:
  - the service should continue to move to an approach that reflects full recognition of the risk factors recognised by the Councils both at a strategic planning level and when conducting assignments.
  - the use of opinions should be reviewed to better reflect the risk appetite of the Council and should reflect identification and escalation of recommendations graded as significant that match risk definitions graded as 'red' or 'amber' within the various risk management systems.
  - the Annual Report of the Chief Internal Auditor should be enhanced to reflect assurance related to awareness of the significant risks being faced by the Council.
- The further development of risk management systems to reflect an Assurance Framework within each Council would enable greater recognition of key mitigating controls and the other sources of assurance with which internal audit effort should be co-ordinated in order to support the Governance Statements process.
- Some revisions to the internal audit process may be beneficial in terms of improving efficiency and transparency of the assurance being provided.



## Assignment Brief

Client			
Assignment			
Audit Year:	Audit Ref:		

<b>Management Objective for the System</b>			
<b>Key Risks</b> <small>Identified from the Risk Register, discussed with management &amp; Knowledge Base</small>	<b>Key Controls (to mitigate risk)</b> <small>To include expected controls, those identified through discussion with client and documentation of controls</small>	<b>Conclusion</b> <small>In terms of adequate and effective mitigation of the risk identified</small>	<b>Report</b> <small>Reference</small>
1			
2			
3			
4			
<b>Audit Approach</b>			

## Example wording for positive annual opinion

- As the internal audit service provider to the organisation, I am required as the Head of Internal Audit to provide the organisation and the Chief Executive with a statement on the adequacy and effectiveness of the organisation's risk management, control and governance processes.
- In giving an opinion it should be noted that assurance can never be absolute. The most that the internal audit service can provide to the organisation is a reasonable assurance there are no major weaknesses in the organisation's risk management, control and governance processes.
- In assessing the level of assurance to be given, the following have been taken into account:
  - All audits undertaken during the year;
  - Any follow-up action taken in respect of audits from previous periods;
  - Significant recommendations not accepted by management or acted upon and the consequent risks;
  - The effects of any significant changes in the organisation's objectives or systems;
  - Matters arising from previous reports to the organisation;
  - Any limitations which may have been placed on the scope of internal audit;
  - The extent to which resources constraints may impinge on the Head of Internal Audit's ability to meet the full audit needs of the organisation;
  - What proportion of the organisation's audit need has been covered to date; and
  - The results of work performed by other assurance providers including the work of the financial statement auditors (if applicable).
- We are satisfied that sufficient internal audit work has been undertaken to allow us to draw a reasonable conclusion as to the adequacy and effectiveness (or inadequacy and ineffectiveness) of the organisation's risk management, control and governance processes.
- Overall in our opinion, based upon the reviews performed during the year, the organisation:
  - has adequate and effective risk management arrangements;
  - has adequate and effective governance; and
  - has adequate and effective control processes.