



AUDIT & GOVERNANCE COMMITTEE
18 March 2013

2012/13 Review of the Effectiveness of the System of Internal Audit

SUMMARY AND PURPOSE:

This report sets out the findings and recommendations from the 2012/13 review of the effectiveness of the system of internal audit in Surrey County Council.

RECOMMENDATIONS:

The Committee is asked to consider the findings of this report and request an update on progress in implementing the recommendations arising from the review be included in the Annual Internal Audit report to be presented to this Committee by the Chief Internal Auditor in June 2013.

BACKGROUND:

- 1 The Accounts and Audit Regulations require local authorities *“to conduct, at least once in each year, a review of the effectiveness of the system of internal audit.”* The Audit and Governance Committee, as the Committee charged with responsibility for Internal Audit, considers that it is best placed to sponsor such a review on behalf of Surrey County Council.
- 2 As well as assessing the effectiveness of the current system of Internal Audit in Surrey County Council, this year’s review considered whether any changes are required to ensure compliance with the new Public Sector Internal Audit Standards (PSIAS) which come into effect from 1 April 2013.
- 3 To ensure an appropriate level of objectivity this review was undertaken by a suitably qualified external assessor (appointed through CIPFA). This approach seems to be favoured by the PSIAS which suggests that *“External assessments must be conducted as least once every five years by a qualified independent assessor or assessment team from outside the organisation”*.
- 4 The report produced by the external assessor concluded that internal audit in the Council is well led and is given a high priority by those charged with good governance who acknowledge that improvements have been made in the service over recent years. The report did however include a number of recommendations to ensure compliance with the PSIAS for 2013/14. The Chief Internal Auditor has agreed actions in response to those recommendations and these are detailed in the full copy of the assessor’s report which is attached at Annex A.

<u>IMPLICATIONS:</u>

Financial

There are no direct financial implications arising from this report

Equalities

There are no direct equalities implications arising from this report

Risk management

An effective system of internal audit complements good risk management across the Council

<u>WHAT HAPPENS NEXT:</u>

The findings from this review will help inform the Council's 2012/13 Annual Governance Statement.

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Sources/background papers: Public Sector Internal Audit Standards

External Review of the System of Internal Audit in Surrey County Council

6th March 2013

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Steve Mungavin, Elizabeth Humphrey and the team at CIPFA would like to thank elected members, the chief internal auditor, management and staff of Surrey County Council for their help and co-operation during this review.

1.0 Introduction

Background and terms of reference

1. A professional, independent and objective internal audit service is one of the key elements of good governance, as recognised throughout the public sector.
2. The Accounts and Audit Regulations 2006 introduced a requirement for local authorities *"to conduct, at least once in each year, a review of the effectiveness of its system of internal audit."*
3. The CIPFA Code of Practice for Internal Audit in Local Authorities in the United Kingdom is recognised as best practice and has been adopted by the County Council and previous effectiveness reviews have assessed the level of compliance against this standard.
4. A collaboration announced by CIPFA and the Chartered Institute of Internal Auditors (IIA) in May 2011 has led to the development of a new set of Internal Audit Standards – the Public Sector Internal Audit Standards (PSIAS) which will, in effect, replace the CIPFA Code of Practice and will provide a coherent and consistent internal audit framework for the whole of the public sector.
5. The draft standard will come into effect from 1 April 2013. In anticipation of this, the Chairman of Audit and Governance Committee of Surrey County Council (the Council) has asked that the effectiveness review for 2012/2013 assesses the Council's readiness for the PSIAS.
6. To ensure an appropriate level of objectivity it is proposed that this review is undertaken by a suitably qualified external assessor. This approach is favoured by the PSIAS which states that *"External assessments must be conducted as least once every five years by a qualified independent assessor or assessment team from outside the organisation"*.
7. The Council therefore commissioned CIPFA in December 2012 to undertake an external review of the system of internal audit. The review was benchmarked against the new PSIAS.
8. The aim of the review as set out in the terms of reference (Annex 3) is to review the effectiveness of the current system of Internal Audit in Surrey County Council and consider whether any changes are required to ensure compliance with the PSIAS from 1 April 2013.

Scope and methodology

9. In order to reach an opinion on the extent to which the internal audit function is complying with the PSIAS, CIPFA undertook:
 - A review of key audit documentation
 - Interviews with internal audit staff

- A review of feedback from key stakeholders through internal audit customer satisfaction questionnaires and interviews (refer to the list of participants in Annex 1)
10. It should be noted that the Council's internal audit service does not carry out any consultancy engagements. The standards relating to consultancy have not been included in this review.

2.0 Executive summary

11. CIPFA found that internal audit in the Council is well led and is given a high priority by those charged with good governance. The Council Leader, Audit Committee and chief executive are all strong advocates of internal audit and acknowledged that improvements have been made in the service over recent years.
12. We undertook an assessment of Surrey County Council's internal audit section's readiness against the Public Sector Internal Audit Standards (PSIAS), interviewing key stakeholders, reviewing working papers and other documents. The review found that most aspects of internal audit are satisfactory. Most of the necessary documents were compliant with the standards or needing only minor tweaks to make them compliant, interviewees were generally complimentary about the service provided by internal audit and audit planning and performance was broadly satisfactory.
13. There are, however, some areas for improvement, as follows:
 - Although assurance was given that all the appropriate processes are followed by auditors in planning and carrying out their work and its supervision and review, there was limited documentation of these processes in the two audits selected for review and so we were unable to assess them
 - In particular, although risks are identified in final audit reports, the links to risk were not made clear in the underlying supporting working papers or terms of reference reviewed by CIPFA
 - Audit should be more explicit about many of the aspects of its work, particularly in relation to the charter, annual internal audit report and other similar documents. For example, the internal audit charter should explicitly state that internal audit activity must be free from interference in determining the scope of internal audits, performing work and communicating results
14. CIPFA has assessed the position against each of the standards as follows:

Standard		CIPFA opinion
1000	Purpose, authority and responsibility	Minor amendments needed to achieve full compliance
1100	Independence and objectivity	Minor amendments needed to achieve full compliance
1200	Proficiency and due professional care	Partially compliant
1300	Quality assurance and improvement programme	Minor amendments needed to achieve full compliance
2000	Managing the internal audit activity	Minor amendments needed to achieve

Standard		CIPFA opinion
		full compliance
2100	Nature of work	Partially compliant
2200	Engagement planning	Partially compliant
2300	Performing the engagement	Partially compliant
2400	Communicating the results	Partially compliant
2500	Monitoring progress	Fully compliant
2600	Communicating the acceptance of risks	Fully compliant

15. In order to address these, CIPFA has made a series of recommendations which are set out in section 3 of this report and which are consolidated in the schedule in Annex 2. However, the three most important recommendations to effect the necessary improvements to internal audit and enable compliance with PSIAS are as follows:

- Use risk as a thread throughout the audit, driving the audit work and acting as a focus for the results (standard 2100)
- Have a standardised approach to audit planning, including documenting discussions between the auditor and audit manager about the audit, related risks and controls and service objectives so that there is a clear link between expectations of the audit through the work carried out to the findings included in the report (standard 2200)
- Introduce standard review sheets (see Annex 5 for a suggested format) for all audits, raising and clearing concerns or identifying where there are no review points (standard 2300)

3.0 Internal audit review findings

16. At a strategic level, we found that internal audit in the Council is well led and is given a high priority by those charged with good governance who acknowledge that improvements have been made in the service over recent years. The Council has proactively sought to improve the internal audit function for example by regular internal reviews, by learning from visits to neighbouring councils and by commissioning this external review.
17. The Leader of the Council recognises the value of the internal audit service and takes a proactive interest in its work. For example, we were informed the Leader makes a point of reading all internal audit reports to help keep informed of risks and controls in the Council. We also found the Audit Committee to be well respected in the Council with a good mix of skills and an effective Chair and Vice-Chair.
18. The chief executive places a strong reliance on internal audit to help provide assurances to the Council and he respects the independence and integrity of the chief internal auditor. The chief executive meets with the chief internal auditor regularly on a one-to-one basis as well as part of the statutory officers' team (which also includes the section 151 officer and the monitoring officer).
19. Despite the financial pressures of the current environment, the Council recognises the need to maintain internal audit resources as an important part of its assurance framework. Overall, we found that users of internal audit believed the service is strong in its regulatory role, although it could make some improvements, and it could add even greater value by providing professional advice and guidance. This is the backcloth to our review of internal audit against best practice.
20. When reviewing internal audit, in order to reach an opinion on the overall level of compliance with PSIAS best practice, CIPFA benchmarked audit practice in the Council with the following standards:

Attribute Standards

- Purpose, authority and responsibility
- Independence and objectivity
- Proficiency and due professional care
- Quality assurance and improvement programme

Performance Standards

- Managing the internal audit activity
- Nature of work
- Engagement planning
- Performing the engagement
- Communicating results
- Monitoring progress
- Communicating the acceptance of risks

Standard 1000: Purpose, authority and responsibility

21. This standard states that 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 *Standards*. The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.
22. This standard is designed to ensure clarity of the role and scope of internal audit and to provide a firm foundation for its powers and rights of access etc.
23. CIPFA found that internal audit has a draft charter (to be approved at the March 2013 Audit and Governance Committee) that reflects all the requirements of the standard although, in some cases, this was implicit rather than explicit. This charter will supersede the current terms of reference. Although the terms of reference are clear, it became evident that some auditees are unsure about audit's role and responsibilities.
24. To address these issues, CIPFA recommends that the chief internal auditor should amend the charter to:
 - Define the scope of internal audit more clearly, explicitly stating that it is able to cover all the operations of the Council
 - Refer to all the resources available to it (for example, hardware and software, access to information and training), rather than just to staff
25. We also suggest that the chief internal auditor produce a one-page summary of the charter, making internal audit's roles and responsibilities clear, to give to auditees at the start of each assignment and to help promote internal audit across the organisation.

Standard 1100: Independence and objectivity

26. This standard states that the internal audit activity must be independent and internal auditors must be objective in performing their work.
27. This is important because internal audit has to be able to carry out its work without being fettered or influenced in any way. If audit's independence is compromised, it is unable to deliver a valid opinion on the Council's operations.

28. CIPFA found that there were no significant problems with independence and objectivity but that some minor improvements would aid the perception of this independence and objectivity. The chief internal auditor's reporting lines do not follow best practice (CIPFA guidance on the role of the head of internal audit states that he or she should report directly to the chief executive or head of finance), something that is of concern to members of the Audit and Governance Committee. In practice, however, the chief internal auditor (CIA) has direct access to and regular contact with the chief executive and the senior management team and we believe that her independence is not, therefore, compromised.

29. The key areas for improvement are as follows:

- Include an explicit independence statement in the chief internal auditor's annual report and the audit plan report and the words "free and unfettered" or similar should be included in the charter
- Ensure internal audit staff receive annual documented reminders of the ethical standards of behaviour expected of them, especially around impartiality and being unbiased. One way to do this would be to discuss this review and the standards in a formal team meeting which would be minuted.

Standard 1200: Proficiency and due professional care

30. This standard states that audit engagements must be performed with proficiency and due professional care.

31. This is important because reliance is placed on audit's work to improve services and to reduce the risk of fraud and error. Poor quality work that includes errors is, at best, worthless and, at worst, could lead to reduced service quality, illegalities and other such problems.

32. CIPFA found that internal audit has a good mix of staff with different skills, knowledge and backgrounds and with access to the IT tools needed to carry out their work. Staff are kept up to date on emerging issues and undertake the training required of them although evidence of this at a corporate level is patchy with inconsistent use of the Galileo module to record training.

33. Our review of two audit files found no evidence of problems with the planning of audit assignments and we were told that the auditor and audit manager discuss approaches to the audit before work starts and as the work progresses. There was, however, no formal evidence of these audit planning discussions. Without these records, it may be difficult to demonstrate that an audit has been carried out as planned and staff may have limited information to refer to if they need reminding of the work required. Furthermore, in the absence of formal audit planning documentation, it may be difficult for audit managers to hold staff to account for their work.

34. Risk is considered as part of each audit assignment as evidenced by the references to risks in the final reports. However, there is no evidence that there is a link between risks and audit tests (formal audit planning

documentation would support this) nor is there any reference to the risks being considered in the audit terms of reference.

35. To address these issues, CIPFA recommends that the chief internal auditor should:

- Require use of the training module in Galileo
- Formalise planning of individual audits, perhaps through an issues and investigations matrix or similar (see Annex 4 for example)
- Consider ways to make the link to risk explicit by, at the very least, highlighting some of the key risks to be examined in the audit terms of reference

Standard 1300: Quality assurance and improvement programme

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

37. This is important because, without such a challenge to processes and systems, audit is unlikely to identify where it is not complying with best practice nor will it identify new areas of audit work and its value to the organisation is likely to diminish. On-going performance monitoring and regular reviews of audit effectiveness will identify where improvement is needed, show when that improvement has been made and demonstrate that audit is delivering as well as it can.

38. CIPFA found that there is an annual assessment of delivery against the plan and customer satisfaction reported in the annual report as well as references to performance at each Audit and Governance Committee meeting. These concentrate on quantitative not qualitative matters. In addition, the Audit and Governance Committee carries out an annual review of internal audit effectiveness, identifying areas for improvement. These reviews are reported separately from the annual internal audit report and no reference is made to them in that report although they clearly could contribute to the conclusions drawn therein. This review is the first external review of internal audit commissioned by the Council and it was set up in accordance with the standards. The Council is to be commended for taking this initiative.

39. To address these issues, CIPFA recommends that the chief internal auditor should:

- Summarise the outcome of the effectiveness reviews in the annual internal audit report.

Standard 2000: Managing the internal audit activity

40. This standard states that the chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organisation.

41. This is important because, without a fully-thought-through risk-based plan, internal audit is highly unlikely to identify where best to concentrate its efforts to deliver a useful output that will support its annual opinion and add value to the Council.
42. CIPFA found that annual audit planning was thorough, consultative and risk-based so that it could support the chief internal auditor's annual opinion. Making the link to the Council's objectives would be ideal but is not practical for two reasons: the objectives are high level and do not lend themselves to audit plans and they are not developed in time for the audit plan. However, although the audit team does consult with senior management to draw up these plans and explain their role and purpose, some managers seemed unaware of this.
43. We also believe that the annual planning report could be more explicit in making the link to risk as the basis for providing the chief internal auditor's annual opinion.
44. To address these issues, CIPFA recommends that the chief internal auditor should include a specific reference in the annual planning report to:
- Risk-based (as opposed to risk priority) planning
 - Supporting the chief internal auditor's opinion
45. The Council should consider ways to develop engagement with senior management and their staff. The one-page summary of the charter referred to above may help. In addition, being explicit about the nature of annual audit planning (and other) meetings, perhaps formalising them with agendas and minutes, could also be of benefit.

Standard 2100: Nature of work

46. This standard states that the internal audit activity must evaluate and contribute to the improvement of governance, risk management and control processes using a systematic and disciplined approach.
47. This is important because these are key areas for delivery of the Council's objectives and fundamental to delivering a comprehensive audit opinion.
48. CIPFA found that internal audit carries out an annual review of risk management, varying the focus each year to ensure broad coverage. These audits may be reduced as risk management is a low risk audit having been assessed as effective in the most recent review.
49. In addition, all audits consider areas of risk and risks are highlighted in reports. However, the wording does not comply with the Council's risk approach nor with best practice in that there is no clear description of underlying cause of the risk, the risk itself or the effect or impact of the risk should it occur. Improving this wording would help management understand the underlying concerns, make the link between risk and audit work clearer and make inclusion in the risk register, if necessary, simpler.

50. We found that controls and their related risks are explicitly documented in audit reports and we were told that auditors place considerable emphasis on controls in their work.
51. Internal audit's remit does not extend to auditing the governance process, other than in relation to information governance, although the chief internal auditor sits on the Governance Panel and contributes towards the Annual Governance Statement. Governance work is carried out by the Governance team in liaison with internal audit. We believe that this coverage of governance is generally sufficient and the CIA is likely to identify where there are areas of concern or where audit should be more closely involved.
52. To address these issues, CIPFA recommends that the chief internal auditor should consider:
- Aligning risk wording in reports with the approach used in the risk register
 - Using risk as a thread throughout the audit, driving the audit work and acting as a focus for the results
53. The Council might want to consider occasional independent (external) reviews of its governance arrangements.

Standard 2200: Engagement planning

54. This standard states that internal auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing and resource allocations.
55. This is important because such plans ensure that auditors, audit management and clients all have the same expectations of the audit and these are agreed in advance. The audit can then be checked against these plans and reviewed accordingly. Without such a plan, misunderstandings and confusion are possible resulting in wasted effort and possible conflict between auditor, auditee and management.
56. CIPFA found that terms of reference were issued for all audits and were accepted by clients before any audit work began. However, there was some evidence that managers did not understand what they were agreeing to as the purpose of the audit was not made completely clear nor is there a clear link to risk in the standard terms of reference. We were told that there was a risk assessment before every audit but, as this was not documented in the notes for the two audits that we reviewed in detail, we were unable to assess this. We were shown risk assessments for some of the more standard (mandatory) audits.
57. Neither of the audits that we reviewed included any audit planning documentation other than the terms of reference. It was, therefore, impossible to assess if the work had been carried out as planned and we did not know what guidance or support had been given to the auditor before carrying out

this work. There is some guidance on sources of information to inform an audit in the manual. This list did not include checking service business plans.

58. To address these issues, CIPFA recommends that the Council's internal audit service should:

- Be more explicit about the risks that are been tested for at the start of each audit, including them in the terms of reference
- Have a standardised approach to audit planning, including documenting discussions between the auditor and audit manager about the audit, related risks and controls and service objectives so that there is a clear link between expectations of the audit through the work carried out to the findings included in the report (the issues v investigation matrix referred to earlier is one possible approach)
- Include service business plans on the sources of information list

Standard 2300: Performing the engagement

59. This standard states that internal auditors must identify, analyse, evaluate and document sufficient information to achieve the engagement's objectives.

60. This is important because, without such information, it is impossible to demonstrate that the audit has been carried out properly and that its conclusions are valid. The chief internal auditor would be unable to form an opinion without this information.

61. CIPFA found that, with the exception of consistently demonstrating audit supervision, the requirements of this standard are met.

62. To address this issue, CIPFA recommends that the chief internal auditor should:

63. Introduce standard review sheets (see Annex 5 for a suggested format) for all audits, raising and clearing concerns or identifying where there are no review points

Standard 2400: Communicating the results

64. This standard states that internal auditors must communicate the results of engagements.

65. This is important because, if the results are not communicated clearly and promptly, risks, frauds or errors may materialise, necessary action will not be taken speedily and the audit opinion will be compromised. In addition, misunderstandings about results can lead to time being spent on clarification rather than on planned audit work.

66. CIPFA found that audit reports were generally clear (other than the risk wording mentioned above), balanced and, in the cases that we examined, issued in a timely manner. All draft reports are reviewed by the relevant audit

manager and by the chief internal auditor to ensure quality. Reports are written on an exception basis and some interviewees commented that on occasions there is, therefore, little recognition of good practice and audit reports can appear judgemental and disproportionate. There is clear guidance about report distribution which was followed in the cases that we reviewed. There was one instance of management concern about not being included in the distribution for a contentious report in a timely fashion, having missed the advanced copy they were sent.

67. Each report contains an overall opinion on a four-point scale and these opinions are defined in each report. We understand that there have been many discussions about these opinion definitions but our interviews revealed that there is some lingering confusion about the distinction between "some improvement needed" and "major improvement needed". In addition, there was concern about the judgement call required to distinguish between these two opinions.

68. To address these issues, CIPFA recommends that the chief internal auditor should:

- Make the basis on which the report is written clearer, perhaps with an opening statement along the following lines: "We have examined such-and-such service, looking at the following areas [list]. All areas other than those mentioned below were effective" or "This report is written on an exception basis and, as such, highlights only those areas where there are weaknesses. Any areas not mentioned below are deemed to be effective"
- Consider ways to improve report writing further, perhaps through a team meeting, discussion and guidance note to be included in the audit manual
- Consider ways to bring management's attention earlier to reports that are contentious so that they are not caught unawares
- Consider sharpening the definitions for the two opinions to make the distinction between them clearer. Alternatively, consider if different opinion titles or a numerical system might assist

Standard 2500: Monitoring progress

69. This standard states that the chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.

70. This is important because otherwise there is a risk that audit recommendations will not be implemented, negating the purpose of the audit and increasing the chance of fraud, error, inefficiencies, etc.

71. CIPFA found that the requirements of this standard were met.

Standard 2600: Communicating the acceptance of risks

72. When the chief audit executive concludes that management has accepted a level of risk that may be unacceptable to the organisation, the chief audit executive must discuss the matter with senior management. If the chief audit executive determines that the matter has not been resolved, the chief audit executive must communicate the matter to the board (i.e. the Audit and Governance Committee).
73. This is important because the organisation should not put itself in a position of taking ill-thought-through risks. CIPFA was told that this situation had never occurred at the Council.

Conclusion

74. Overall, our review found that most aspects of internal audit are satisfactory. Most of the necessary documents were compliant with the standards or needing only minor tweaks to make them compliant.
75. From the range of personnel interviewed, feedback was generally complimentary about the service provided by internal audit and we found that audit planning and performance was broadly satisfactory. There are, however, some areas for improvement which we have identified under each standard and in summary format in Annex 2.

Annex 1: Participants in the review

CIPFA would like to thank all those who contributed to this review.

Bill Barker	Audit and Governance Committee Vice Chair
Anne Butler	Assistant Director for Commissioning, A&SC Directorate
Paul Carey-Kent	Senior Finance Manager, A&SC Directorate
Ann Charlton	Head of Legal and Democratic Services
Cath Edwards	Risk and Governance Manager
Julie Fisher	Strategic Director Change and Efficiency
Denise Le Gal	Cabinet Member for Change and Efficiency
Nick Harrison	Audit and Governance Committee Chair
David Hodge	Leader of the Council
Sue Lewry-Jones	Chief Internal Auditor
Sheila Little	Chief Financial Officer & Deputy Director for Change & Efficiency
David McNulty	Chief Executive
Sarah Mitchell	Strategic Director, A&SC Directorate
Trevor Pugh	Strategic Director Environment and Infrastructure
John Woods	Assistant Director Transformation, A&SC Directorate
Members of the internal audit team	

Annex 2: Schedule of recommendations

Standard	Recommendation	Management Response	Further action
Std 1000	Purpose, authority and responsibility		
	Define the scope of internal audit more clearly, explicitly stating that it is able to cover all the operations of the Council	The Internal Audit Charter will be amended to reflect this requirement	
	Refer to all the resources available to it (for example, hardware and software, access to information and training), rather than just to staff	The Internal Audit Charter will be amended to reflect this requirement	
	Produce a one-page summary of the internal audit charter	Once the internal audit charter has been approved by Audit and Governance Committee the Chief Internal Auditor will produce a one-page summary for sharing with auditees at Service Liaison meetings and audit planning meetings	
Std 1100	Independence and objectivity		
	Include an explicit independence statement in the annual report and the audit plan report and the words "free and unfettered" or similar should be included in the charter	Agreed	
	Ensure internal audit staff receive annual documented reminders of the ethical standards of behaviour expected of them, especially around impartiality and being unbiased	There will be an annual reminder at an internal audit team meeting at the start of each year – with appropriate meeting minutes as evidence	

Standard	Recommendation	Management Response	Further action
Std 1200	Proficiency and due professional care		
	Require use of the training module in Galileo to record training and development	The Chief Internal Auditor will remind the team to keep training records updated in Galileo	
	Formalise planning of individual audits	Internal Audit Management will devise a standard approach to audit planning which clearly identifies risks. The approach for each audit will be formally documented and agreed between the auditor and the audit manager. Team briefing on this proposed approach will be provided at the April 2013 team meeting with the Audit manual updated to reflect this.	
	Consider ways to make the link to risk explicit by, at the very least, highlighting some of the key risks to be examined in the audit terms of reference	From April 2013 when the PSIAS come into effect the Internal Audit team will ensure the Terms of Reference for each audit identify the key risks.	
Std 1300	Quality assurance and improvement programme		
	Summarise the outcome of the effectiveness reviews in the annual internal audit report	Agreed- this will be actioned by the Chief Internal Auditor	
Std 2000	Managing the internal audit		
	Include a specific reference in the annual planning report to risk-based (as opposed to risk priority) planning	Agreed- this will be actioned by the Chief Internal Auditor	

Standard	Recommendation	Management Response	Further action
	Include specific links to risk supporting the chief internal auditor's opinion in the annual planning report	The Chief Internal Auditor will make it clear when presenting the proposed annual audit plan to the Audit and Governance Committee, that the plan is risk based and that as such, delivery of the audit plan of work will enable the Chief Internal Auditor to form an opinion on the Council's control environment.	
	Consider ways to develop engagement with senior management and their staff	A summary (1 page) charter will be used to assist this.	
Std 2100	Nature of work		
	Align risk wording in reports with the approach used in the risk register	The Chief Internal Auditor will discuss this in more detail with the Risk and Governance Manager. One approach may be to amend the Internal Audit Manual to provide more information on drafting internal audit reports. This could include describing risks in terms of cause, risk and effect.	
	Use risk as a thread throughout the audit, driving the audit work and acting as a focus for the results	This will be actioned through formalising the audit planning process and including risks in each audit's terms of reference.	
Std 2200	Engagement planning		
	Be more explicit about the risks that are being tested for at the start of each audit, including them in the terms of reference	Agreed. From April 2013 when the PSIAS come into effect the Internal Audit team will ensure the Terms of Reference for each audit identify the key risks.	

Standard	Recommendation	Management Response	Further action
	Have a standardised approach to audit planning, including documenting discussions between the auditor and audit manager about the audit, related risks and controls and service objectives so that there is a clear link between expectations of the audit through the work carried out to the findings included in the report	Internal Audit Management will devise a standard approach to audit planning which clearly identifies risks. The approach for each audit will be formally documented and agreed between the auditor and the audit manager. Team briefing on this proposed approach will be provided at the April 2013 team meeting with the Audit manual updated to reflect this.	
	Include service business plans on the sources of information list	Agreed – this will be included as part of a wider update of the Internal Audit Manual planned for Quarter 1 2013/14	
Std 2300	Performing the engagement		
	Introduce standard review sheets for all audits, raising and clearing concerns or identifying where there are no review points	The Galileo system already provides this facility although it is currently not consistently used. The team will be reminded at the April team meeting, of the need to mark working papers for review so audit management can raise review points at the earliest opportunity.	
Std 2400	Communicating the results		
	Make the basis on which the report is written clearer, perhaps with an opening statement along the following lines: "We have examined such-and-such service, looking at the following areas [list]. All areas other than those mentioned below were effective" or "This report is written on an exception basis and, as such,	Will consider this as part of a team meeting discussion on audit report writing with any agreed changes to guidance included in the Internal Audit Manual	

Standard	Recommendation	Management Response	Further action
	highlights only those areas where there are weaknesses. Any areas not mentioned below are deemed to be effective"		
	Consider ways to improve report writing further, perhaps through a team meeting, discussion and guidance note included in the audit manual	Agreed –this will be actioned during Quarter 1 2013/14.	
	Consider ways to bring management's attention earlier to reports that are contentious so that they are not caught unawares	Agreed. This will be considered at an Audit Management Team meeting.	
	Consider sharpening the definitions for the two opinions to make the distinction between them clearer. Alternatively, consider if different opinion titles or a numerical system might assist	The Chief Internal Auditor will discuss this with the S151 Officer.	

Annex 3: Terms of reference

Effectiveness of the system of internal audit 2012/2013

Background

The Accounts and Audit Regulations 2006 introduced a requirement for local authorities "to conduct, at least once in each year, a review of the effectiveness of its system of internal audit."

The CIPFA Code of Practice for Internal Audit in Local Authorities in the United Kingdom is recognised as best practice and has been adopted by the County Council and previous effectiveness reviews have assessed the level of compliance against this standard.

A collaboration announced by CIPFA and the Institute of Internal Auditors (IIA) in May 2011 has led to the development of a new set of Internal Audit Standards – the Public Sector Internal Audit Standards (PSIAS) which will in effect replace the CIPFA Code of Practice and will provide a coherent and consistent internal audit framework for the whole of the public sector.

The draft standard has been out for consultation and the expectation is that the PSIAS will be published in December 2012 and come into effect from 1 April 2013. In anticipation of this, the Chairman of Audit and Governance Committee has asked that the effectiveness review for 2012/2013 assesses the Council's readiness for the PSIAS.

To ensure an appropriate level of objectivity it is proposed that this review is undertaken by a suitably qualified external assessor. This approach would seem to be favoured by the (draft) PSIAS which suggests that "External assessments must be conducted at least once every five years by a qualified independent assessor or assessment team from outside the organisation"

Therefore an Independent External Assessor will be appointed to complete a review in line with these Terms of Reference on behalf of the Audit and Governance Committee.

Purpose of the review

To review the effectiveness of the current system of Internal Audit in Surrey County Council and consider whether any changes are required to ensure compliance with the PSIAS from 1 April 2013.

Work to be undertaken

This review of current working practices against the PSIAS will involve the following:

- Review of key audit documentation
- Interviews with Internal Audit Staff

- Review of feedback from key stakeholders – this may involve review of Internal Audit Customer Satisfaction Questionnaires and interviews with key stakeholders such as:
 - Leader of the Council
 - Members of the Audit and Governance Committee
 - Cabinet Portfolio holder for Change and Efficiency
 - Chief Executive
 - Section 151 Officer
 - Monitoring Officer
 - Risk and Governance Manager
 - Selected auditees

Outcomes

The findings of this review will inform the report of Audit and Governance Committee on the Effectiveness of the System of Internal Audit 2012/2013 which will be presented at a meeting of the Committee in February 2013. It is anticipated that the Independent External Assessor will attend that meeting of the Committee to present their findings.

Reporting arrangements

Auditor:	Independent External Assessor – to be appointed
Reporting to:	Audit and Governance Committee
Audit Ref:	IR / 171

Annex 4: Issues and investigation matrix

Issue/Risk	Investigation	Approach	Possible findings/notes
Individual aspects (risks, concerns, issues) that the audit is trying to reach a conclusion on, ideally expressed so that if everything is as it should be the audit response will be "yes" (eg payment are made on time and to the correct payee)	Method for checking this: <ul style="list-style-type: none"> • Testing • Interview • Observation • Review of papers • Cumulative audit knowledge (CAKE) • Etc 	<ul style="list-style-type: none"> • Details for the testing samples • Who should be interviewed • Where and when to carry out observations • Which papers to be reviewed • Etc 	Use this column for any other comments, ideas, etc

Annex 5: Review sheet

Review point	Response	Cleared Date