

**Manchester City Council
Report for Information**

Report to: Audit Committee - 26 March 2015

Subject: Annual Review of the System of Internal Audit 2014/15

Report of: City Treasurer

Summary

In accordance with the requirements of the Accounts and Audit Regulations 2011 the Council conducts an annual review of the effectiveness of its system of internal audit to be considered as part of its governance assurance processes, including the production of the Annual Governance Statement.

The report demonstrates that the Council has an effective system of internal audit including a policy framework, internal audit function, Audit Committee and effective management engagement.

Recommendations

Members are requested to consider and comment on the Annual Review of the System of Internal Audit 2014/15.

Wards Affected:

None

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Background documents (available for public inspection):

Internal Audit Annual Plan 2014/15 (June 2014)
Internal Audit Annual Report 2013/14 (June 2014)
Head of Internal Audit Annual Opinion 2014/15 (March 2015)

Manchester City Council Annual Review of the System of Internal Audit 2014/15

- 1.1 The Accounts and Audit Regulations 2011 require that “a larger relevant body (*the Council*) must, at least once in each year, conduct a review of the effectiveness of its internal audit” and confirms that the findings of the review “must be considered as part of the consideration of the system of internal control”. Internal Audit is defined as the means by which the Council assesses its governance and assurance requirements, ensuring that an effective internal control system is in place. Outcomes from the current governance processes are being evaluated and will be reported in the Annual Governance Statement.
- 1.2 To address the Accounts and Audit Regulations requirement, an assessment of Internal Audit has been carried out and is presented for consideration by those tasked with completion of the Annual Governance Statement and by the Audit Committee. The review was overseen by the City Treasurer and the report is presented for Audit Committee consideration and comment.

2 Current Arrangements for Internal Audit

- 2.1 A dedicated Internal Audit Section forms part of the system of internal audit in the Council. The Section is part of the Internal Audit and Risk Management Division of the Corporate Services Directorate. It is led by the Head of Internal Audit and Risk Management. It has links with the Risk and Resilience, Insurance and Claims and Health and Safety sections which form the Division and works closely with others in the Council tasked with governance, assurance and risk management. Whilst part of a wider Division, the Section retains its own identity as Internal Audit for the Council being managed by the Audit Manager.
- 2.2 The Head of Internal Audit and Risk Management reports directly to the City Treasurer but also has direct access to the Chief Executive, Executive Member for Finance and Human Resources and the Audit Committee.
- 2.3 At the start of 2014/15 the in-house team comprised 18 approved posts plus the Head of Internal Audit and Risk Management. One auditor post within the structure remained vacant during the year. The team delivered work for the Council and some external organisations including the Greater Manchester Combined Authority within that resource.
- 2.4 The Vision for Internal Audit was described in the Divisional Business Plan and Annual Audit Plan 2014/15. The Internal Audit Service Terms of Reference (TOR) outlines the status of the Section and define the principles of how it operates within the Council. The TOR provides appropriate arrangements to ensure that the Section is sufficiently independent and objective and that there is access to all information and people required to discharge its responsibilities.
- 2.5 Arrangements for counter fraud work are defined in the Council’s policies and procedures for Anti-Fraud and Whistleblowing and these were reported to the

City Treasurer and Audit Committee in the Annual Fraud Report in July 2014. During the year additional funding was obtained from DCLG to further develop and enhance the Council's approach to Counter Fraud and this includes collaboration opportunities with GMCA and Bolton Council. Progress in this area will be reported to Audit Committee in the coming year and quarterly to DCLG.

- 2.6 To examine the effectiveness of the Internal Audit Section for the past year this annual review considered several key elements and assessed their contribution to enabling the Section to fulfil its responsibilities. These were:
- The structure and resourcing level, including qualifications and experience of the audit team.
 - The extent of conformance with the PSIAS in producing quality work.
 - Ensuring audit work was successfully delivered in the most appropriate areas on a prioritised (risk) basis.
 - The overall performance of the audit team.

3 Resourcing, Qualifications and Experience

Resourcing

- 3.1 During 2014/15 there were no staff changes within the structure. Available resources were reduced by 0.8 FTE as three staff work on reduced hours arrangements and there was a vacant audit post. As a result there were on average 16.2 audit staff available for audit work during the year and this was assigned to the risk based audit plan.
- 3.2 Audit work was actively managed within the resources available with scope and timing reviewed and agreed with clients with progress toward delivery reviewed regularly and reported to management and Audit Committee. The Head of Internal Audit and Risk Management and Audit Manager took on responsibility for some referred work and investigations where appropriate to support delivery and auditors were assigned flexibly in year working within different teams based on priority issues arising. Alternative means for gaining assurance were also used where appropriate to support audit opinions and advice and guidance offered where a full audit was not deemed appropriate.
- 3.3 The audit plan remains on target for completion by year end and there will be minimum need to carry forward audit work from 2014/15 into next year except where draft reports still require management responses to enable final reports to be issued or where timing and/or scope changes agreed with the business have moved some work into April. A full outturn will be reported in June 2015.

Structure

- 3.4 The structure of the Section in 2014/15 remained as in the previous year. This reflected the Council at Strategic Director level and continued to allow for close client liaison from Lead Auditors. We consider this approach remained successful and the Section continued to receive positive feedback from managers on this approach. However there is a need for some staff rotation

for development purposes and to maintain objectivity and it is planned to move Lead Auditor responsibilities in the coming year which will require management support and appropriate training.

Audit and Risk Management

- 3.5 Being part of the Audit and Risk Management Division enabled the objectives for Internal Audit to be effectively articulated through the business planning process and demonstrated in business plans. Key priorities, options for development and service delivery, business objectives, assessments of performance and workforce plans are described in the Audit and Risk Management business plan which has been used to inform the development of section, team and personal objectives and provide the basis for performance management and improvement. Shared intelligence and some joint working has been undertaken to improve the assurance and support services offered to the business and to schools while maintaining the Internal Audit's distinct identity.

Training and Experience

- 3.6 The training and development approach encourages development through both the career grade auditor scheme and continuing professional development. This is managed through the Council appraisal system and workforce development. In the year one trainee auditor completed the examination stage of the IIA Diploma and one completed the IIA Certificate. One member of staff is working toward the IIA diploma. Staff were encouraged to undertake continuing professional development and were able to undertake relevant courses or attend conferences in Internal Audit; Management and Leadership; Council developments and systems. Individuals keep records of their continuing professional development based on their professional body requirements.
- 3.7 The following information about qualifications and experience of staff available for audit work demonstrates the experience and qualification mix.

Experience 2014/15

| Auditing Experience | All Auditing | % | Local Govt Auditing | % |
|---|---------------------|----------|----------------------------|----------|
| Up to 1 year | 0 | 0 | 0 | 0 |
| 1 to 2 years | 4 | 22% | 4 | 22% |
| 2 to 5 years | 0 | 0 | 0 | 0 |
| 5 to 10 years | 4 | 22% | 8 | 45% |
| Over 10 years | 10 | 56% | 6 | 33% |
| Total Staff | 18 | | 18 | |
| Includes Head of Internal Audit & Risk Management but excludes one vacancy. | | | | |

Qualifications

Accountants (CIPFA, FCCA, ICAEW)

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| | |
|--|-----------|
| Institute of Internal Auditors - fully member | 9 |
| Institute of Internal Auditors – part qualified or Audit Certificate | 6 |
| Total | 18 |

- 3.11 The skills level available remained high based on the substantial number of staff with over 10 years experience and competencies in specific areas.
- 3.12 At 31 March 2015 the Section will have one auditor vacancy and an equivalent of 0.8 full time post will remain unresourced based on reduced hours working arrangements. Further impact on resources will occur due to two maternity absences through out the coming year. These reductions will be more than offset by approved increases in planned resources agreed in the service budget for 2015/16 with two additional investigation posts, an auditor post and counter fraud posts funded by CLG grant to be filled in year. Whilst the emergent plan does not reflect this planned growth in capacity, it is intended that appropriate resource be identified and staff appointed in quarter one of 2015/16 so the final plan should reflect the increased resource position.
- 3.13 Options for the resourcing of additional posts for counter fraud work and to appoint to the vacant auditor post will be explored and addressed in the early part of 2015/16.

4 Conformance with UK Public Service Internal Audit Standards (PSIAS)

- 4.1 Internal Audit carried out a self assessment against the key elements of the PSIAS. For 2014/15 this demonstrated that that the Section was meeting 92% of the applicable Code requirements fully and 4% partially met. The areas This is slightly higher than last year but the areas still to be met which will be part of the Audit Manager’s annual objectives for 2015/16 are as follows:
- There is further work to be done to enhance and formalise current processes and documents and to develop and agree an improvement plan known as the Quality Assurance Improvement Programme (QAIP).
 - Arrangements for a five yearly independent assessment of Internal Audit have to be finalised. Peer reviews by other Internal Audit Services in Core Cities and AGMA are being considered to support part of this process but this is not a pressing requirement.
 - The text in the Internal Audit Charter needs to be updated to reflect all the requirements of the Standards.
- 4.2 All staff provided declaration of interest statements and signed the ethics and behaviours statement for the PSIAS in 2013/14 and the Head of Internal Audit and Risk Management is looking to align this process across the Division this year. The declaration process enables management to ensure that there is sufficient information from which to address any potential conflicts of interest which may affect audit activities. Staff remain obliged to raise any conflicts or issues with management during the year and records are maintained for this purpose.
- 4.3 Quality of audit work was actively managed in year through formal review. The achievement of quality standards enabled the Head of Internal Audit and Risk

Management to confirm that work was done in conformance with PSIAS. Individual audits had agreed and clear plans and scope; activity was reviewed and assessed for its effectiveness during and after completion of work; and customer feedback was received on some draft reports and from post audit questionnaires.

- 4.4 External Audit continued to provide positive assurance over the approach to Internal Audit. As a result of their last review they confirmed that they could take assurance over the quality and extent of audit work done in 2013/14 including assurance over the core financial systems activity and agreed to the approach taken for the work in the 2014/15 audit plan. Their review of work on the 2014/15 programme is due for completion in March 2015. Liaison with the external auditor was productive and audit plans were co-ordinated within this process. The two services continued to share information and to use this to inform risk assessments and direct audit activity.

5 Ensuring the Effective Prioritisation of Audit Work

- 5.1 Prioritisation of the work of the Section is achieved by the development and delivery of an annual, risk based audit plan. This describes the assurance plans for the Section and includes some capacity for flexibility to adjust to changing circumstances and for demand led and urgent work if appropriate. The plan is based on a mix of different types of audit and investigation work to ensure that assurance over the Council's systems of governance, risk management and internal control is obtained from a number of different directions and sources.
- 5.2 The Section's methodology for establishing audit priorities is aligned with the Council's governance and risk management systems. Audit plans are developed through an assessment of risk and assurance needs to support the Council's overall objectives. The approach is set out in the Emergent and Final Audit Plans presented and agreed by the Audit Committee.
- 5.3 It is considered that the 2014/15 Audit Plan represented a reasonable view of critical areas for audit review and assurance needs when it was constructed and agreed with senior management and Audit Committee and is mainly on track for delivery by year end. It is considered that it was based on reasonable estimates of available resources. There have been some reported changes based on organisational change or matters of timing. The emergent plan for 2015/16 will be presented to Audit Committee for consideration in March 2015 and will be finalised in June 2015.

6 Performance Measures

- 6.1 Performance management of the Section and for individual auditors is focused on deployment of auditor time to best effect. This has three main elements related to how much time is spent auditing, completion of audits within set timescales and effectiveness of time deployed. The key deliverable for is the completion of the plan within the year. Performance and progress are monitored through KPIs. These are agreed across Core Cities and allow for

benchmarking to assess effectiveness. Comparative figures are used to consider areas for closer review.

6.2 Key performance measures for the Section over the last five years are:

| | Target | 2014/15 | 2013/14 | 2012/13 | 2011/12 | 2010/11 |
|--|---------------|----------------|----------------|----------------|----------------|----------------|
| Days spent on audit work as % of available days | 76% | 91% | 86% | 81% | 83% | 82% |
| Audit reports and other outputs issued in year | 140 | 96 | 111 | 109 | 219 # | 254 # |
| Actual time on audits compared to original estimates | 110% | 134% | 98% | 109% | 121% | 112% |
| Draft reports issued within 3 months of audit start | 90% | 77% | 62% | 73% | 91% | 85% |

Included FMSIS reports that ceased in 2011/12

6.3 The key performance measures show that the percentage of available days spent directly on audit work was above target at 91% which is a positive indicator of how available time was utilised. This was due to continued active management of time and effective scoping and agreed timing for audit work which reduced delays and any down time.

6.4 There were 96 audits issued with other work still in progress based on the original plan. Some audits had been cancelled or deferred based on business needs and timescales. A full outturn will be reported in June 2015 against the agreed audit plan.

6.5 The percent of time against plan was over the target at 134% based on a small number of jobs running significantly over estimated budgets established at the start of reviews. A major contributor to this is investigations where it can be difficult to determine in advance the amount of time required for completion and where issues identified can lead to the need for further work. For 2015/16 we will revisit the planning and allocation approach for these investigations to ensure budgets are reprofiled on a timely basis as the scope and required scale of work emerges. We will also continue to focus support and challenge on the delivery of wider audit work to agreed time and budgets.

6.6 There was positive feedback on a number of specific jobs during the year where clients provided the Head of Audit and Risk Management with a number of positive comments about who found the flexibility that the audit

team had shown in supporting them to address emerging issues and in adapting audit plans to better address business risk.

- 6.7 The very low level of CSQ returns meant there was no meaningful data for this indicator and this will be reconsidered in the coming year. This is an area which other authorities also struggle to define with a quantitative measure and we propose to explore with AGMA and Core Cities to assess alternatives.
- 6.8 The elapsed time indicator is an assessment of the timeliness of the audit activity from start to draft report. This had improved from last year to 77% of reports issued within three months of audit start dates but still below target. This is was due to some slow client responses and we continue to work with managers to ensure that agreed report response times are met.
- 6.9 No concerns have been raised in relation to the application of professional standards for audit work and there have been no formal complaints about the Service.
- 6.10 Internal Audit costs and coverage are benchmarked with other Councils through CIPFA as well as through the Greater Manchester and Core Cities networks. The latest available figures for example showed that the cost of Internal Audit in Manchester, as a percentage of Council turnover, remains below average. There are a range of other figures and measures that the service uses to inform business planning and to ensure that ongoing actions are taken to deliver and demonstrate value for money in the work done.

Implementation of Recommendations

- 6.11 The process for monitoring implementation of recommendations built on improvements last year and with regular contact with managers the service ensured that action was taken on high risk issues though rates of implementation fluctuated in year and remained below target. Reasons for delays were generally understood and alternatives sought where possible.
- 6.12 Internal Audit used the Council's quarterly reporting process to ensure assurance reports were shared regularly with Directorate Management Teams and with SMT bringing together issues from audit and other risk services to consolidate key risks and actions required. This process continues to helped ensure that the time spent by the Service is targeted on key issues and that appropriate support and advice is offered at the right time.
- 6.13 Audit Committee were provided with regular updates from the Section during the year and this offers the opportunity to challenge managers and Internal Audit on progress and outcomes. This included asking senior managers to provide business updates as necessary where there was a significant risk or concern. To enhance this process Strategic Directors or other appropriate managers will be asked to attend Audit Committee to discuss limited assurance reports and explain how exposure to risk is being addressed.

7 Audit Committee

- 7.1 The system of Internal Audit includes the role of the Audit Committee and in particular its role in the receipt and evaluation of audit reports, both in terms of assurance opinions and in ensuring that appropriate arrangements are in place for the delivery of an effective service. The arrangements for the Audit Committee remained the same during 2014/15.
- 7.2 Audit Committee requested that management attend to discuss any audit where limited assurance opinion has been provided in individual Audit reports. This is a positive step being taken by the Committee to formally seek assurance from management over actions being taken to respond to key concerns.

8 Summary and key priorities

- 8.1 Service delivery remains a key priority in support of the Council's priorities. The Section provides advice and guidance to the business where we identify risks to delivery and help seek solutions. The Section remains on track to deliver its audit plan for the year and it is considered that the Section has a sound base for carrying out its audit activities and meeting its objectives to provide audit assurance and advisory support to the Council.

9 Conclusions

- 9.1 Members are asked to note the findings and conclusions of the 2014/15 review of the effectiveness of the system of internal audit.