

Internal Audit External Quality Assessment

Sevenoaks District Council
May 2015

Executive Summary

Background

The purpose of the review was to assess the current level of performance of the Internal Audit function against relevant industry / sector best practice where appropriate and professional internal audit standards including the Public Sector Internal Audit Standards (PSIAS).

Our review has included interviews with key business and Internal Audit stakeholders (including Senior Management and the Chairman of the Audit Committee), a review of the Internal Audit function's organisation, methodology and human resource capability and a detailed review of a sample of Internal Audit working paper documentation and reporting.

The internal audit service for Sevenoaks is shared with Dartford Borough Council and this assessment has been undertaken as a joint exercise but is reported separately to each Council. We have considered the context and organisation of the internal audit service at each council separately; this is the key difference between the two reports.

Context

The Dartford and Sevenoaks shared internal audit service

The shared service function has been in operation since April 2010. This is part of a wider partnership incorporating the Benefits and Revenues Function and Anti-Fraud. The partnership created the Audit, Risk and Anti-Fraud team, which is line managed by the Audit, Risk and Anti-Fraud Manager.

The audit team currently comprises 2.8FTE senior auditors who work across both councils, a full time Audit, Risk and Anti-Fraud Manager and 0.6FTE administrative assistant. There are currently two full time vacancies in the team; a senior auditor and a principal auditor, an agency member of staff is supporting the team in the short term. The team work to the same set of protocols and manuals and deliver approximately 630 days of work for each council which covers audit work, fraud, advice, administration and management.

Scope of our work

The scope of our review considered the following elements:

- a) **Organisation and independence** : the way that Internal Audit is structured and supported by the organisation to allow it to deliver its terms of reference;
- b) **Audit Team**: the availability (both in terms of quality and quantity) and management of internal audit resources to allow Internal Audit to deliver its remit;
- c) **Quality Assurance and Audit Management**: the processes and procedures in place to assess risk across the organisation and to develop high level plans for internal audit activities; the processes and procedures in place to ensure the efficient and effective detailed planning and completion of internal audit activities;
- d) **Communication and reporting**: the way that Internal Audit interacts with the organisation and third parties to ensure that the results of the audit are fully understood and appropriately acted upon; and
- e) **Quality, Tools and Performance Management**: to determine whether internal audit has processes and tools to ensure the quality of its delivery, including the appropriate and effective use of technology, sharing knowledge across the function and performance metrics in place to measure the effectiveness of Internal Audit against Stakeholders' objectives.

Overall observations

Areas of strength

- The Audit, Risk and Anti-Fraud Manager has undertaken a self - assessment of the internal audit function against the Public Sector Internal Audit Standards (PSIAS). The results of this assessment have been communicated to the management team and the Audit Committee and the team have an action plan in place to address gaps/ areas for improvement. The team also had an away day to identify further areas for improvement; these were incorporated into the action plan. The assessment and action plan was provided to us as part of this review and a number of the findings in this report are consistent with issues identified in this self-assessment.
- An audit manual and full set of templates is in place which is used by all team members; this supports the team and brings consistency. The team also has a quality management system in place which complies with ISO 9001: 2008. The manual and quality management system are comprehensive in that they cover all aspects of internal audit including the role of audit, independence and ethics, relationships, reporting, strategy, and steps for individual assignments, follow ups and other audit work. Some minor areas for improvement were identified which are detailed in there port below, however the documents in place largely represent good practice and conform with PSIAS.

Our review has identified a number of improvements to processes and procedures which Management and Internal Audit should consider as part of their continuous improvement programme. In particular our interviews with senior stakeholders identified a clear desire for Internal Audit to add more value. On further exploration it was clear that the internal audit function needs to strengthen its relationships with management to ensure that their needs are understood and that the key events, issues and risks the Council is managing are identified and that internal audit can be agile to provide assurance over these. This could include a greater use of internal audit advisory work, where appropriate, to provide ongoing assurance support, which will help to prevent risks crystallising and the objectives of management and the wider organisation being achieved.

Our findings below and the resulting action plan should be considered in accordance with the requirement for greater engagement with management and the need to understand what value from internal audit looks like from the perspective of senior stakeholders.

Significant issues and key areas for improvement

Area 1: Organisation and Independence –we have identified scope for improvement in the following areas; strategy, independence safeguards and updates to the Internal Audit Charter and Service Level Agreement.

Through stakeholder interviews we identified that there is currently a gap between current internal audit delivery and where stakeholders would like the service to be. The Council has changed a lot in recent years and the internal audit service needs to modernise and move on from, what may be seen as, more traditional approaches to audit and find innovative ways of providing assurance and adding value to the organisation. Examples of this could include the greater use of data tools and specialist skill sets to ensure that audit is providing assurance over the most complex and difficult risks that the Council is trying to manage.

This requirement should be captured in an audit strategy or vision to which all of the other recommendations in this report should be linked. There is a need for internal audit to showcase the good work it is doing and importantly the value it can add to the organisation and this strategy and vision is a good way to do this.

Area 2: Audit team – the current audit team are all generalist auditors with no specialisms or training in areas such as IT audit or project audit. A skills assessment of the current team against audit needs of the Council now and in the future should be undertaken.

Where gaps are identified a training/ development plan should be created to align the audit team to the current and future audit needs of the Council including filling current vacancies where appropriate. We have also identified areas below where training is needed now (for example application of methodology) to address immediate quality concerns.

In some cases it is not practical or possible to train an in house team to cover all of the specialist areas that an internal audit function needs to look at. Therefore, a review of the operating model is required to determine whether such skills and experience can be sought from within council departments (on a secondment basis), from audit functions at other councils or from private sector internal audit providers.

Area 3: Quality assurance and audit management – we identified scope for improvement in the following areas; risk assessment and planning; assignment planning; methodology; and review of working papers. A number of these areas should be addressed as a matter of urgency to improve the quality of the audit work delivered by the team:

- **Annual audit planning** - the PSIAS state that internal audit's plan of activity should be based on a documented risk assessment undertaken at least annually. The current audit planning process does not clearly evidence this requirement and we cannot confirm that the audit plan covers all relevant strategic risk areas.
- **Methodology** – we identified areas for improvement in audit protocols and templates used by the team. The key finding in this area was in relation to the application of methodology – auditors did not clearly articulate risks in Audit Briefs and did not clearly identify key controls in place within processes and systems to mitigate risks within audit test papers; training and detailed supervision is needed to improve quality in these areas.
- **Review of working papers** – peer review was in operation at the time of this review; the Audit, Risk and Anti-Fraud Manager did not review all working papers. We identified issues in the quality of audit work based on our file reviews that should have been identified in this review process; this suggested

the peer review process does not provide adequate oversight and challenge. We understand this system is no longer in place; however the new arrangements in place should be reviewed to ensure this provides adequate challenge and oversight.

The current structures and quality assurance process need to be considered as part of any review of the operating model, structure and resource needs of the function.

Area 4: Communication and reporting – we have suggested improvements in communication of audit annual risk assessment; format and content of audit reports; summary reporting; and audit follow up. Follow up results are currently reported based on returns from management; audit confirmation of implementation through review of evidence is not currently up to date or adequately documented.

Area 5: Quality, tools and performance management – we identified areas for improvement in the review process (as mentioned previously), an additional performance indicator that should be tracked (the time between completion of fieldwork and reporting), lack of technology and tools in use (paper files are still used), a lack of knowledge sharing, including of good practices across councils and time taken to complete audits

We found that a time tracking template is in use and auditors should track any delays and seek approval for additional time needed for audits. We reviewed some of these tracking templates and found that explanations were not comprehensive; the audit manager should further investigate the root causes of delays and where explanations are not provided more stringent measures should be considered.

Summary of recommendations

2.1 Organisation and independence

- a) **Strategy and vision** – the Audit, Risk and Anti-Fraud Manager should work with key stakeholders including the Chief Executive and the Strategic Management Team to understand expectations of internal audit; what they want from the service now and in the future. This should be captured in a strategy and vision for internal audit and an analysis undertaken to determine what additional skills and resources are needed to achieve this vision (see further recommendations below on Audit Team).
 - b) **Internal Audit Charter** – a number of improvements should be made as follows:
 - a. The Charter should clearly define the ‘board’ and ‘senior management’ within the Authority;
 - b. Further detail should be included on work undertaken outside of the audit programme and independence safeguards in place to maintain auditor independence;
 - c. The PSIAS state that the Charter should define the role of internal audit in fraud related work; this is not captured in the Charter at present; and
 - d. Reporting in place, including the annual summary report should be noted in the Charter.
 - c) **Service Level Agreement (SLA)** – ongoing operational issues should be resolved as a matter of urgency and the SLA should be updated and finalised to ensure arrangements for the provision of the internal audit service are clear.
-

2.2 Audit team

- a) **Skills assessment and training/ development plan**- the Audit, Risk and Anti-Fraud Manager should undertake a skills assessment of the current team against audit needs of the Council now and in the future. Where gaps are identified a training/ development plan should be created to align the audit team to the current and future audit needs of the Council.

In some cases it is not practical or possible to train an in house team to cover all of the specialist areas that an internal audit function needs to look at. Therefore, a review of the operating model is required to determine whether such skills and experience can be sought from within Council departments (on a secondment basis), from audit functions at other councils or from private sector internal audit providers.

- b) **Training** – weaknesses were identified in audit files reviewed, see 2.3.3 and 2.3.4. There are therefore some immediate training needs within the audit team including articulation of risk and identification of controls.
-

2.3 Quality assurance and audit management

- a) **Audit risk assessment and planning** – the Audit, Risk and Anti-Fraud Manager should ensure a full risk assessment is undertaken, this should be kept up to date, discussed with senior management and the audit committee and should drive the audit plan.
- b) **Audit scoping/ planning meetings** – these should be mandated in the audit manual and held for all audits to ensure auditors gain a more detailed understanding of the area under review and the key risks. This also helps auditors to build rapport with auditees and manage expectations. The Strategic Management Team should support this approach.
- c) **Content of Audit Brief** – the audit brief should be expanded to include a section on limitations, generic risks should be tailored to the area under review and risks should be clearly articulated. The Audit, Risk and Anti-Fraud Manager should hold a risk session with auditors to help them more clearly articulate risks.
- d) **Identification and assessment of controls** – test papers require auditors to document controls but this requirement is not being complied with. Additional training and guidance should be provided to all auditors to enable them to effectively identify, document and assess controls to mitigate risks in the processes/ systems under review for all risks identified in the audit brief.
- e) **Audit risk assessment and planning** – the Audit, Risk and Anti-Fraud Manager should ensure a full risk assessment is undertaken, this should be kept up to date, discussed with senior management and the audit committee and used to create the audit plan.
- f) **Sample sizes** – sample size guidance should be included in the audit manual to ensure consistency in sample testing across the audit team. Auditors should then justify sample sizes in working papers.
- g) **Review of reports and working papers** – the current review process should be reviewed to ensure adequate challenge, oversight and consistency of all reports and working papers.

2.4 Communication and reporting

- a) **Communication of audit risk assessment** – an audit risk assessment should be undertaken and the results of this should be discussed with relevant stakeholders and then used to inform the audit plan. The audit plan should be presented to the Management team and the Audit Committee in the context of this risk assessment.
- b) **Audit reports** – The Audit, Risk and Anti- Fraud Manager should review the report template and consider including an executive summary, limitations, the period covered by testing and good practice feedback. When reviewing audit reports the Audit, Risk and Anti-Fraud Manager should ensure adequate context is included in the action plans, and that actions are agreed and assigned a responsible officer and implementation deadline.
- c) **Annual report** – the Audit, Risk and Anti-Fraud Manager should review the opinion statement in the

annual audit report and update this to reflect the requirements of the PSIAS.

- d) **Summary reporting** – the Audit, Risk and Anti-Fraud Manager should ensure all relevant KPIs are regularly reported to Strategic Management Team and the Audit Committee.
 - e) **Reporting of audit recommendation implementation** - the Audit, Risk and Anti-Fraud Manager should make it clear to the Audit Committee that, at present, reporting of implementation is based on confirmation from the audit owner and no audit follow up procedures undertaken.
 - f) **Validation of implementation of audit recommendations** – validation of implementation should be brought up to date as a matter of urgency, test papers should also be created so it is clear what evidence has been reviewed to confirm implementation. Guidance on the level of audit evidence deemed appropriate should also be included in the audit manual.
-

2.5 Quality, tools and performance management

- a) **Performance metrics** – the Audit, Risk and Anti-Fraud manager should consider more formally tracking time between completion of fieldwork and reporting to ensure audit findings are reported and agreed in a timely manner.
 - b) **Time delays** – whilst the Audit, Risk and Anti-Fraud manager has implemented tracking of audit days and auditors are required to provide explanations of additional time/ audit days needed to complete audit work and seek approval, delays are still occurring and explanations are not always sufficiently documented. The Audit, Risk and Anti-Fraud manager should seek to get to the root causes of these delays and incorporating unexplained delays into staff performance appraisals. This also needs to be considered as part of the risk assessment and planning process to ensure that audits are as efficient and effective as possible.
 - c) **Audit tools and technology** – the audit team should consider implementing an electronic audit management tool to document audits to enable greater efficiency. They should also commence the use of Idea before knowledge gained through the training is lost and consider what other tools would be useful in the context of the internal audit strategy and vision.
 - d) **Sharing knowledge and good practices across councils** - the internal audit team should consider how they can better share knowledge and good practice across the two councils where relevant. This is a key benefit of the shared service that is currently not being fully realised.
-