**Manchester City Council
Report for Information**

Report To: Audit Committee - 5 October 2017

Subject: Review of Internal Audit and Findings of Peer Review

Report of: City Treasurer
Head of Audit and Risk Management

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. This process is designed to provide assurance to the City Treasurer, and Audit Committee in particular over the system of internal audit including the role, function and performance of the internal audit service.

For 2016/17 the review has been informed by an internal review and an external quality assessment ("EQA") conducted by Liverpool City Council that tested service conformance with the requirements of the Public Sector Internal Audit Standards.

During 2017 the Council's internal audit service also embarked on a programme to review and refresh the internal audit approach and under a shared Head of Audit and Risk Management, further develop collaboration with Bolton Council and the GM Combined Authority. This report summarises progress to date and key areas of proposed development for Audit Committee consideration and comments.

Recommendations

Audit Committee is requested to:

- Consider the level of assurance provided by the review of effectiveness and management actions agreed in response to areas for development.
- Note proposals emerging from the service development programme and receive assurance over the completion of this work as part of the 2017/18 Review of Effectiveness and 2018/19 Annual Internal Audit Plan in February and March 2017.
- Review and approve the Internal Audit Charter

Wards Affected:

All

Contact Officers:

Carol Culley
City Treasurer
Tel: 0161 234 3506
E-mail carol.culley@manchester.gov.uk

Tom Powell
Head of Internal Audit and Risk Management
Tel: 0161 234 5273
E-mail t.powell@manchester.gov.uk

Background documents (available for public inspection):

Documents used in the development of the assurance report include:

- Internal Audit Plan 2016/17 (July 2016 Audit Committee)
- Internal Audit Plan 2017/18 (June 2017 Audit Committee)
- Head of Audit and Risk Management Annual Opinion (June 2017 Audit Committee)

1   Introduction and Background

1.1   Internal Audit is one of the means by which the Council assesses the adequacy and effectiveness of its governance and risk management arrangements, ensuring that an effective internal control system is in place. It is a key source of independent assurance to management and Members and its work helps inform the Annual Governance Statement.

1.2   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".

1.3   The areas for development and agreed improvement actions arising from the 2016/17 review are summarised in section 2. These are based on two key sources of information.

    •   An internal review of the effectiveness of the system of internal audit including feedback from Audit Committee (section 3).
    •   Findings and actions agreed from an External Quality Assessment ("EQA") of the Internal Audit Service conducted by Liverpool City Council (section 4).

1.4   The Internal Audit Service is currently undertaking an audit development programme and a summary of key actions being progressed as part of this are set out in section 5. The development programme has been used to incorporate actions agreed in response to the EQA as well as changes requested by Audit Committee in respect of recommendation monitoring, classification of audit risks/priorities and formats for reporting to Audit Committee. This approach is being taken to ensure that all areas for development are agreed and implemented as part of a coordinated and sustainable plan.

2   Summary

2.1   The conclusion of the review is that the Council has an effective system of internal audit and effective internal audit service and that improvement actions will further strengthen arrangements to provide assurance and support for the Council's systems of governance, risk management and internal control.

2.2   In particular the EQA reported that the Service complies with the main requirements of the Public Sector Internal Audit Standards, that areas for development were in the main identified through the Service's own self-assessment and there is a service development plan already in place that will address the areas for improvement. The overall conclusion from the EQA is included at appendix 2 (paragraph 4.1).

2.3   The areas for development and agreed improvement actions arising from the internal review, EQA and Audit Committee feedback are as follows:

Area for Development (source)	Improvement Action	Ref in Report
Performance measures for the service could be improved (Self Assessment and EQA)	Measures defined as part of the service development programme by end December 2017	3.7 5.22
Executive Members notified of outstanding high risk audit recommendations (Self Assessment and EQA)	Complete – reports shared with Executive Members as requested by Audit Committee	3.10
Ensure Executive Members are provided with Audit Reports (Audit Committee request)	New format for audit Assignment and Summary reports being developed as part of service development programme. Distribution to include Executive Members from 1 April 2018.	3.10
Update Internal Audit Charter to reflect new PSIAS Standards (Self Assessment and EQA)	Updated Internal Audit Charter attached at appendix 1 for Audit Committee review and approval.	3.12 5.10
Development Quality Assurance Improvement Programme (Self Assessment and EQA)	Draft QAIP produced but will be finalised following completion of Audit Development Programme to ensure that it reflects the revised audit approach by end December 2017.	3.13 5.21
Recording of staff Continuing Professional Development (EQA)	Learning and development plan in place for service but approach to recording of all CPD to be included in Quality, Ethics and Standards element of Audit Development Programme to commence from 1 April 2018.	5.18
A formal audit of risk management arrangements has not been completed in the last three years (EQA)	Audit of risk management to be included in Annual Plan for 2018/19 to be reported to Audit Committee in March 2018	5.27
Documentation of fraud risk, value for money and IT risk at the scoping stage of audits. (EQA)	Included in Assignment Planning element of Audit Development Programme to commence from 1 April 2018.	5.28
Some inconsistencies were noted in documenting evidence of management review. (EQA)	Included in Fieldwork element of Audit Development Programme to commence from 1 April 2018.	5.29
Need to refresh the Audit Manual to reflect the Standards. (EQA)	Updated manual finalised as part of the Audit Development Programme to commence from 1 April 2018.	5.30
Engagement results (reports) do not include narrative regarding the limitations on distribution. (EQA)	Updated narrative will be considered as part of the Assignment Reporting element of the Audit Development Programme to commence from 1	5.32

Area for Development *(source)*	Improvement Action	Ref in Report
	April 2018.	

3   Internal Review of the System of Internal Audit

Structure, Staffing and Skills

3.1   The Internal Audit Service is led by the Head of Audit and Risk Management, who performs the same role for Bolton Council and the GM Combined Authority. This arrangement supports the development of collaboration opportunities across teams and sharing of knowledge, skills and experience across the three authorities. The team includes an Audit Manager supported by six Lead Auditors with responsibilities for dedicated portfolios as follows:

- Adults, Children's, Education and Skills
- Growth and Neighbourhoods
- Corporate Core
- Procurement, Commissioning and Contracts (and GMCA)
- Counter Fraud and Irregularity
- Data, Information and Systems

3.2   The in house service comprises 18 FTE posts and is supplemented by up to 80 days per annum of specialist ICT audit support which in 2016/17 was commissioned through the Council's financial service framework. In 2016/17 the actual FTE in the service was 17 as a result of three staff working reduced hours.

3.3   The team has a rich mix of experience and qualifications. It includes four qualified accountants (CCAB), six fully qualified internal auditors (MIIA) and all other staff are part qualified members of CIPFA or the Institute of Internal Auditors. Members of the team are also qualified and certified in investigate techniques (PINS, CIPFA) and the use of data interrogation software (IDEA) and undertaken ongoing training as part of the service learning and development plan.

3.4   For 2017/18 there is one staff member on maternity leave and one vacancy held pending the outcome of the service development review. This resource reduction for 2017/18 will be offset by the commissioning of specialist, external resources to support work, particularly around risk and assurance mapping; counter fraud awareness and training; and ICT audit.

Planning, Delivery and Performance

3.5   The work of internal audit for 2016/17 was set out in an audit strategy and an annual plan approved by Audit Committee in July 2016. The approach taken is to provide a range of audit work with different scope and coverage comprising:

- Audit Opinion Reviews (c50% of plan)
- Audit Assurance Reviews (c20% of plan)
- Advice, Guidance and Support (c10% of plan)
- Counter Fraud, Probity and Investigations (c20% of plan)

3.6   Delivery and the outcomes of audit work are reported to Directorate Management Teams ("DMTs", Strategic Directors, the City Treasurer and Audit Committee on a quarterly basis. Whilst performance and impact cannot be assessed wholly on the numbers of reports issued, in 2016/17 there was an increase from the previous year, largely due to the stable staffing position as illustrated in table 1 below.

Table 1: Audit Outputs Issued at Year End

Audit Status	2016/17	2015/16
Final Reports Issued	111	79
Additional Work Issued	11	
Draft Reports Issued	8	10
Fieldwork Completed or Started	29	10
Totals	**159**	**99**
Cancelled/Deferred	16	22

3.7   From the PSIAS self-assessment and the EQA there is a recognised need to refine performance measures and performance reporting for the service. This is being progressed as part of and Ethics, Standards and Quality work stream in the service development programme.

3.8   Any complaints made against the service are addressed as part of the Council's corporate complaints process but a revised policy and supporting process has been developed in 2016/17 to ensure that any whistleblowing allegations against the service are considered by the City Solicitor. There has been three complaints in the year and one allegation linked to whistleblowing. All of these related to matters in respect of counter fraud activity. Whilst the complaints raised against the service were not upheld, appropriate learning has been reflected in changes to the service approach.

Findings and Reporting

3.9   The findings of internal audit work are confirmed in individual assignment audit reports. For all opinion audits, a clear assessment of assurance is provided from "no" to "full" and agreed actions are assigned a priority from "critical" to "minor". All final reports with agreed action plans are issued to the City Treasurer, City Solicitor and Chief Executive. Summaries and all opinions issued are reported to strategic management team and Audit Committee.

3.10   Agreed actions are followed up by internal audit on a regular basis and performance is reported to DMTs, Strategic Management Team and Audit Committee. For 2017/18 following feedback from Audit Committee the implementation of recommendations is also reported to Executive Members

and a process is being finalised to provide Executive Members with details of all audit reports and key issues arising. This is being developed alongside the redesign of reports as part of an assignment and stakeholder reporting work stream within the service development programme.

3.11   The role of the Audit Committee in considering findings and issues arising from audit reports has continued to support an effective system of internal audit. The Committee met seven times a year and considered reports from the service and the responses from management. In the last twelve months this has resulted in reports being presented to Committee from management and Executive Members in respect of ICT, highways, children's services and adult services.

Standards Compliance

3.12   The Internal Audit Section works in conformance with UK Public Service Internal Audit Standards (PSIAS). The latest self - assessment demonstrated that 95% of the applicable Code requirements were met fully and 5% partially met. This was an increase from 2015/16 as a new Internal Audit Charter was developed (attached at appendix 1 for Audit Committee approval) and an EQA was undertaken in the year.

3.13   The key area still to be developed was also noted in the EQA and relates to the enhancement of processes and documents within a Quality Assurance Improvement Programme (QAIP). This has been produced in draft and will be finalised as part of the service development programme because the QAIP will need to reflect changes arising from the review and refresh of the internal audit approach and revised internal audit manual.

3.14   The quality of audit work was actively managed in year through formal review. The achievement of quality standards enabled the Head of Audit and Risk Management to confirm that work was completed in conformance with PSIAS. Individual audits had agreed 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.

Independence and Other Responsibilities

3.15   The Internal Audit Section is part of the Audit and Risk Management Division of Corporate Services. This includes risk and resilience; health and safety; and insurance and claims. The arrangements supports effective collaboration between these teams on key risks areas and major programmes such as Our Town Hall; health and social care; and information governance. It also works closely with other services across the Core including finance, legal, procurement, HR and ICT. Whilst working collaboratively with colleagues, the Section retains its own identity and is managed by the Audit Manager. Any audit work in respect of services for which the Head of Audit and Risk Management is also responsible can be reported directly to the City Treasurer by the Audit Manager. This was acknowledged as part of the EQA.

3.16   The Head of Audit and Risk Management reports directly to the City Treasurer but also has direct access to the Chief Executive, Executive Member for Finance, ICT and Human Resources and the Audit Committee. This helps ensure independence and allows for issues to be escalated should the need arise. No such requirements arose in 2016/17.

Role of the Audit Committee

3.17   The system of Internal Audit includes the role of the Audit Committee and in particular its role in reviewing and assessing the annual audit plan, the receipt and evaluation of audit assurance and considering where appropriate arrangements are in place for the delivery of an effective service.

3.18   The Audit Committee has a thorough work programme covering reports in respect of internal audit activity, external audit, risk management, governance and financial reporting. It includes agenda items to receive assurance and updates from senior management and Executive Members and did so in respect of highways, ICT, children's services and adult's services in the last twelve months. The Committee has directed further areas for assurance in respect of outstanding audit recommendations which is now reflected in the 2017/18 audit work programme.

3.19   During 2016/17 the Audit Committee Chair attended external training arranged through CIPFA and a number of members of the Committee attended a training session on the roles of internal audit and external audit.

4   External Quality Assessment

4.1   The PSIAS require that an external quality assessment ("EQA") be conducted for principal local authorities at least every three years. The PSIAS do not prescribe how this is undertaken, but provides a framework and standards to be met for an assessment. Most local authorities have chosen to enter into a peer review process and for Manchester, this was arranged as part of the Core Cities group.

4.2   This work was conducted in late 2016 and a final report issued in April 2017. This is attached in full as appendix 2.

4.3   The external assessment concluded that "Manchester City Council's Internal Audit Service complies with the main requirements of the Public Sector Internal Audit Standards". It noted that "Areas for development have been identified through this assessment, however these were in the main identified through the self-assessment demonstrating clear self-awareness of the audit team and a commitment to continuous improvement. The team also have in place an ongoing Service Improvement Plan to further evidence this".

4.4   All the areas for development have been agreed. One was to update the Internal Audit Charter and this is included at Appendix 1 for Audit Committee review and approval. The purpose of the Charter is to confirm Internal Audit's

position within the Council and its reporting lines, authorisation of access to records, personnel and physical property relevant to the performance of audit work, and define the scope of Internal Audit activities. It required updating because it did not reflect the latest updates to expected practice as set out under the PSIAS.

4.5   Actions were also agreed to refresh aspects of the audit approach which are being addressed holistically as part of the service development programme referred to in section five below. The actions largely relate to ensuring that existing practice is recorded as part of the audit planning, fieldwork and reporting processes.

4.6   A key point from the review is to develop a Quality Assurance Improvement Plan ("QAIP"). This has been produced in draft but will only be completed once the revised audit approach and audit manual have been finalised. This is ongoing and is scheduled for completion by December 2017.

5   Audit Development Programme

5.1   In 2016/17 the Head of Audit and Risk Management commissioned an external company (Risk and Assurance Insights) to help design a programme of development work across the audit functions in Manchester, Bolton Council and the GM Combined Authority. The aim of the support was to help develop a common audit strategy and approach across the three authorities, explore collaboration opportunities and develop more efficient and impactful ways of working. This programme is also being used to implement all the areas for development identified in the Manchester EQA and feedback from Audit Committees.

5.2   This programme has involved engagement of all audit staff across the three authorities through a series of workshops and events, exploring principles such as risk and assurance mapping, development of lean audit methodologies and the enhancement of reporting arrangements. Officers from across the three teams have been involved in nine work streams to co-design a new, common audit approach covering the following areas:

· Quality, Ethics and Standards
· Risk and Assurance Mapping
· Annual Audit Planning
· Assignment Planning
· Fieldwork and Testing
· Assignment Reporting
· Follow Up of Recommendations
· Metrics and Performance Management
· Stakeholder Reporting

5.3   This development programme will result in the establishment of a common set of audit principles, shared audit approach and new/amended audit management system. A draft approach for these areas will be completed for final consultation with audit teams and subsequent agreement by the

Treasurers of Manchester, Bolton and the GMCA by the end of December. The intention is for the common approach to be implemented for 2018/19.

5.4   The programme has also taken into account feedback and actions requested by from Audit Committee. In particular the new approach will reaffirm the new process for recommendation monitoring and reporting, ensure onward reporting of issues and risks to Executive Members and will result in clearer summary reporting to Audit Committee.

5.5   The key changes likely to emerge from this development programme are:

- A single set of simple quality and performance standards for onward reporting to the City Treasurer and Audit Committee.
- Development of assurance maps for Head of Service and Directors to support their assessment of sources of assurance, guide improvement actions and help inform internal audit planning. This links into the sources of assurance work being led by the Deputy City Treasurer and previously reported to Audit Committee as well as the Annual Governance Statement.
- Refinement of the annual audit planning process, to ensure effective engagement of key stakeholders and ensure timely approval of the annual audit plan.
- Refinement of the overall audit approach, to minimise elapsed time on audits and further enhance the efficiency of audit teams.
- New reporting formats, both for audit assignments and for key stakeholders. This will include new Executive Summaries for all reports that will be provided to Executive Members and Audit Committee as part of regular reporting.
- Simplification of language and opinions used in reports to further aid understandings and transparency of audit reporting.
- Agreed areas and approach to develop collaborative working in key risk areas such as counter fraud; information and ICT; schools and academies; and procurement, commissioning and contracts.

5.6   As part of the development programme, the Head of Audit and Risk Management is also considering the service structures for Manchester, Bolton and the GMCA, to maximise the benefits that can be derived from collaboration and will share proposals and potential options with the City Treasurer by the end of October 2017.

7   Conclusions

7.1   The internal review of the effectiveness of the system of internal audit and the EQA of the internal audit service in 2016/17 have not identified any issues of concern.

7.2   The PSIAS self-assessment process, EQA and service review have helped confirm areas for development which are being addressed as part of a development programme led by the Head of Audit and Risk Management across Manchester, Bolton and the GMCA. This programme will conclude in December 2017 and a refreshed audit approach will be established for implementation in 2018/19.

8   Recommendations

8.1   Audit Committee are requested to:

- Consider the level of assurance provided by the review of effectiveness and management actions agreed following the EQA.
- Review and approve the Internal Audit Charter
- Note proposals emerging from the service development programme and receive assurance over the completion of this programme as part of the 2017/18 Review of Effectiveness and 2018/19 Annual Internal Audit Plan in February and March 2017.

Appendix One

Manchester City Council: Internal Audit Charter

1   Introduction

1.1   This Charter sets out roles, responsibilities, accountabilities and governance structures concerning the operation of internal audit in Manchester City Council (the Council). It establishes Internal Audit's compliance with the UK Public Sector Internal Audit Standards (PSIAS), introduced with effect from 1 April 2013. The Standards encompass mandatory elements of the Global Institute of Internal Auditors International Professional Practices Framework and apply to all public sector internal audit service providers, whether in-house, shared or outsourced. A CIPFA Local Government Application Note sets sector-specific requirements for the application of the PSIAS in local government organisations.

2   Definitions

2.1   For the purpose of this Charter the following definitions of PSIAS terms apply within the Council:

- Internal Audit - 'an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives of bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.'
- Audit Committee - 'The Board'
- City Treasurer - 'Senior Management'
- Head of Audit and Risk Management - 'Chief Audit Executive'

3   Authority And Accountability

3.1   The Council's Constitution sets out Internal Audit's constitutional role and rights of access to all records, properties, physical assets and explanations from Officers in the course of its assignments. These rights are accompanied by accountability for confidentiality and safeguarding of records and information. Internal Audit has unrestricted access to senior management and to the Audit Committee, and will work with officers who are requested to assist it in fulfilling its roles and responsibilities.

3.2   The Head of Audit and Risk Management leads the Section, reporting to the City Treasurer and supporting the discharge of responsibilities for the administration of financial affairs under Section 73 of the Local Government Act 1985. The Head of Audit and Risk Management has direct access to the Audit Committee Chair, attends all meetings, reports on internal audit activity and advises on the adequacy and effectiveness of Council systems of governance, risk management and internal control. The provisions in this document enable the Head of Audit and Risk Management to deliver an

annual opinion on the Council's systems of governance, risk management and internal control.

4   Independence And Objectivity

4.1   The PSIAS define independence as "freedom from conditions that threaten the ability of the internal audit activity to carry out its responsibilities in an unbiased manner". To assist Internal Audit to carry out the role and constructively challenge senior managers of the Council, the Head of Audit and Risk Management holds a sufficiently senior position in the Council. Internal Audit independence is confirmed in the Annual Review of Effectiveness of the System of Internal Audit and Audit Committee approves, but does not direct, the annual audit plan.

4.2   Independence is primarily a state of mind and is developed by the training and development approach. Auditors challenge, on the basis of objective evidence, decisions, policies or practices they consider inappropriate or in need of improvement, no matter who is involved in decision making. It is essential for Council officers and Members to recognise Internal Audit's role and responsibilities and accept audit comment and advice in this spirit, giving a reasoned response if they take a different view.

4.3   Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the activities or processes audited. They make a balanced assessment of relevant circumstances and are not unduly influenced in forming judgments by their own interests or others.

4.4   Objectivity and independence in the provision of advice and guidance are maintained, and conflicts of interest avoided, as decision making remains with service managers. Auditors have no operational responsibility for, or authority over, activities audited and also submit declarations of interest annually, including 'nil' returns.

4.5   The Head of Audit and Risk Management also has operational responsibility for the Risk and Resilience; Health and Safety; and Insurance and Claims Services, as well as being involved in corporate boards and working groups. Given this wider role, the Audit Manager has the authority to report directly to the City Treasurer on any audit work in these areas to avoid actual or perceived risk of self-review by the Head of Audit and Risk Management.

5   Responsibilities

Internal Audit

5.1   The prime purpose of internal audit is to assure Members and senior managers over the adequacy and effectiveness of the Council's governance framework, risk management and internal control. This is achieved by working with managers to assess and improve arrangements by undertaking audit assignments, providing assurance and making appropriate recommendations

for change. Internal Audit may also provide advice and guidance to managers on specific issues subject to the availability of skills and resources. The scope of internal audit's work includes:

- All Council systems, processes, policies, plans and procedures;
- Use and safeguarding of resources and assets, including data;
- Governance and risk management processes;
- Commissioning and procurement;
- Projects and programmes; and
- Counter Fraud, including investigation of allegations of fraud and corruption.

Audit Committee

5.2   The system of internal audit includes Audit Committee's role, particularly receipt and evaluation of assurance opinions. Terms of Reference are set out in the Constitution, Part 4 Section B. The Audit Committee includes two independent members, in line with CIPFA good practice and there is a development and training process.

5.3   Key responsibilities include:

- Approval of the Annual Accounts and Treasury Management Strategy;
- Consideration of External Audit reports;
- Consideration of the review of the effectiveness of the system of internal control and the Annual Governance Statement;
- Oversight of the effectiveness of the control environment including risk management, counter-fraud and anti-corruption arrangements; and
- Review of the Council's internal audit programme and assurance reports, as appropriate, from the Head of Audit and Risk Management.

Statutory Officers

5.4   The roles and responsibilities, including delegated functions, of the Head of Paid Service, Monitoring Officer and Treasurer are set out in the Council's Constitution, Part 3, Section D 'Scheme of Delegation of Functions to Chief Officers'.

External Audit

5.5   Internal Audit works actively with the external auditor to maximise the value obtained from the total audit resource available. In addition to its financial statements work, External Audit provide assurance over Internal Audit's approach and coverage.

Counter Fraud

5.6   Managers are responsible for preventing and detecting fraud and corruption, managing associated risks through effective internal control and investigating

fraud. Internal Audit is responsible for developing the Counter Fraud Strategy including raising fraud awareness across the Council, investigating allegations and assisting managers with investigations and carrying out proactive fraud detection exercises. Suspicions of fraud or corruption may be reported directly to the Head of Audit and Risk Management under Whistleblowing and Anti-fraud and Corruption policies. Decisions to refer matters to the police rest with the Head of Audit and Risk Management in consultation with the Treasurer and relevant senior managers.

6 Professionalism

6.1 Compliance with the PSIAS and its associated Code of Ethics promotes an ethical, professional culture. Internal Audit officers are subject to the Council's Code of Conduct for Employees and associated policies and are governed by the ethical codes of professional bodies to which they belong. Auditors hold or are studying for accounting or internal audit qualifications and maintain professionalism through a career grade scheme and continuing professional development.

6.2 Internal Audit conducts an annual self-assessment against the PSIAS, including an evaluation of the effectiveness of service activity and performance. A formal quality assurance, feedback and improvement programme informs a plan of continuous improvement. The key measurable is delivery of the audit plan within the year and assignment performance is managed through key performance measures, agreed with CIPFA, AGMA and Core Cities to support benchmarking.

7 Resources and Audit Planning

7.1 The Service is structured in client and risk based teams whose portfolios mirror Council directorates and key risk areas to support effective client relationships and better understanding of needs.

7.2 In line with PSIAS requirements, Internal Audit has an Audit Strategy and an annual risk-based audit plan which is produced for a period of one year giving assurance over the Council's internal control, governance and risk management systems. The plan is developed through an assessment of risk and assurance needs and is sufficiently flexible to reflect changing organisational risks and priorities. It is submitted to the Treasurer and Audit Committee for review and approval and the Head of Audit and Risk Management reports periodically any resource limitations or significant deviation from the approved plan.

8 Monitoring And Reporting

Assignments

8.1 A written report is prepared and issued by the Head of Audit and Risk Management following the conclusion of internal audit assignments. The report includes management's response and any actions necessary regarding

the findings and recommendations. Internal audit outputs and assurances are reported in summary to the Audit Committee.

Monitoring Reports

8.2   In-year the Head of Audit and Risk Management reports to Audit Committee on:

- Progress against plan including any necessary changes;
- Significant control issues identified; and
- Outstanding recommendations from previous audit reports.

Annual Assurance Report

8.3   The Head of Audit and Risk Management prepares an annual report for Audit Committee which includes:

- Summary of audit work carried out in the year;
- Achievement against plan; and
- An overall annual opinion on the adequacy and effectiveness of the systems of Governance, Risk Management and Internal Control. This is a source of evidence for the Council's Annual Governance Statement.

Annual Review of the Effectiveness of the System of Internal Audit

8.4   The Accounts and Audit Regulations 2011 require an annual review of the effectiveness of the Council's system of internal audit to be considered as part of its governance assurance processes, including the Annual Governance Statement. The report demonstrates that there is an effective system of internal audit including a policy framework, internal audit function, Audit Committee and effective management engagement.

9   Review

9.1   The Head of Audit and Risk Management will review and update this Charter on an annual basis.

Appendix Two

External Assessment of Manchester City Council Internal Audit Service Against UK Public Sector Internal Audit Standards

Peer Review of Internal Audit Carried Out By Liverpool City Council
29 November – 1 December 2016

Report Date: 21 April 2017

1.   Introduction

1.1   In April 2013, a new set of Public Sector Internal Audit Standards (PSIAS, "the Standards") became effective. These Standards are mandatory and apply to Internal Audit in all parts of the public sector in the UK. The Standards are intended to reflect that "a professional, independent and objective internal audit service is one of the key elements of good governance".

1.2   The Standards introduced a requirement for an external assessment of an organisation's internal audit function, which must be conducted at least once every five years by a qualified, independent reviewer from outside of the organisation.

1.3   The Core Cities Chief Internal Auditors group has established a 'peer review' process that is managed and operated by the constituent authorities. This process addresses the requirement of external assessment with independent validation and this report presents the summary findings of the review carried out on behalf of Manchester City Council.

2.   Purpose

2.1   The purpose of the external assessment is to help improve delivery of the audit service and establish whether governance requirements relating to provision of the service are embedded. The assessment should be a supportive process that identifies opportunities for development and enhances the value of the audit service to the authority.

3.   Approach/Methodology

3.1   The Core Cities Chief Internal Auditors group agreed a detailed terms of reference that outlines the broad methodology for the conduct of each review. This was issued to Manchester City Council prior to the peer review.

3.2   In summary the peer review was undertaken in three stages: pre-review, on-site review, and the post-review evaluation and reporting. The review covered the audit activity during the period covered in the latest Internal Audit Annual Assurance Report and the current financial year to the end of November 2016. The peer review was undertaken by the two Lead Audit Managers from Liverpool City Council.

Review of Self-Assessment

3.3   The Chief Audit Executive (CAE) and Audit Manager had completed a self-assessment of Manchester City Council's Internal Audit Service and its compliance with the Standards. This self-assessment was used as the basis for the external assessment, which was then evidenced with a range of internal and externally published documentation.

Further Evidence Gathering and Testing

3.4   To support and further inform the assessment a sample of elements of the audit process was examined and compared against the requirements of the Standards and the related CIPFA Local Government Application Note. This included examination of core documents and a sample of audit files for individual audits.

3.5   Operational practices were discussed with the CAE, the Audit Manager and other members of the Audit Team. Meetings were also held with Senior Council Officers including the Section 151 Officer and the Chair of the Audit Committee (the "Board") to explore key expectations of the audit services. The review team attended the Audit Committee meeting held on 1st December 2016 to observe.

4.   Opinion of the External Assessment

4.1   This external assessment concludes that Manchester City Council's Internal Audit Service **complies** with the main requirements of the Public Sector Internal Audit Standards.

5.   Findings

5.1   It was evident from all aspects of the review that Manchester's Internal Audit Service is a well-established team who is highly regarded by the organisation. The team is well-positioned within the Authority and it was evident that they are viewed as a valuable resource.

5.2   The service is headed by an engaging and experienced leader who is highly regarded by Senior Management and the Board. There is a clear vision in place for the service and staff within the team are engaged and invested in the delivery of audit activity. From discussion with senior officers it is clear that the audit team and their work are highly valued and contribute to the efficient workings of the Council.

5.3   Areas for development have been identified through this assessment, however these were in the main identified through the self-assessment demonstrating clear self-awareness of the audit team and a commitment to continuous improvement. The team also have in place an ongoing Service Improvement Plan to further evidence this.

PSIAS Requirements – Definition of Internal Auditing

5.4   The Public Sector Internal Audit Standards include a specific definition of Internal Auditing, a Code of Ethics and eleven specific standards that are divided into attribute standards and performance standards.

5.5   The definition of Internal Auditing has been formally adopted by the Audit Team within their Internal Audit Charter and it is evident from our review that the audit activity undertaken is in line with the definition. The CAE and the audit team act to provide *"independent, objective assurance and consulting activity"*. This is outlined within the Audit Charter and demonstrated in practice through audit activity undertaken and the operational positioning of the team.

5.6   Through discussions with senior officers at Manchester City Council, the self-assessment review and on-site work it is clear that the work of the audit team helps the organisation *"accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes."*

PSIAS Requirements – Code of Ethics

5.7   The mandatory Code of Ethics is referenced within the Internal Audit Charter and the audit team was viewed to be operating in line with the Code and to a high degree of professionalism.

5.8   It was evident that ethics and professional standards are given high regard within the Team. All staff are professionally qualified or studying to be so, and staff are formally reminded of the importance of maintaining high standards through adherence with the Code of Ethics, the Council's Code of Conduct and the completion of an Ethics Declaration and a Declaration of Interest.

Attribute Standards: 1000 - Purpose, Authority and Responsibility

5.9   The Internal Audit Charter sets out the purpose, authority and responsibility of the internal audit activity and this has been reported to the Board. The arrangements outlined in the Charter appear to accurately reflect the organisational and operational arrangements in place and show a good understanding of the role of internal audit.

5.10   The substance of the Charter is in line with the Standards however there are some minor amendments that could be made to ensure the document is fully compliant. A recommendation has been made to update the Charter and present this to Senior Management and the Board.

Attribute Standards: 1100 - Independence and Objectivity

5.11   The Charter sets the standard for the CAE's independence and access to Senior Management and the Board. The CAE reports directly to the Board and attends all Board meetings to present reports and answer questions. Senior management may also be required to attend Board meetings to

respond to audit findings in their area. As part of this review we observed a meeting of the Board and it was clear that the CAE is a valuable contributor to such meetings, and his input both formally and verbally is valued.

5.12   The CAE was appointed by managers and not by the Board. Whilst this is not in accordance with the Standards it is in line with prevailing Local Government practice and in our opinion is an appropriate deviation from the Standards.

5.13   The Standards require feedback to be sought from the Chief Executive and the Board to contribute to the CAE's performance appraisal. At present the CAE's performance appraisals are undertaken by the Section 151 Officer in her line management capacity. This is considered to be in line with prevailing Local Government practice and in our opinion is an appropriate deviation from the Standards.

5.14   There are suitable arrangements in place to manage threats to objectivity at different levels. All staff are required to complete a declaration of interest and these were last updated in September 2016. The CAE confirms to the Board that audit activity is operating independently at least annually through the Audit Plan, the Annual Assurance Report and the Audit Charter.

5.15   Lead Auditors within the team have set areas of the plan that they are responsible for, however these roles were rotated 18 months ago and there is ongoing rotation of other members of the audit team.

5.16   The CAE does have responsibility for some operational areas outside of Internal Audit. Where audit activity is undertaken in such areas the audit activity is cleared through the Audit Manager rather than the CAE.

Attribute Standards: 1200 - Proficiency and Due Professional Care

5.17   The CAE is a member of the Chartered Institute for Public Finance and Accountancy (CIPFA) and is a highly experienced audit professional who has been in his current post for 8 years and also currently serves as the CAE for Bolton Council and Greater Manchester Combined Authority.

5.18   As all members of the audit team are professionally qualified or studying to be so, they are required to comply with the Continuing Professional Development (CPD) requirements of their own professional bodies. An area for development identified through the self-assessment is to improve the record keeping for staff training and CPD undertaken. A recommendation has been made to introduce comprehensive record keeping in this area.

5.19   The Standards set out the requirements for auditors to exercise due professional care for each audit engagement. There is clear evidence that there are suitable arrangements in place to support this including the completion of an Annual Planning Template and a Terms of Reference document for each engagement.

Attribute Standards: 1300 - Quality Assurance and Improvement Programme

5.20   The Standards require that a Quality Assurance and Improvement Programme (QAIP) is developed which covers all aspects of the internal audit activity and enables conformance with all aspects of the Standards to be evaluated. The QAIP should also assess the efficiency and effectiveness of the internal audit activity and identify any areas for improvement. The QAIP is currently in development and once complete will be presented to the Board.

5.21   A self-assessment of compliance with the Standards' checklist was however undertaken in May 2016, and the results of this were reported to the Board in the 2015/16 Annual Assurance report. Once the QAIP has been developed the results of this should be reported to the Board annually.

5.22   The self-assessment identified that the current Key Performance Indicators (KPIs) for the service are in need of a refresh. A recommendation has been made to complete this exercise and to include performance against the KPIs in the Annual Assurance Report to the Board.

5.23   The Internal Audit Team do not currently hold ISO accreditation, however this is currently being explored. ISO accreditation is not a requirement of the Standards but may serve to enhance the quality assurance arrangements.

Performance Standards: 2000 - Managing the Internal Audit Activity

5.24   The Standards require that the risk based plan takes into account the organisation's assurance framework. The CAE seeks to place reliance on assurance mechanisms within the Council as well as findings of other auditors and inspectors. This remains an area for ongoing development for the Authority as a whole and collective action is being taken to further develop risk and assurance mapping across the Council.

5.25   The CAE has to ensure that sufficient audit work is undertaken throughout the year to enable his opinion to be given at the year end and whilst the service operated at a reduced resource during 2015/16, following successful recruitment exercises it held a full complement of 18 staff by August 2016.

5.26   No areas of non-compliance with the Standards were identified.

Performance Standards: 2100 - Nature of Work

5.27   Internal audit planning is undertaken in reference to the corporate and directorate risk registers *(standard 2120: risk management).* The audit plan demonstrates how individual audits relate to risks identified on these risk registers, and risk assessments are performed as part of scoping individual audit assignments. It would be beneficial for an audit of the corporate risk management arrangements to be planned so that assurance can be gained in relation to risk management processes at a strategic level.

Performance Standards: 2200 - Engagement Planning

5.28   Terms of Reference are prepared for each audit engagement which are issued to the respective client officers. These Terms of Reference include the objectives, scope, timing and resource allocation for the engagement. Whilst the consideration of fraud risk, value for money and IT risk is made at the scoping stage this process is not formally documented within the audit planning template, we suggest this is explored further.

Performance Standards: 2300 - Performing the Engagement

5.29   We found that work was well planned, with clear Terms of Reference issued at the start of each audit. When we reviewed a sample of audit files within the Galileo audit system risks, controls, testing and evaluation of results were recorded but there were inconsistencies in how management review had been recorded. The Standards require that appropriate evidence of supervision is documented and retained for each engagement *(standard 2340 engagement supervision);* the adoption of a consistent approach should be considered.

5.30   The use of the Galileo audit management system for working papers is supported by an audit manual documenting key processes. The service has already identified on their service improvement plan that there is a need to refresh the audit manual, dated September 2010, to reflect the requirements of the Standards. The intention is for this to be done following the outcome of this external quality assessment so that the findings can be taken into account.

Performance Standards: 2400 - Communicating Results

5.31   Clear reports are issued following the conclusion of audits. Examples of good practice include:

- giving an overall assurance opinion and the capacity to improve;
- categorisation of both control and compliance issues identified (critical, major, significant, moderate and minor);
- limitations on work; and
- identifying areas of good practice in addition to areas for improvement.

5.32   The Standards (*2410 Criteria for Communicating)* require that the communication of engagement results include limitations on the distribution of the results. As such the existing audit report templates do not contain specific limitations, consideration should be given to the inclusion of Freedom of Information riders to address this requirement.

5.33   The annual report to the Board follows the requirements of the Standards, in that it includes:

- an opinion on the effectiveness of the Council's framework of governance, risk management and control;
- a summary of work undertaken, from which the opinion was drawn; and

- a statement on conformance with the Standards.

5.34 The CAE's annual report to date has not included the results of the QAIP as required by the Standards. This is due to the QAIP being in draft. This has already been referenced and recommendations made in Attribute Standards 1300 above.

Performance Standards: 2500 - Monitoring Progress

5.35 There is a formal follow-up procedure where audit recommendations are made. As part of the performance monitoring of the Internal Audit Service, a report has recently been taken to the Board specifically focussing on numbers and types of audit recommendations made and action taken to address them; a notable area of good practice.

5.36 No areas of non-compliance with the Standards were identified.

Performance Standards: 2600 - Communicating the Acceptance of Risks

5.37 Where the CAE has concluded that a level of risk may be unacceptable to the organisation, he has discussed the matter with senior management and communicated this to the Board.

5.38 We would like to thank all those involved in the review, in particular Tom Powell and Kathryn Fyfe.

6.   Action Plan

No.	Observation	Recommendation	Management Response
1	An Internal Audit Charter is in place to define the purpose, authority and responsibility of internal audit activity. The Charter is generally compliant with the Standards' requirements however there are some changes required to make the document fully complaint.	The Internal Audit Charter should be updated to fully reflect the requirements of the Standards. The updated Charter should be presented to Senior Management and the Board. The update should include the following points: • The Charter should be updated to reflect the more up to date Accounts and Audit Regulations 2015. • The Charter should be more explicit in stating that Internal Audit should be notified of all suspected or detected fraud. • The nature and definition of consulting services should be included within the Charter. • Consideration should be given to including a timescale for review of the Charter (e.g. annually or bi-annually) rather than periodically.	Agreed. Refreshed Charter to be presented to Audit Committee by End October 2017.
2	Whilst all staff undertake CPD and training, both in-house and through their respective professional bodies, the record-keeping of this is not up to date. Improvements in this area were identified through the self-assessment.	Comprehensive record-keeping should be introduced to capture staff training and CPD activities.	Agreed. To be included in Quality and Standards element of Audit Development Programme to commence from 1 April 2018.

No.	Observation	Recommendation	Management Response
3	The Standards require that a Quality Assurance and Improvement Programme (QAIP) is developed which covers all aspects of the internal audit activity and enables conformance with all aspects of the Standards to be evaluated. The QAIP should also assess the efficiency and effectiveness of the internal audit activity and identify any areas for improvement.	The QAIP should be developed and formally reported to the Board. An assessment of the performance against the QAIP should be undertaken annually with the results reported to the Board. This will allow the CAE to confirm annually that the audit activity has been undertaken in accordance with the Standards if supported by the results of the QAIP assessment.	Agreed. QAIP to be presented to Audit Committee as part of the City Treasurer's Review of Effectiveness 2017/18 scheduled for February 2018.
4	The self-assessment identified that the current Key Performance Indicators (KPIs) for the service are in need of a refresh.	The current KPIs should be reviewed and updated. Once the revised KPIs have been developed, performance against the indicators should be included in the Annual Assurance Report to the Board.	Agreed. KPIs to be refreshed as part of development programme. To be confirmed with City Treasurer and reported to Audit Committee as part of the City Treasurer's Review of Effectiveness 2017/18 scheduled for February 2018.
5	An audit of corporate risk management arrangements has not been performed for some time.	Schedule an internal audit review of corporate risk management arrangements.	Agreed. Audit to be included in Annual Plan for 2018/19 to be reported to Audit Committee in March 2018.

No.	Observation	Recommendation	Management Response
6	Whilst it is clear that there is consideration of fraud risk, value for money and IT risk at the scoping stage, this process is not formally documented within the audit planning template.	Consideration should be given to incorporating value for money, fraud risk and IT risk in to the audit planning template.	Agreed To be included in Assignment Planning element of Audit Development Programme to commence from 1 April 2018.
7	It was evident that audit system risks, controls, testing and evaluation of results are recorded and evidence, however some inconsistencies were observed in documenting evidence of management review.	Consideration should be given to enhancing the current arrangements for the management review of working papers so that a clear and consistent approach to review is evidenced.	Agreed To be included in Fieldwork element of Audit Development Programme to commence from 1 April 2018.
8	There are described systems of audit in place supported by the Audit Manual. However, there is a need to refresh the Audit Manual to reflect the Standards.	Audit Management to update the Audit Manual to reflect the Standards, as outlined in the Service Improvement Plan.	Agreed Updated manual will be finalised as part of the Audit Development Programme to commence from 1 April 2018.

No.	Observation	Recommendation	Management Response
9	Engagement results do not include narrative regarding the limitations on the distribution of the results.	Consideration should be given to the inclusion of Freedom of Information riders on audit report templates to address this requirement.	Agreed Updated narrative will be considered as part of the Assignment Reporting element of the Audit Development Programme to commence from 1 April 2018.