



cutting through complexity

Wiltshire Council

Review of Internal Audit Function

June 2013

PLANNING

CONTROLS

AUDIT

RISKS

MANAGEMENT



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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.uk.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

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We have reviewed the way in which SWAP undertakes internal audit work and assessed it against the eleven areas of the *CIPFA Code of Practice for Internal Audit in Local Government in the UK (2006)*.

Background & Information

South West Audit Partnership (SWAP) was formed in April 2005 to provide Internal Audit services to public sector clients within the South West of England. It currently provides such services to eleven local authorities throughout the region, including Wiltshire Council (the Authority).

Internal Audit is essential in providing an independent and objective opinion to the Authority on the control environment comprising risk management, control and governance by evaluating the Authority's effectiveness in achieving its objectives. An effective Internal Audit function enables the Authority to make informed decisions as to improvements required to the control environment. It also assists in the Audit Committee's responsibility to ensure that a sound system of control is in operation.

In addition to providing assurance that risks are being adequately controlled, there is an expectation that internal audit will add value to the Authority and help to ensure that there are processes in place to meet strategic targets.

In order to ensure that the provision of Internal Audit is of a satisfactory quality, external standards have been developed which outline the way in which such services should be planned, managed and delivered. These standards help to ensure that the Internal Audit function meets the needs of clients, their expectations, and the demands of ethical requirements.

During the 2012/13 year, and previous years, the standards applicable to public sector entities were contained in sector specific guidance. In relation to local government, this was CIPFA's *Code of Practice for Internal Audit in Local Government in the UK (2006)*.

As of 1 April 2013 this was replaced with the *Public Sector Internal Audit Standards (PSIAS)* which are based upon the *International Standards for the Professional Practice of Internal Auditing* developed by the Chartered Institute of Internal Auditors. This new set of standards applies to all public sector organisations, regardless of sector boundaries.

Scope & Objectives

We have reviewed the way in which SWAP undertakes internal audit work and its interactions with the Authority, in order to comply with the requirements of the *CIPFA Code of Practice* in relation to the eleven areas outlined below:

1. Scope of Internal Audit
2. Independence
3. Ethics for Internal Auditors
4. Audit Committees
5. Relationships
6. Staffing, Training, & Professional Development
7. Audit Strategy & Planning
8. Undertaking Audit Work
9. Due Professional Care
10. Reporting
11. Performance, Quality, & Effectiveness

Our review was undertaken specifically in relation to the work of SWAP for the Authority during 2012/13. As a result of this, compliance with the PSIAS has not been considered and this review does not represent an 'external assessment' as required by the PSIAS over a five year cycle.

SWAP has, however, undertaken an independently verified self assessment against these new standards which indicated that whilst there were some areas for improvement, compliance had generally been achieved. We have not verified the results of this exercise. In addition, where improvements were identified as a result of that review but have not been mentioned in this report, no assurance should be taken as to whether or not such improvements have been implemented.

We have reviewed the processes implemented by SWAP and assessed their compliance with the *CIPFA Code of Practice*.

We have not undertaken any work in relation to SWAP's compliance with the *Public Sector Internal Audit Standards*.

Audit Approach

The objective of the review was to ensure that the methodologies and practices adopted by SWAP provide the Authority with an internal audit service which complied with the *CIPFA Code of Practice* requirements.

Our work involved assessing the design of those controls and processes which SWAP has implemented in relation to the overarching governance arrangements. We reviewed a significant amount of supporting documentation and evidence provided by SWAP. We also selected a sample of Internal Audit reviews undertaken by SWAP during 2012/13 in order to assess the level of compliance in relation to specific areas of work completed.

As stated on the previous page, we have not undertaken any work in relation to SWAP's compliance with the newly implemented *PSIAS*. In practice many of the requirements will be similar. Despite this, compliance with the *CIPFA Code of Practice* should not be seen as guaranteeing compliance with the *PSIAS*.

Our testing indicates that in general the activities of SWAP complied with the requirements of the CIPFA Code of Practice.

We identified no areas of non-compliance. There were, however, a limited number of areas of partial compliance.

Conclusions

Our work identified no areas of non-compliance with the *CIPFA Code of Practice*. Whilst we identified a limited number of areas where there was scope for further improvements, none of these were indicative of major failings in SWAP’s methodologies and processes.

As a result of this, we have concluded that the activities of SWAP generally complied with the standards set out in the *CIPFA Code of Practice for Internal Audit in Local Government in the UK (2006)*.

Further details on our findings are provided on pages 5-8 of this report. In addition, we have outlined those areas which we identified partial compliance in [Appendix 1](#).

Whilst the *CIPFA Code of Practice* is no longer applicable, the resolution of the areas of partial compliance should help ensure that the requirements of the *PSIAS* are met and will also ensure that SWAP provides a high quality service to the Authority.

Overall Compliance Analysis

Sub Heading	No of standards assessed	Compliant	Partially Compliant	Non-Compliant	Coverage in this Report	
					Overarching Governance (pages 5-7)	Detailed reviews (page 8)
1. Scope of Internal Audit	8	8	-	-	✓	
2. Independence	9	9	-	-	✓	
3. Ethics for Internal Auditors	8	8	-	-	✓	
4. Audit Committees	6	5	1	-	✓	
5. Relationships	10	8	2	-	✓	
6. Staffing, Training & Professional Development	7	7	-	-	✓	
7. Audit Strategy & Planning	10	10	-	-	✓	
8. Undertaking Audit Work	11	10	1	-		✓
9. Due Professional Care	3	3	-	-	✓	
10. Reporting	19	19				✓
11. Performance, Quality, & Effectiveness	13	12	1	-	✓	
Total	103	99	4	-		

SWAP has developed an Internal Audit Charter which acts as a Terms of Reference and sets out the key elements of the relationship with the Authority.

SWAP's legal structure, in addition to the controls which have been internally implemented, help to minimise the risk in relation to independence.

All audit staff are required to comply with the Institute of Internal Auditor's Ethics Code and sign an annual declaration of compliance.

Scope of Internal Audit

SWAP has implemented a formal Internal Audit Charter which has been approved by both Wiltshire Council's Audit Committee and full Council. This document clearly sets out the roles and responsibilities relating to the Internal Audit service and how they are shared between the Authority and SWAP.

The Internal Audit Charter is designed to be reviewed on an annual basis, with input being provided by the Head of Internal Audit as to the need to make amendments. To this end, it is periodically included within the quarterly update reports which are presented by SWAP to the Authority's Audit Committee.

One area of potential risk in relation to the provision of Internal Audit services is the adequacy of skills and resources when delivering consultancy work. The Internal Audit Charter clearly states that consultancy work will only be accepted by SWAP when it is satisfied that it has the necessary skills and resources to deliver the specific work in question.

SWAP has also developed a documented audit planning process in relation to the formulation of the Annual Audit Plan. This process requires that the risks identified by the Authority, as well as any emerging risks, be considered when developing the audit plan for any given year.

Independence

SWAP's existence as a separate legal entity helps to reduce the independence risks that are encountered in relation to in-house Internal Audit provision. Such risks are further combated through the controls which SWAP has implemented, including annual declarations of interests for all staff and a register of hospitality and gifts received.

During the course of its work, SWAP may provide advice to the Authority as to the development of systems, processes or policies.

However, such advice does not extend to the actual development of systems. We identified no issues in relation to advice provided by SWAP.

Under the Internal Audit Charter, SWAP has direct and unrestricted access to key officers and Members. This is in addition to the general process whereby reports are provided to the Director of Finance and the Audit Committee. Access to such individuals is essential to ensuring that SWAP can adequately address any issues and risks identified as a result of its work.

Ethics for Internal Auditors

All staff are required to sign an annual Declaration of Independence & Ethical Behaviour. This sets out the key elements of those ethical codes governing the work of SWAP and serves to remind staff of the importance of adhering to their requirements. In addition, all new employees are provided with induction training which includes a session on the code of ethics published by the Institute of Internal Auditors. All SWAP staff are members of this body and are therefore bound by its ethical code.

Auditor objectivity, both perceived and actual, is protected through the requirement that any and all gifts received are disclosed and recorded. Where necessary, approval will be required prior to the gift being accepted. Further protection is also provided through the requirement that no auditor works on an area where they have held an operational role within the last year.

Briefings provided to auditors in relation to each review to be undertaken, in addition to testing and information recorded in SWAP's audit Software (MKI), help to ensure that work is undertaken in a competent and efficient manner.

In relation to confidentiality, SWAP has developed an Data Sharing Protocol which sets out the instances in which it would be permissible to share Authority data.

SWAP's interactions with the Authority's Audit Committee generally meet the requirements of the CIPFA Code of Practice. Despite this improvements could be made by formalising the access to private sessions with the Audit Committee.

There is currently no formally documented approach setting out how SWAP will work alongside regulators.

Timing of Internal Audit work has generally met the needs of External Audit, with one exception, and thereby helped to reduce the needs for duplication of work.

Audit Committees

The Authority has its own Audit Committee to which both Internal and External Audit report. From our observations at Audit Committee meetings, and discussions with relevant individuals, we have identified no issues in relation to the effectiveness of the working relationship between SWAP and the Audit Committee.

SWAP's annual audit plan is approved by the Audit Committee, and quarterly updates are provided to the committee in relation to the delivery of the plan. The Audit Committee also receives the Annual Internal Audit Report.

At current, the Internal Audit Charter does not state that the Head of Internal Audit has the right to meet with the Audit Committee in private. Whilst we feel that any such request would be accepted by the Audit Committee it would be beneficial to clarify this formally within the Internal Audit Charter when it is next revised.

Relationships

SWAP has developed formalised working relationships both within the Authority (governed by the Internal Audit Charter) and with ourselves as External Auditors (governed by a formal protocol agreement).

There is, however, no formal documentation as to how SWAP will work with regulators and other external agencies. In relation to such entities the agreement of formal protocols may not be feasible. In such instances, despite this SWAP's approach to such relationships should be clearly documented.

In relation to its work with External Audit, SWAP has ensured that work is mostly available on a timely basis so as to avoid any duplication of work, thereby reducing the impact on client staff. We identified one where this had not been achieved, namely the completion of general IT control testing relating to the SAP database.

We identified no issues in relation to the quality of relationships with the Authority (both officers and members), External Audit, or regulators.

Staffing, Training & Professional Development

SWAP staff are all members of the Institute of Internal Auditors and meet the Continued Professional Development requirements of that body. In addition, many of the staff currently employed by SWAP have joined the organisation through a TUPE process from partner authorities. This has helped to ensure that staff have the necessary knowledge and experience to provide Internal Audit services to local authorities.

We have confirmed that job descriptions are in place for all major job types and that these are updated on a regular basis. Where a more specific role is to be filled a specific person specification would be developed as part of the recruitment process.

SWAP has implemented a competencies matrix which identifies the skills required for each of the staff grades currently in operation. This is used as the basis for staff self-assessments and feeds into the personal development plans for each member of staff. These plans are designed to ensure that relevant training needs are met so that the required competencies are delivered.

Audit Strategy & Planning

SWAP developed an Annual Audit Plan for 2012/13 which was approved by the Audit Committee on 20 June 2012. This plan identified the individual reviews which were to be undertaken, the relevant risks, and the specific drivers behind each review. Delivery of the plan is monitored and reported to the Audit Committee on a quarterly basis. Whilst there have been a number of changes to the plan during the year, the Audit Committee has been kept fully informed throughout the year of such changes.

In addition to the Annual Audit Plan, SWAP has developed a formalised Business Plan which outlines its aims and objectives going forward, along with how it intends to deliver these objectives. Due to the separate legal nature of SWAP, this has not been subject to approval by the Authority's Audit Committee. It has, however, been appropriately approved within SWAP.

The need to exercise due professional care is reiterated through the Declaration of Independence & Ethical Behaviour.

Whilst SWAP has developed an Audit Manual, this is undergoing review and development in order to ensure that it provides necessary information to auditors and is fully available, including incorporation within the MKI system.

The quality of work is monitored through both an internal review process and regular external review undertaken in partnership with other local internal audit providers.

Due Professional Care

The exercising of due professional care is in part enforced through the requirement that staff comply with the Institute of Internal Auditors' Ethical Code. The need for compliance with this Code is reiterated to all staff through the requirement to completed an annual Declaration of Independence and Ethical Behaviour return.

In addition to the overriding ethical standards applicable, SWAP requires all staff to disclose any interest possessed or gifts received which may pose a threat to the exercising of professional care.

SWAP's Audit Manual sets out the requirements in relation to the delivery of work, including the evidence requirements applicable. Adherence to this requirements is monitored through the internal review process undertaken in relation to all work delivered. This review process is evidenced within the MKI system.

Performance, Quality, & Effectiveness

In order to support auditors in the delivery of their work, SWAP has developed a detailed Audit Manual. At the time of our work this was undergoing a full review process which is designed to ensure that the manual is fully up-to-date and represents SWAP's current practices and procedures. SWAP is also reviewing how the manual is made available to staff. The aim is to provide a version on the organisation's network or intranet whilst also incorporating it into the MKI system.

SWAP has implemented an internal quality review process which is designed to ensure that all audit work is undertaken to the appropriate standards and is fully evidenced and documented. Allocation of work to individual auditors is undertaken so as to take account of their skills and competencies.

As part of its quality processes, SWAP has entered into an arrangement with three other internal audit providers so as to provide independent external validation of compliance with applicable standards. The plan is to undertake an externally validated self-assessment exercise on a tri-annual basis. The self assessments undertaken by SWAP will be validated by the Devon Audit Partnership.

In addition to the above processes, SWAP has also issued client surveys in order to ascertain the perception of its clients. This highlighted a number of areas of concern in relation to the Authority which SWAP is in the process of discussing with the Authority and developing resolutions.

We noted that the quality of working papers produced by Internal Audit has improved significantly from prior years.

Despite the improvements observed, scope for further improvements remains in relation to:

- sample selection;
- Sample size; and
- referencing.

Reports produced by SWAP, both for individual reviews and the annual report, meet the requirements of the standards.

Undertaking Audit Work

The use of the MKI software helps to ensure that audit work is clearly documented and links back to the risks identified at the planning stage. Through the use of approved work programmes it also helps to ensure that adequate work is undertaken to reach an opinion of each area tested.

As a result of the implementation of this system significant improvements in relation to the documentation of audit work undertaken have been seen.

We have reviewed a sample of internal audit reviews undertaken during the year, in addition to those covered by our Financial Statements work. This confirmed that work was being undertaken in a risk based manner and was subject to appropriate review prior to reports being issued. Despite this, we identified a limited number of areas where further improvements could still be made in relation to:

- **Sample selection** – we identified one instance where the samples selected for testing were skewed towards the period immediately prior to the audit being undertaken rather than offering assurance over the whole year;
- **Sample size** – there were four instances where, in relation to work covered by the Protocol Agreement, the sample size adopted was less than we would have expected given the frequency of the control; and
- **Referencing** – whilst we noted that in general the clarity of work was significantly improved, there remained a small number of areas where the clarity of referencing could have been improved so as to make work easier to follow.

Despite these areas for improvement, the way in which work is undertaken by SWAP remains generally compliant with the *CIPFA Code of Practice*.

Reporting

In order to ensure that all reports issued by SWAP are of sufficient quality, and meets the expected standards, a template report document has been developed. This is designed to ensure that all relevant sections, including the provision of an overall opinion. The MKI system is designed to record the information which will populate this report as the audit work is undertaken. It also ensures that issues are prioritised according to the level of risk identified.

Clear timelines have been developed for the delivery of reports which set out the time lapse expected between each of the stages of the audit process. Our review of actual performance identified no significant failings in relation to this. We are aware, however that the timeframe for delivery of a number of reviews has been changed during the year. In many instances this was the result of a request from the Authority.

An annual audit report is produced by SWAP at the end of each financial year and presented to the Audit Committee. The 2012/13 report was presented to the Audit Committee on 18 June 2013. This report provided the overall Head of Internal Audit Opinion, details of the outcomes for the audit work undertaken during the year, an update on the plan for the subsequent year, and an assessment of the performance of Internal Audit during the period. The Annual Report is designed to support the Authority in the development of its Annual Governance Statement.

Appendices

Appendix 1 – Areas of Partial Compliance

We have outlined below the areas of partial compliance which we identified as a result of our work:

Standard	SWAP Current Position	Potential Improvements
4 - Audit Committees		
4.2.5 - Is there the opportunity for the Head of Internal Audit to meet privately with the Audit Committee?	<p>The Internal Audit Charter makes reference to the Head of Internal Audit having direct access to the Chair of the Audit Committee, but does not include a provision relating to the ability to meet privately with the Audit Committee.</p> <p>The relationship with the Council is such that any such request is likely to be accepted, but it could be expressed more clearly in the Audit Charter.</p>	Amend the Internal Audit Charter to include a clear provision stating that the Head of Internal Audit has the right to meet with the Audit Committee in a private session as and when deemed necessary.
5 - Relationships		
5.1.2 - Is there a protocol that defines the working relationship for Internal Audit with: <ul style="list-style-type: none"> a) Management? b) Other Internal Auditors? c) External auditors? d) Other regulators and inspectors? e) Elected members? 	<p>These relationships are governed by a number of documents:</p> <ul style="list-style-type: none"> ■ Management & Members – governed by the Internal Audit Charter and the Council's own Terms of References. ■ Other Internal Audit – at current there are no formal arrangements in place, although this is being reconsidered due to the increasing likelihood of working with other entities going forward. ■ External Audit – governed by a formal protocol agreed between the parties. ■ Regulators & Inspectors – There is no formal documentation as to how such a relationship would work. 	<p>Whilst it may not be possible to negotiate a protocol directly with regulators, it would be beneficial to include provisions within the Internal Audit Charter which provide clarity as to how SWAP will work with such organisations</p> <p>SWAP should also review any relationships it has with other Internal Audit providers, i.e. the internal auditors of the any entities with whom the Authority operates a joint budget. Where such relationships are likely to be ongoing, formal protocol arrangements should be developed to cover such relationships. In relation to more ad hoc working arrangements, it may be more appropriate to include details as to the approach to be adopted within the Internal Audit Charter.</p>
5.4.3 - Are the Internal and External Audit Plans co-ordinated?	In general SWAPs work has been timed so as to be available in time to meet the needs of External Audit. There was, however, one area of work where the SWAP work was not completed so as to be available for External Audit.	SWAP and KPMG will continue to work together to ensure that the delivery of audit work is planned so as to reduce the potential for duplication of effort between Internal and External Audit.

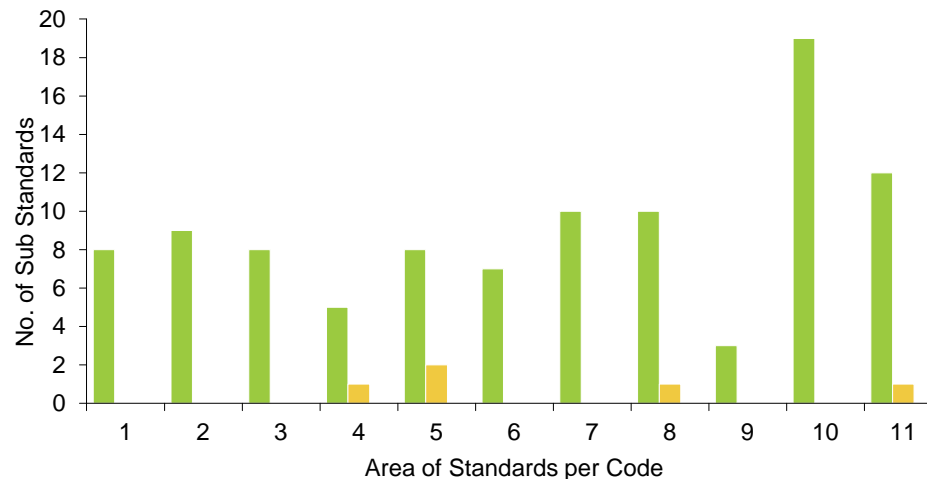
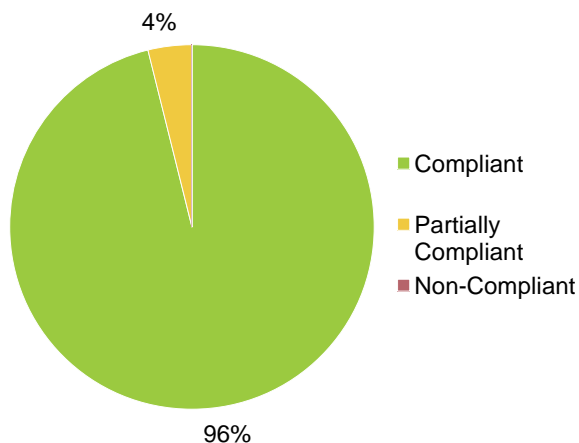
Appendix 1 – Areas of Partial Compliance (continued)

Standard	SWAP Current Position	Potential Improvements
8 – Undertaking Audit Work		
<p>8.3.2 - Are working papers such that an experienced auditor can easily:</p> <p>a) Identify the work that has been performed?</p> <p>b) Re-perform it if necessary?</p> <p>c) See how the work supports the conclusions reached?</p>	<p>Our review of a sample of audit files confirmed that in general the work had been performed to a high standard and was capable of re-performance.</p> <p>There were, however, a limited number of areas where the potential for improvement was identified (sample selection, clarity of referencing, sample size).</p> <p>The areas for improvement we identified in relation to sample sizes relate to areas covered by the Protocol Agreement between KPMG and SWAP.</p>	<p>Whilst recognising the progress which has already been made, SWAP should continue to emphasise the importance of producing high quality audit files. This includes the appropriateness of sample selection and size, and the clarity of referencing.</p> <p>Example sample sizes are provided within the <i>KPMG & SWAP Joint IA Protocol</i> document.</p>
11 – Performance, Quality, & Effectiveness		
<p>11.1.1 - Is there an Audit Manual?</p>	<p>SWAP has developed an Audit Manual which governs all work to be delivered.</p> <p>The audit manual is in the process of being uploaded into the MKI system in order to ensure that it is available to all staff during audits. In addition, it is held on the network drives in word format for reference.</p> <p>The recent independent assessment in relation to <i>PSIAS</i> compliance indicated that improvements to the manual were required in order to ensure that it was up-to-date and fully available to all staff. This is still a work in progress and is scheduled for completion in September 2013.</p>	<p>SWAP should ensure that plans are in place to complete the review of the Audit Manual on by the agreed deadline so as to ensure that staff are fully supported in the delivery of their work. Once completed, processed should be implemented which ensure that regular reviews are undertaken going forward.</p> <p>It is also essential to ensure that issues around the availability of the Audit Manual are resolved so that staff can freely refer to it when needed. It is essential that such access be available when working away from SWAP offices.</p>

Appendix 2 – Analysis of Compliance

We have set out below an analysis of the level of compliance achieved overall and, where not fully compliant, by standard area.

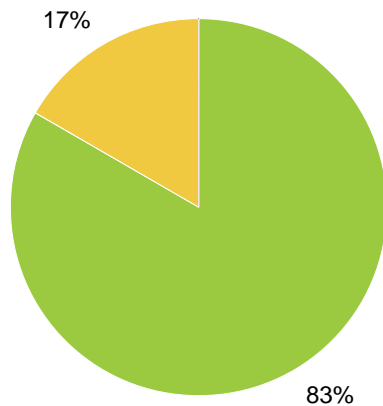
Overall Compliance Levels



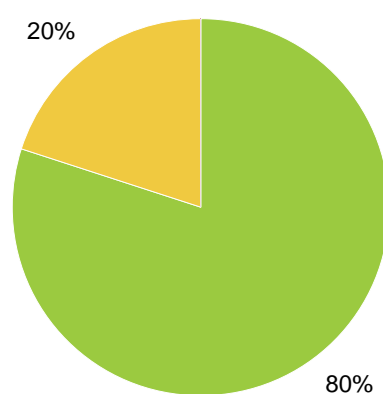
Areas of Standards per Code

1. Scope of Internal Audit
2. Independence
3. Ethics for Internal Auditors
4. Audit Committees
5. Relationships
6. Staffing, Training, & Professional Development
7. Audit Strategy & Planning
8. Undertaking Audit Work
9. Due Professional Care
10. Reporting
11. Performance, Quality, & Effectiveness

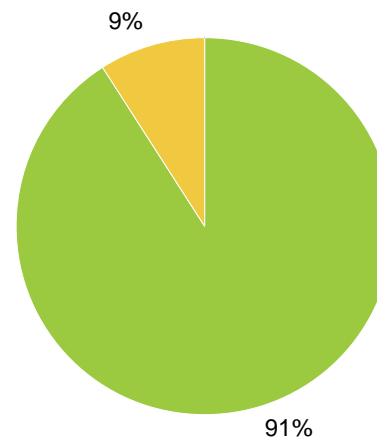
4 – Audit Committees



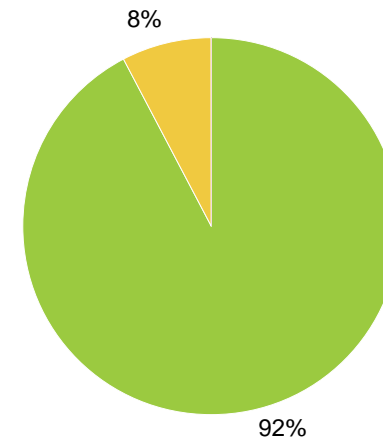
5 - Relationships



8 – undertaking Audit Work



11 – Performance, Quality & Effectiveness



In relation to all other areas SWAP achieved 100% compliance



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