

AUDIT COMMITTEE – 5th DECEMBER 2018

ANNUAL REVIEW OF THE EFFECTIVENESS OF INTERNAL AUDIT

1. Purpose of the Report

- 1.1 The purpose of this paper is to inform the Committee of the framework proposed to prepare, manage and deliver the Quality Assurance and Improvement Programme (QAIP) for the Internal Audit function as required by the Public Sector Internal Audit Standards 2017 (PSIAS).

2. Recommendation

- 2.1 **Members consider and assess the proposed QAIP Framework which sets out how it will meet the requirements set out in the PSIAS.**
- 2.2 **That the Committee receives an annual update report on the delivery of the QAIP.**

3. Background Information

- 3.1 Revised Public Sector Internal Audit Standards (PSIAS) came into effect from April 2017. Within those standards is the requirement for the Head of Internal Audit to develop and maintain a Quality Assurance and Improvement Programme (QAIP).
- 3.2 The particular standard in the PSIAS is 1300 - *Quality Assurance and Improvement Programme*. This states that:

“The Head of Internal Audit must develop and maintain a quality assurance and improvement programme that covers all aspects of the internal audit activity”.

Guidance in relation to this states that:

“A quality assurance and improvement programme is designed to enable an evaluation of the internal audit activity’s conformance with the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The programme also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement. The Head of Internal Audit should encourage [Audit Committee] oversight in the quality assurance and improvement programme”.

- 3.3 Whilst the 2017 PSIAS formalised this as a specific requirement, previous Internal Audit standards and professional requirements ensured that Heads of Internal Audit had effective quality assurance arrangements in place. This incorporated the duty to undertake an annual self-assessment and an independent external assessment against the PSIAS once every five years. An independent external assessment was undertaken in late 2015 and reported to the Audit & Governance Committee in early 2016. This assessment confirmed that the Internal Audit function was in full conformance with the PSIAS.
- 3.4 It is important for the Internal Audit Team and client organisations that the requirements of professional standards are met and are seen to be met. A revised framework has been developed to ensure all aspects of the PSIAS are considered and factored into how the Internal Audit function is resourced, managed, audit work is identified and delivered, and personal professional standards are met.
- 3.5 The full PSIAS covering the QAIP is attached as Appendix 1. Note that the PSIAS refers to the *chief audit executive* as a generic term for the officer responsible for the Internal Audit function. The job title 'Head of Internal Audit' is most commonly used in the public sector. Also, the term '*board*' is used which in the public sector context is the audit committee. CIPFA have recently produced a Local Government Application Note (LGAN) to provide guidance to ensure consistency in how the PSIAS are interpreted specifically in a local government context.
- 3.6 The key framework of the QAIP are shown in the table below. A more detailed analysis of the PSIAS is shown at Appendix 2 alongside the actions being undertaken or planned below.

Key Standard 1300 Requirements	Action / Current Position
Internal Assessments:	
Ongoing monitoring of the performance of the internal audit activity.	Embedded processes in place as part of audit management arrangements. Action – review all aspects of performance monitoring as part of this QAIP process.
Periodic self-assessments or assessments by other persons within the organisation with sufficient knowledge of internal audit practices.	Annual self-assessments undertaken to check conformance. Action - Consider input from people from within client organisations.
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.	First external assessment undertaken in Nov/Dec 2015 and reported to Audit Committees in early 2016. Action – Consider approach and timing of next external assessment. Note – must be undertaken by December 2020.

Reporting on the Quality Assurance and Improvement Programme:	
The chief audit executive must communicate the results of the quality assurance and improvement programme to senior management and the board.	Previously reported through the HoIA Annual Report and also IA Effectiveness Update Reports. Action – specific annual QAIP report alongside the HoIA Annual Report.
Use of “Conforms with the International Standards for the Professional Practice of Internal Auditing”:	
Indicating that the internal audit activity conforms with the <i>International Standards for the Professional Practice of Internal Auditing</i> is appropriate only if supported by the results of the quality assurance and improvement programme.	Self-assessments indicate conformance and this statement has been incorporated in all internal audit reports. Action – this will be confirmed (or otherwise) during the full QAIP process to be undertaken between December and January and reported as above.
Disclosure of Non-conformance:	
When non-conformance with the <i>Code of Ethics</i> or the <i>Standards</i> impacts the overall scope or operation of the internal audit activity, the chief audit executive must disclose the non-conformance and the impact to senior management and the board.	Not applicable. Action – to ensure transparent reporting of any non-conformance identified following the full QAIP process in December/January and publication of an action plan.

- 3.7 The detailed draft QAIP action plan is currently being discussed within the Internal Audit Team to ensure understanding and importantly an ownership of the improvement opportunities and actions.
- 3.8 In order to ensure continuous improvement and focus on quality and conformance, consideration is being given to designate a Principal Auditor within the IA Team with the responsibility to maintain and manage the QAIP and general quality process. This Principal Auditor will report to the Audit Management Team on a quarterly basis with an updated PSIAS self-assessment and QAIP action plan.
- 3.9 In addition to the specific requirements of the PSIAS, there are a number of other continuous improvement related activities underway. These include:
- a) A fundamental review of the MKInsight audit management system to ensure, in liaison with the supplier, that its current full functionality is being utilised and that the system is developed to meet our needs;
 - b) A review of the format and content of audit reports (including terminology for the assurance opinion and recommendation categorisation) and the quarterly progress reports to audit committees to improve the clarity of key messages and assessment of implications (rather than making recommendations) for management to specify actions to be implemented;

PUBLIC SECTOR INTERNAL AUDIT STANDARDS - EXTRACT

1300 Quality Assurance and Improvement Programme

The chief audit executive must develop and maintain a quality assurance and improvement programme that covers all aspects of the internal audit activity.

Interpretation:

A quality assurance and improvement programme is designed to enable an evaluation of the internal audit activity's conformance with the *Standards* and an evaluation of whether internal auditors apply the *Code of Ethics*. The programme also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement. The chief audit executive should encourage board oversight in the quality assurance and improvement programme.

1310 Requirements of the Quality Assurance and Improvement Programme

The quality assurance and improvement programme must include both internal and external assessments.

1311 Internal Assessments

Internal assessments must include:

Ongoing monitoring of the performance of the internal audit activity.

Periodic self-assessments or assessments by other persons within the organisation with sufficient knowledge of internal audit practices.

Interpretation:

Ongoing monitoring is an integral part of the day-to-day supervision, review and measurement of the internal audit activity. Ongoing monitoring is incorporated into the routine policies and practices used to manage the internal audit activity and uses processes, tools and information considered necessary to evaluate conformance with the *Code of Ethics* and the *Standards*.

Periodic assessments are conducted to evaluate conformance with the *Code of Ethics* and the *Standards*.

Sufficient knowledge of internal audit practices requires at least an understanding of all elements of the International Professional Practices Framework.

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 must discuss with the board:

The form of external assessments.

The qualifications and independence of the external assessor or assessment team, including any potential conflict of interest.

Interpretation:

External assessments may be accomplished through a full external assessment, or a self-assessment with independent external validation. The external assessor must conclude as to conformance with the *Code of Ethics* and the *Standards*; the external assessment may also include operational or strategic comments.

A qualified assessor or assessment team demonstrates competence in two areas: the professional practice of internal auditing and the external assessment process. Competence can

be demonstrated through a mixture of experience and theoretical learning. Experience gained in organisations of similar size, complexity, sector or industry and technical issues is more valuable than less relevant experience. In the case of an assessment team, not all members of the team need to have all the competencies; it is the team as a whole that is qualified. The chief audit executive uses professional judgment when assessing whether an assessor or assessment team demonstrates sufficient competence to be qualified.

An independent assessor or assessment team means not having either an actual or a perceived conflict of interest and not being a part of, or under the control of, the organisation to which the internal audit activity belongs. The chief audit executive should encourage board oversight in the external assessment to reduce perceived or potential conflicts of interest.

Public sector requirement

The chief audit executive must agree the scope of external assessments with an appropriate sponsor, e.g. the accounting/accountable officer or chair of the audit committee as well as with the external assessor or assessment team.

1320 Reporting on the Quality Assurance and Improvement Programme

The chief audit executive must communicate the results of the quality assurance and improvement programme to senior management and the board. Disclosure should include:

The scope and frequency of both the internal and external assessments.

The qualifications and independence of the assessor(s) or assessment team, including potential conflicts of interest.

Conclusions of assessors.

Corrective action plans.

Interpretation:

The form, content and frequency of communicating the results of the quality assurance and improvement programme is established through discussions with senior management and the board and considers the responsibilities of the internal audit activity and chief audit executive as contained in the internal audit charter. To demonstrate conformance with the *Code of Ethics* and the *Standards*, the results of external and periodic internal assessments are communicated upon completion of such assessments and the results of ongoing monitoring are communicated at least annually. The results include the assessor's or assessment team's evaluation with respect to the degree of conformance.

Public sector requirement

The results of the quality and assurance programme and progress against any improvement plans must be reported in the annual report.

1321 Use of "Conforms with the International Standards for the Professional Practice of Internal Auditing"

Indicating that the internal audit activity conforms with the *International Standards for the Professional Practice of Internal Auditing* is appropriate only if supported by the results of the quality assurance and improvement programme.

Interpretation:

The internal audit activity conforms with the *Code of Ethics* and the *Standards* when it achieves the outcomes described therein. The results of the quality assurance and improvement programme include the results of both internal and external assessments. All internal audit activities will have the results of internal assessments. Internal audit activities in existence for at least five years will also have the results of external assessments.

1322 Disclosure of Non-conformance

When non-conformance with the *Code of Ethics* or the *Standards* impacts the overall scope or operation of the internal audit activity, the chief audit executive must disclose the non-conformance and the impact to senior management and the board.

Public sector requirement

Such non-conformances must be highlighted by the chief audit executive to be considered for inclusion in the governance statement.

DRAFT QAIP Action Plan

PSIAS / LGAN Ref	Requirement	Action	Action Officer	Timescale	Current Status
Core Principles - 3.1 Demonstrates integrity:	Having regard to your review of conformance with the Code of Ethics (Integrity, Seven Principles of Public Life), do you consider that the internal audit activity fully conforms with the PSIAS and LGAN by demonstrating integrity?	Review annual declaration made by Internal Audit staff to ensure a positive affirmation is recorded.	Audit Manager (BMBC)	By 31/12/18	In progress
Core Principles - 3.5 Is appropriately positioned and adequately resourced:	Based on your review of conformance with standards, do you consider that the internal audit activity fully conforms with the PSIAS and LGAN by being appropriately positioned and adequately resourced?	Review skill set requirements for the IA function for 2019/20 and beyond	HolA	By 31/03/19	To commence in January
Core Principles - 3.6 Demonstrates quality and continuous improvement:	Based on your review of conformance with standards, do you consider that the internal audit activity fully conforms with the PSIAS and LGAN by demonstrating quality and continuous improvement?	The delivery of the QAIP Action Plan will provide the framework and process to ensure quality and continuous improvement	Principal Auditor (QA and Standards)	By 31/03/19	In progress
1200 Proficiency and Due Professional Care – 12.5	Do internal auditors have sufficient knowledge of key information technology risks and controls	Review skills required based on 2019/20 planning process and explore options to address any identified gaps.	Audit Manager (BMBC)	By 31/03/19	In progress
1200 Proficiency and Due Professional Care – 12.6	Do internal auditors have sufficient knowledge of the appropriate computer-assisted audit techniques that are available to them to perform their work, including data analysis techniques	Review skills required based on 2019/20 planning process and explore options to address any identified gaps.	Audit Manager (BMBC)	By 31/03/19	In progress