

**Audit Committee****on 26<sup>th</sup> June 2007**Report Title: **The review of the Effectiveness of the system of Internal Audit**Report of: **Head of Audit & Risk Management**Wards(s) affected: **All**Report for: **Non-key decision****1. Purpose**

1.1 To inform Members of the requirements of the Accounts and Audit (amendment) (England) Regulations 2006 and the action taken to address these.

**2. Recommendations**

- 2.1 That the Audit Committee notes the findings of the review of the effectiveness of the system of internal audit.
- 2.2 That the Audit Committee approves the action plan to address the identified areas for development.

**Report Authorised by:** Gerald Almeroth  
Acting Director of Finance



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**3. Reasons for any change in policy or for new policy development (if applicable)**

3.1 None

**4. Local Government (Access to Information) Act 1985**

4.1 List of background documents:

The following background documents were used in production of this report:

- Accounts and Audit (amendment) (England) Regulations 2006.

## 5. Background

- 5.1 Regulation 4 of the Accounts and Audit Regulations (2003) required audited bodies to conduct a review at least once a year of the effectiveness of its system of internal control and publish a statement on internal control (SIC) each year with the authority's financial statements.
- 5.2 The Accounts and Audit (Amendment) (England) Regulations 2006 came into force on 1 April 2006. Whilst many of the amendments clarify or correct elements of the 2003 Regulations, two of the amended regulations in particular have an impact on the process for preparing the SIC:  
**Regulation 4** requires the findings of the review of the system of internal control to be considered by a committee of the relevant body, or by members of the body meeting as a whole.  
**Regulation 6** requires bodies to review the effectiveness of their system of internal audit once a year and for the findings of the review to be considered by a committee of the body, or by the body as a whole, as part of the consideration of the system of internal control referred to in regulation 4.
- 5.3 The requirement to review Internal Audit does not specify what the review should consist of, nor does it state who should undertake this task. However, as the Audit Committee has responsibility for approving the Statement on Internal Control (SIC), it is considered appropriate that this Committee should have responsibility for approving how the new responsibility under Regulation 6 is discharged.
- 5.4 This report provides the Audit Committee with references to existing procedures, sources of information and measures in place in order to assist in being able to reach a conclusion on the adequacy and effectiveness of the Internal Audit Service.
- 5.5 In order to assess compliance with the amended regulations, Haringey's Internal Audit service was independently reviewed. The review was based on the revised CIPFA Code of Practice for Internal Audit in Local Government which was issued in December 2006 and covered the requirements of the Accounts and Audit Regulations.

## 6. Existing Processes and Sources of Assurance

- 6.1 The Council's Constitution contains the relevant statutory requirements for Internal Audit, and identifies the s151 Officer. Responsibilities of managers in relation to the management of risk and fraud are also included within the Constitution.
- 6.2 Audit and Risk Management follow the CIPFA Code of Practice for Internal Audit in Local Government 2006 which covers the following areas:
- Scope of Internal Audit
  - Independence
  - Ethics

- Audit Committees
- Relationships
- Staffing, Training and Continuing Professional Development
- Audit Strategy and Planning
- Undertaking Audit Work
- Due Professional Care
- Reporting
- Performance, Quality and Effectiveness

- 6.3 In addition, members may gain assurance on the effectiveness of the system of internal audit from a number of other sources, including:
- The Constitution (overall governance arrangements)
  - Management Structure (Directors Assurance Statements)
  - Audit Committee (terms of reference)
  - Audit Commission (CPA and Use of Resources reviews)
  - External Audit reports (Annual Audit and Inspection Letter)
  - Annual Internal Audit Report
  - Training provided (e.g. briefing sessions for Audit Committee).

## **7. The Independent Review**

- 7.1 In order to comply with the Accounts and Audit Regulations, arrangements were made between the London Borough of Haringey (LBH) and the Royal Borough of Kensington and Chelsea (RBKC) to carry out reciprocal peer group reviews of compliance with the standards set out in the CIPFA Code of Practice for Internal Audit in Local Government in the UK 2006.
- 7.2 The approach was developed with reference to appropriate standards and available guidance and a Terms of Reference for the review was agreed. A copy of the Terms of Reference is included at Appendix A.
- 7.3 In order to reach an opinion, the Internal Audit function at LBH was compared against the requirements of the CIPFA Code of Practice. A visit to LBH's Internal Audit department was made by RBKC and evidence of compliance against the CIPFA Code of Practice checklist was reviewed.
- 7.4 Based on the review undertaken, the Haringey's Internal Audit function was found to comply with the CIPFA Code of Practice for Internal Audit in Local Government in the UK (2006).
- 7.5 RBKC issued a report on their findings, which is attached at Appendix B. The report details the work undertaken and, although no high priority recommendations were made, identifies some areas for improvement in order to fully meet the CIPFA Code of Practice and Accounts and Audit Regulations.
- 7.6 In order to address these, an action plan has been drawn up and is attached at Appendix C for approval.

## APPENDIX A

# INDEPENDENT REVIEW OF INTERNAL AUDIT (2006/07) - TERMS OF REFERENCE

The terms of reference for undertaking an independent review of the arrangements made by the Authority in their provision of an effective internal audit function are set out below. This review will concentrate on the position of internal audit within the Authority and their performance / outcomes during 2006/07.

### 1. OVERALL OBJECTIVES

**Objective1:** To determine and assess the performance and effectiveness of the internal audit function against professional and local standards.

**Objective2:** To identify good practice and make recommendations for ensuring that the Authority's internal audit function is continuously seeking to improve its service and adds value as well as contributes to the organisation's strategic objectives / priorities and the effectiveness of and internal control framework.

**Objective 3:** To provide independent assurance to members, management and the authority's residents, key partners/stakeholders as to the effectiveness of internal audit and the internal control framework.

### 2. OUTCOMES

To provide a report to the s151 officer and develop a programme and action plan for addressing any weaknesses identified. The report and action plan will be reported to the Authority's relevant Committee and be used as evidence in support of providing assurance on the Council's overall governance arrangements and the system of internal control including the drawing up of the Authority's Statement of Internal Control (SIC).

### 3. BACKGROUND

This review is commissioned by the Authority's s151 officer in response to requirement under the Accounts and Audit regulations 2003 (as amended in 2006) to conduct an annual review of the effectiveness of its system of internal audit.

For the purposes of this review, proper practices in relation to internal audit relate to CIPFA's 2006 Code of Practice for Internal Audit in local government in the UK as supplemented by local standards. These standards define the way in which the internal audit service should be established and should undertake its functions. They apply equally to internal audit services provided by in-house audit units; or those provided by external contractors who provide either partial services in support of an in house team or the whole internal audit service

The annual review of the effectiveness of the system of internal audit is to be informed by several sources including reviews undertaken by external audit and/or other external inspections.

### 4. APPROACH AND SCOPE OF THE REVIEW

This review is to be undertaken by appropriately qualified and independent "reviewers". Such reviews are undertaken at least once a year and are based on 11 standards as promoted by CIPFA. In particular, the review will draw heavily on

**INDEPENDENT REVIEW OF INTERNAL AUDIT (2006/07) - TERMS OF REFERENCE**

the CIPFA Checklist – compliance with the code which is to be completed by the Authority’s Internal Audit/Head of Internal Audit. The completed checklist and accompanying evidence is then to be independently reviewed, evaluated and reported upon in terms of forming an opinion to the S151 officer as to the performance and effectiveness of the internal audit function. Where appropriate, key officers of the Authority will be interviewed. In addition, relevant evidence will be requested and examined. Client surveys/compliance testing is not being undertaken as part of this review.

Specific emphasis will be placed on the following areas:-

- The terms of reference for the internal audit service
- The independence and objectivity of internal audit
- The efficiency and effectiveness of the approach adopted in formulating the audit strategy and plans
- Compliance with CIPFA and local standards including accompanying guidance e.g. audit manual
- The achievement of key performance standards / indicators
- The adequacy and mix of resources to deliver its work & development/ improvement plans and programmes
- The reporting arrangements to management and members

**5. REPORTING ARRANGEMENTS**

Upon completion of this review, an exit meeting will be held with the nominated officer of the Authority, following which a draft report will be presented for consideration/comment to the section 151 officer.

**6. WORK PLAN / COST**

The proposed work plan is set out below:

	<b>Deadline</b>
• Planning	End March
• Interviews (where appropriate)	End April
• Evaluation	End April
• Feedback & Report (Including interim report at the end of April 2007)	End May

The review is estimated to take approximately 2-4 days depending upon the need to undertake interviews/seek clarification or require further evidence. The cost is to be met through a reciprocal arrangement with another local authority.

Signed: (S151 officer)  
Date:

Signed: (Head of Audit)  
Date:

***London Borough of Haringey***  
***Review of the Effectiveness of the System of Internal***  
***Audit***  
**FINAL AUDIT REPORT**

**May 2007**

**Report circulated to:** Anne Woods – Head of Audit and Risk Management  
LB of Haringey

**Prepared by:** Steve Armstrong – Audit Manager  
Royal Borough of Kensington and Chelsea

<b>TABLE OF CONTENTS</b>	<b>Page</b>
<b>EXECUTIVE SUMMARY</b>	3
<b>APPENDIX A</b> Summary of findings of the review	

## **EXECUTIVE SUMMARY**

1. The Accounts and Audit Regulations 2003, as amended by the Accounts and Audit (Amendment) (England) Regulations 2006, requires that a "relevant body shall maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with the proper internal audit practices". These regulations also require that provision for Internal Audit must be made in accordance with the CIPFA Code of Practice for Internal Audit in Local Government in the UK 2006.
2. Regulation 4 of the Accounts and Audit Regulations (2003) required audited bodies to conduct a review at least once a year of the effectiveness of its system of internal control and publish a statement on internal control (SIC) each year with the authority's financial statements.
3. The Accounts and Audit (Amendment) (England) Regulations 2006 came into force on 1 April 2006. Whilst many of the amendments clarify or correct elements of the 2003 Regulations, two of the amended regulations in particular have an impact on the process for preparing the SIC:
  - **Regulation 4** requires the findings of the review of the system of internal control to be considered by a committee of the relevant body, or by members of the body meeting as a whole.
  - **Regulation 6** requires bodies to review the effectiveness of their system of internal audit once a year and for the findings of the review to be considered by a committee of the body, or by the body as a whole, as part of the consideration of the system of internal control referred to in regulation 4.
4. To comply with these requirements arrangements have been made with the London Borough of Haringey to carry out reciprocal peer group reviews of compliance with the standards set out in the CIPFA Code of Practice for Internal Audit in Local Government in the UK 2006.
5. This report details the results of the review carried out by the Royal Borough of Kensington and Chelsea's Internal Audit, of the effectiveness of the London Borough of Haringey's system of internal audit.
6. In order carry out this review Internal Audit at the London Borough of Haringey was compared against the requirements of the CIPFA Code of Practice for Internal Audit. The reviewer visited Haringey's Audit department and compared evidence of compliance against the CIPFA Code of Practice checklist. The Code of Practice comprises the following eleven standards and the checklist addressed all of these detail to ensure compliance:



- Scope of Internal Audit
  - Independence
  - Ethics for Internal Auditors
  - Audit Committees
  - Relationships
  - Staffing, Training and Continuing Professional Development
  - Audit Strategy and Planning
  - Undertaking Audit Work
  - Due Professional Care
  - Reporting
  - Performance, Quality and Effectiveness
7. A detailed summary of the findings of the review are attached at Appendix A. No high priority recommendations were made as part of this review. **The London Borough of Haringey's system of internal audit was found to be compliant with the CIPFA Code of Practice for Internal Audit in Local Government in the UK 2006.**
8. A small number of areas for development were identified as part of this review and recommendations were made to address these issues. These are summarised below:
- Head of Audit should report in own name to Audit Committee.
  - Declaration of interests should be formally taken into account as part of planning process.
  - The Audit Committee should regularly review it's own remit and effectiveness.
  - Relations with other regulators and inspectors should be defined.
  - The Audit Strategy should include the resources and skills required for it's delivery.
  - An access policy should be developed and documented in respect of audit files and records.
  - The annual report to support the Statement on Internal Control presented to the Audit Committee should include a comparison of the actual work undertaken with that planned

**CIPFA Code of Practice - Standards**

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>1. Scope of Internal Audit</b></p> <ul style="list-style-type: none"> <li>•Terms of reference</li> <li>•Scope</li> <li>•Responsibilities in respect of:                             <ul style="list-style-type: none"> <li>-Other organisations</li> <li>-Fraud and corruption</li> </ul> </li> </ul>	<p>1.1 Terms of reference reflecting the current Code of Practice were approved by the Audit Committee on 26 April 2007.</p> <p>1.2 The scope of audit work takes into account risk management processes and wider internal control.</p> <p>1.3 The terms of reference define audit responsibilities in relation to fraud and consultancy work.</p>	
<p><b>2. Independence</b></p> <ul style="list-style-type: none"> <li>•Organisational independence</li> <li>•Status of Head of Internal Audit</li> <li>•Independence of individual internal auditors</li> <li>•Independence of internal audit contractors</li> <li>•Declaration of interest</li> </ul>	<p>2.1 Internal Audit is independent of the activities it audits.</p> <p>2.2 The Head of Audit has direct access to those charged with governance, members and officers as necessary.</p> <p>2.3 Reports are in the Head of Audit's own name to management however not to the Audit Committee.</p> <p>2.4 No conflict of interests between operational responsibilities and audit was found.</p> <p>2.5 Auditors are required to declare interests however these are not formally taken into account as part of the planning process.</p>	<p>Head of Audit should report in her own name to Audit Committee.</p> <p>Declaration of interests should be formally taken into account as part of the planning process.</p>

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>3. Ethics</b></p> <ul style="list-style-type: none"> <li>• Integrity</li> <li>• Objectivity</li> <li>• Competence</li> <li>• Confidentiality</li> </ul>	<p>3.1 Staff are regularly reminded of their ethical responsibilities.</p> <p>3.2 Internal Audit has established an environment of trust, confidence and confidentiality.</p> <p>3.3 Staff rotation is part of normal processes.</p> <p>3.4 The Head of Audit ensures that staff have sufficient knowledge of the organisation and specific audit area in order to fulfil the scope of audit work.</p>	
<p><b>4. Audit Committee</b></p> <ul style="list-style-type: none"> <li>• Purpose of the Audit Committee</li> <li>• Internal Audit's relationship with the Audit Committee</li> </ul>	<p>4.1 The Audit Committee approves and monitors Internal Audits terms of reference, strategy and plan and monitors progress.</p> <p>4.2 The Head of Audit attends the Audit Committee meetings, reports on the outcome of internal audit work, identifies necessary changes to the audit plan, and presents an annual report and opinion or assurance on the internal control and risk management framework. However the Committee do not review their own remit and effectiveness.</p> <p>4.3 The Head of Audit has the facility to meet privately with the Committee.</p>	<p>The Audit Committee should regularly review it's own remit and effectiveness.</p>

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>5. Relationships</b></p> <ul style="list-style-type: none"> <li>•With management</li> <li>•With other internal auditors</li> <li>•With external auditors</li> <li>•With other regulators and inspectors</li> <li>•With elected Members</li> </ul>	<p>5.1 Good working relationships have been defined and established with management, external audit and elected members.</p> <p>5.2 Relationships with other regulators and inspectors have not been as well explored.</p>	<p>Relations with other regulators and inspectors should be defined.</p>
<p><b>6. Staffing, Training and Development</b></p> <ul style="list-style-type: none"> <li>•Staffing</li> <li>•Training and CPD.</li> </ul>	<p>6.1 Internal Audit are appropriately staffed to achieve their objectives and comply with the Code standards.</p> <p>6.2 Individual training and development plans have been agreed through the appraisal process and are being delivered.</p> <p>6.3 Professional staff are required to complete CPD.</p>	

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>7. Audit Strategy and Planning</b></p> <ul style="list-style-type: none"> <li>•Strategy</li> <li>•Planning</li> <li>•Adherence to the Standard</li> </ul>	<p>7.1 The Audit Strategy complies with the Code of Practice and has been formally approved by the Audit Committee. It is reviewed annually, however the resources and skills required for it's delivery are not specified in the strategy.</p> <p>7.2 The Audit Plan has been prepared in accordance with the strategy and was approved by the Audit Committee. The corporate risk register has been used as the basis of the plan. The Head of Audit has also carried out a risk assessment.</p> <p>7.3 Stakeholders were consulted on the plan.</p>	<p>The Audit Strategy should include the resources and skills required for it's delivery.</p>
<p><b>8. Undertaking Audit Work</b></p> <ul style="list-style-type: none"> <li>•Planning</li> <li>•Approach</li> <li>•Recording Audit Assignments</li> </ul>	<p>8.1 An appropriate audit brief is prepared and agreed with management for each audit.</p> <p>8.2 A risk-based approach is used and issues are discussed with management as they arise.</p> <p>8.3 Standards of working papers are specified and checked as part of the file review.</p> <p>8.4 An adequate document retention policy is in place, however there is not a documented access policy.</p>	<p>An access policy should be developed and documented in respect of audit files and records.</p>

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>9. Due Professional Care</b></p> <ul style="list-style-type: none"> <li>•Responsibilities of the individual auditor</li> <li>•Responsibilities of the Head of Internal Audit</li> <li>•Head of Internal Audit reviews all audit files and reports.</li> <li>•Appraisal and training</li> </ul>	<p>9.1 All internal auditors are aware of their individual responsibilities for due professional care, and arrangements are in place to monitor this.</p> <p>9.2 Work is assigned so as to avoid potential conflicts of interest.</p> <p>9.3 Procedures and policies are in place for the disclosure of fraud, corruption or improper conduct e.g. Anti-Fraud strategy and Whistle-blowing policy.</p>	

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>10. Reporting</b></p> <ul style="list-style-type: none"> <li>•Reporting on audit work</li> <li>•Annual reporting</li> </ul>	<p>10.1 Standards have been set-out for audit reports, and each report gives an opinion on the control environment and risk exposure.</p> <p>10.2 Draft reports are discussed with management and action plans agreed in response to recommendations made.</p> <p>10.3 Assurances are sought from managers on delivery of agreed actions and an escalation procedure has been defined and is used as appropriate.</p> <p>10.4 Issues are referred as necessary, to ensure that risk registers are up-dated.</p> <p>10.5 An annual report to support the Statement on Internal Control is presented to the Audit Committee. The report includes the opinion on the control environment and any qualifications to that opinion. The work on which the opinion is based is set out in the report and significant issues are highlighted. The report does not compare the actual work undertaken with that planned.</p>	<p>The annual report to support the Statement on Internal Control presented to the Audit Committee should include a comparison of the actual work undertaken with that planned.</p>

<b>2006 Code standard</b>	<b>Evidence of Achievement</b>	<b>Areas for development</b>
<p><b>11. Performance, quality and effectiveness</b></p> <ul style="list-style-type: none"> <li>•Principles of performance, quality and effectiveness</li> <li>•Quality assurance of audit work</li> <li>•Performance and effectiveness of the internal audit service</li> </ul>	<p>11.1 Policies and procedures are defined in the audit manual.</p> <p>11.2 The Head of Audit has adequate arrangements in place to assess the performance and effectiveness of each audit and of the service as a whole.</p> <p>11.3 Audits are assigned according to the skills, experience and competencies required for the work. Audit work is appropriately supervised and monitored throughout.</p> <p>11.4 A performance management and quality assurance programme is in place.</p> <p>11.5 Client feedback forms are issued with each final report and are summarised in the annual report.</p> <p>11.6 Arrangements have been made for periodic reviews to ensure compliance with the Code of Practice and the audit manual and processes.</p>	



## INTERNAL AUDIT REVIEW OF EFFECTIVENESS 2006/07 – ACTION PLAN

Recommendation	Response	Responsibility & Implementation Date
Head of Audit should report in their own name to the Audit Committee.	Agreed. Arrangements in place.	Head of Audit June 2007
Declaration of interests should be formally taken into account as part of the planning process.	Agreed. Will be completed formally for 2008/09 audit plan. Review of declarations will take place to ensure any risks identified are appropriately included in the 2007/08 annual audit plan	Head of Audit/Deloitte & Touche July 2007
The Audit Committee should regularly review its own remit and effectiveness.	Agreed. A review of the Audit Committee's remit and effectiveness will be undertaken during 2007/08.	Head of Audit/Audit Committee October 2007
Relations with other regulators and inspectors should be defined.	Agreed. The relationships with other regulators and inspectors will be formally defined in a protocol and will be included in the audit manual.	Head of Audit August 2007
The Audit Strategy should include the resources and skills required for its delivery.	Agreed. The Audit Strategy will be updated to reflect the agreed resource and skills mix.	Head of Audit September 2007
An access policy should be developed and documented in respect of audit files and records.	Agreed. A formal access policy will be documented which complements the existing procedures and will be included in the audit manual	Head of Audit August 2007
The annual report to support the Statement on Internal Control presented to the Audit Committee should include a comparison of the actual work undertaken with that planned.	Agreed. Completed for the 2006/07 annual internal audit report.	Head of Audit June 2007