

**AUDIT COMMITTEE – 5<sup>TH</sup> NOVEMBER 2014**

**PUBLIC SECTOR INTERNAL AUDIT STANDARDS - PROPOSALS FOR  
UNDERTAKING AN EXTERNAL ASSESSMENT**

**1. Purpose of the Report**

- 1.1 This report outlines the benefits of, and seeks Audit Committee agreement to, the proposed arrangements for carrying out the external review of the Council's Internal Audit function, as required by the Public Sector Internal Audit Standards (PSIAS).

**2. Recommendations**

**2.1 It is recommended that the Audit Committee:**

- i. **Considers and accepts the proposed arrangements for the review in order to meet the requirements of the PSIAS and to provide the necessary external assurances on the effectiveness of the Council's Internal Audit Service.**
- ii. **Alternatively, Members propose alternative arrangements for the assessment in order to gain the necessary external assurances on the effectiveness of the Internal Audit function.**

**3. Background Information**

- 3.1 The Accounts and Audit Regulations 2011 require the Council to have an Internal Audit function which operates in accordance with best professional practice. The recently introduced Public Sector Internal Audit Standards (PSIAS) are acknowledged as that best practice.
- 3.2 The Audit Committee received reports at the July 2013, December 2013 and June 2014 meetings which provided information on the requirements of, and extent of compliance with, the new standards. These reports made reference to the need to arrange external assessments of the Internal Audit service in line with the following standard:

*“Standard 1312 - External Assessments - External assessments must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organisation. The Chief Audit Executive [Head of Internal Audit] must discuss with the board [Audit Committee]; the form of external assessments; the qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.”*

#### **4. Options for Procuring the External Assessor**

4.1 As previously outlined, the Heads of Internal Audit across West and South Yorkshire have discussed the potential options for procuring their external assessment, as required by the PSIAS. Such options include:

- Peer reviews to be carried out by Heads of Internal Audit across the West / South Yorkshire Group;
- Buying-in the function from a professional body, e.g. The Institute of Internal Auditors;
- Buying-in the service from another suitably qualified and experienced individual / firm;
- Provision of the function via the appointed External Auditor.

4.2 Following detailed discussions of the options above, the consensus amongst the Heads of Internal Audit was that some form of Peer review of each other's arrangements was preferred. To this extent a Briefing Note / Terms of Reference document has been produced by the Group – see Appendix 1 attached, which sets out the benefits of the proposed approach, including:

- Cost benefits through carrying out the Peer Reviews within existing resources;
- Consistency of approach through all “signing up” to one method of review;
- Provides further evidence of the willingness and benefits of collaborative working.

4.3 In addition to the benefits above it should be noted that undertaking the External Assessments through a Peer Review exercise will also create enhanced Peer to Peer learning opportunities amongst senior officers within each Council taking part, thus providing valuable experience and knowledge which can be put to further use in the future.

4.4 One potential disadvantage identified from the proposed approach is the extent to which there may be a potential negative impact on professional relationships in the event of adverse findings from the assessment. The attached Briefing Note / TOR at Appendix 1 outlines how steps would be taken to mitigate against such a risk / issue.

4.5 Whilst the standards require external reviews to be carried out every 5 years, professional guidance indicates there is an expectation that the first review will be carried out no later than 2016. Once each West / South Yorkshire Council has obtained necessary approvals to the proposed Peer Review process, it is intended that a timetable will be drawn up for the proposed reviews to be completed.

4.6 Once the reviews have been completed, an evaluation of the Peer Review process will be undertaken to inform views for how and by whom future external reviews are undertaken.

## **5. Local Area Implications**

5.1 There are no Local Area Implications arising from this report.

## **6. Consultations**

6.1 The proposals for undertaking the external assessment have been subject to discussion with numerous internal and external parties in contributing to the recommendation made in this report.

## **7. Compatibility with European Convention on Human Rights**

7.1 In the conduct of audit work and investigations particularly, Internal Audit operates under the provisions of the Data Protection Act 1998, the Regulation of Investigatory Powers Act 2000 and the Police and Criminal Evidence Act.

## **8. Reduction of Crime and Disorder**

8.1 An inherent aspect of audit work is to prevent, detect and investigate incidents of fraud, theft and corruption. An essential element of the control and management of such work is the adherence to professional standards as defined with the PSIAS.

## **9. Risk Management Considerations**

9.1 The legislation and associated professional standards confirm the role of the Internal Audit Service as impacting on all the Council's strategic internal control and risk issues. It is therefore appropriate to periodically gain independent assurance that the service is effective in achieving its primary aims.

9.2 The professionalism of the service is based on adherence to statutory requirements and therefore the service must satisfy itself that it has fulfilled its obligations as set out in the 2011 Regulations, which were drawn up to set out provisions on financial management, annual accounts and audit procedures applying to local authorities.

9.3 Adherence to the PSIAS is featured as an important control measure which contributes to the management and control of several risks cited within the Division's operational risk register. All of these risks have been assessed and remain within the tolerance of the Division.

## **10. Employee Implications**

10.1 There are no employee implications arising from this report.

## **11. Financial Implications**

11.1 There are no specific financial implications associated with the recommendation within this report. Costs associated with the proposed external assessment process will be met from existing resources.

**12. List of Appendices**

Appendix 1 - West & South Yorkshire Heads of Internal Audit Group External Assessment – Peer Review: Terms of Reference

**13. Background Information**

Accounts and Audit Regulations 2011  
Public Sector Internal Audit Standards

Contact Officer: Head of Internal Audit & Risk Management  
Telephone: 01226 773241  
Date: 24th October 2014

**West & South Yorkshire Heads of Internal Audit Group**

**External Assessment – Peer Review**

**Terms of Reference**

**Purpose of the Paper**

At the meeting of the West and South Yorkshire HoIA Group held on the 20<sup>th</sup> November 2013 it was agreed that member authorities should begin to formalise the arrangements for their external assessments and develop a clear basis for the approach to be taken to undertaking such assessments.

It was agreed at this meeting that the external assessment process should be undertaken as a peer review whereby one Authority would undertake a peer assessment of a different Authority within the group. This approach forms the basis of this paper which provides background information regarding the requirements of the Public Sector Internal Audit Standards (PSIAS) in so far as they apply to external assessments along with details of the process to be followed by members of the group.

**Background Information**

Members of the Peer Group:

West Yorkshire: Wakefield Metropolitan District Council; Bradford City Council; Calderdale Council; Kirklees Metropolitan Council

South Yorkshire: Rotherham Metropolitan Borough Council; Doncaster Metropolitan Borough Council; Barnsley Metropolitan Borough Council

NB: Sheffield and Leeds City Council intend to undertake a similar Peer Review but alongside other Core Cities.

External Assessments:

The purpose of the external assessment is to help improve delivery of the audit service to an organisation. The assessment should be a supportive process that identifies opportunities for development which ultimately helps to enhance the value of the audit function to your Authority.

External assessments must be conducted at least once every five years by a qualified, independent reviewer from outside of the organisation. The HoIA should involve their Audit Committee and Section 151 Officer in determining the frequency, timing and scope of their external assessments as well as the selection of who will conduct the review and terms of reference for the review.

The two possible approaches to external assessments include either a full external assessment or an internal self-assessment which is validated by an external reviewer.

External reviewers should:

- Possess a recognised professional qualification
- Have appropriate experience of internal audit - at least five years at manager level within the public sector / local government
- Have detailed knowledge of leading practices in internal audit
- Have current, in-depth knowledge of the Definition, the Code of Ethics and the International Standards.

The HoIA should discuss the proposed form of the external assessment with their Line Manager (where relevant) and Audit Committee or Section 151 Officer (or equivalent) or Chief Executive prior to making recommendations to the Board (this is usually the Audit Committee) regarding the nature of the assessment. The scope of the external assessment should have an appropriate sponsor, such as the Chair of the Audit Committee or Section 151 Officer.

The HoIA should report the results of their quality assurance improvement programme (ongoing activity, internal and external assessments) to stakeholders. Such stakeholders should monitor the implementation of actions arising from internal and external assessments.

Members of the West and South Yorkshire HoIA Group have elected to adopt the latter of the 2 approaches with another member of the West and South Yorkshire Internal Group undertaking the validation. The key benefit to this approach is cost. The Chartered Institute of Internal Auditors (CIIA) offer a service to provide external assessments and can undertake a full external quality assessment which takes around 8 days at a minimum cost of £10K. They also provide a validated assessment, similar to the approach agreed by the West and South Yorkshire Internal Audit Group, which takes 6-8 working days and costs between £6K and £9K. Reviews at the higher end of the scale would include interviews with the senior team and the Audit Committee chair.

There are obvious financial savings to Members of the peer group by adopting the agreed approach as outlined within this paper. In addition, such an approach is in keeping with the promotion of collaborative working arrangements.

One of the risks identified by the group in respect of this form of peer review approach relates to the potential negative impact on professional relationships in the event of adverse findings. The terms of reference outlined within this paper would aim to mitigate against such a risk / issue. The CIIA have been consulted in terms of this form of peer assessment and are supportive of the approach. At the CIPFA audit update meeting held during November 2013, such an approach was cited as a good example of best practice in obtaining best value. In addition, there have been examples of groups similar to the South and West Yorkshire Group proposing to adopt a similar approach i.e. Greater London Authorities, South West Audit Group, Core Cities.

In adopting this approach HoIA and / or Section 151 Officer should be mindful that their Audit Committees and Section 151 Officer may require an external version of the assessment which may be perceived as providing a more robust and independent form of challenge.

### **Independence and Objectivity**

Prior to the commencement of the assessments taking place all parties should agree the programme of peer reviews and an appropriate timetable. It is important to ensure the independence of the Auditor undertaking the peer assessment. Any known or perceived

conflicts of interest should therefore be disclosed. It should be acknowledged at the outset that all West and South Yorkshire Internal Audit services have some knowledge of each other.

### **Agreeing the Assessment Process**

West and South Yorkshire colleagues should agree a programme of assessments taking into account the requirement noted above regarding independence and objectivity. In addition, colleagues should agree the number of days to be assigned to undertaking assessments, along with the sponsor for each review.

### **The Assessment Process**

#### **Completion of the Checklist:**

Each HoIA must complete the Checklist for Conformance with the PSIAS which is attached to the Local Government Application Note in advance of the external assessment.

#### **Pre Assessment Phase:**

- Confirm the terms of reference for the review, timescales and dates for the review.
- Obtain background information in order to obtain an appreciation of the function. This should include the IA Charter / Strategy or Terms of Reference (independence, scope authority, purpose and the relationship with the Audit Committee and senior executives).
- Obtain details of responsibilities, resources, structure and activity.
- Obtain details of any external client organisations e.g. YPO, Joint Authorities and consider whether such organisations may have different outcomes in terms of compliance with the PSIAS and whether separate assessments may be required.
- Obtain the completed self assessment which has been sign posted to the supporting evidence.
- Obtain evidence of how quality is maintained and how performance is measured and reported.

#### **Assessment Phase:**

- Review of documentation in support of the standards / checklist.
- Examine a sample of audit engagements according to the PSIAS and procedures.
- Interview key staff to confirm audit procedures and process.
- Undertake an exit meeting with the HoIA.

#### **Post Assessment Phase:**

The review should conclude with a detailed report providing an opinion on the Internal Audit activity's conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards highlighting any areas of partial conformance or areas which do not conform along with recommendations for improvement, where appropriate.

#### **Reporting Phase:**

- Discussion of the draft report with the HoIA and Sponsor.
- Issue of final report and agreed actions to the HoIA and Sponsor to confirm accuracy.
- Issue final report to the HoIA and Sponsor. HoIA / Sponsor to issue final report to their Audit Committee which includes an action plan and implementation dates.

In order for each Authority to obtain maximum benefit from the peer assessment approach each HoIA should share a synopsis of their respective outputs / report with members of the West and South Yorkshire HoIA group.

It is envisaged that each phase of the assessment process should take no longer than 1 day i.e. 4 days in total.