

**Manchester City Council  
Report for Information**

**Report to:** Audit Committee - 15 April 2019

**Subject:** Review of Effectiveness of Internal Audit

**Report of:** Deputy Chief Executive and City Treasurer

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**Summary**

The Council conducts an annual review of the effectiveness of its system of internal audit as part of its governance assurance processes. This process is designed to provide assurance to the Deputy Chief Executive and City Treasurer, and Audit Committee over the system of internal audit including the role, function and performance of the internal audit service.

This report sets out the process for the 2018/19 review, key findings and actions proposed to further develop the effectiveness of internal audit in 2019/20.

**Recommendations**

Audit Committee is requested to:

- Consider the level of assurance provided by the review of effectiveness and progress on management improvement actions from the QAIP 2018/19 and planned actions for 2019/20 (appendix one).
- Review and comment on the proposed refresh of the Audit Committee Terms of Reference (appendix two).
- Review and approve the Internal Audit Charter (appendix three)

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**Wards Affected:** All

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**Background documents (available for public inspection):**

Documents used in the development of the assurance report include the 2018/19 Internal Audit Plan, 2017/18 Review of Effectiveness and Progress reports to Audit Committee during 2018/19.

## **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, including the Head of Internal Audit's Annual Opinion, helps inform the Annual Governance Statement.
- 1.2 The Public Sector Internal Audit Standards (PSIAS) 2017 enable the application the Institute of Internal Auditors (IIA) International Standards to the UK public sector. For 2018/19 the review of effectiveness of internal audit has been informed by a review of progress against the Internal Audit service development plan; ongoing monitoring of the performance of the internal audit activities; and a self-assessment against the PSIAS.
- 1.3 The service development plan incorporated actions agreed in response to the External Quality Assessment (EQA) 2017; self assessment and changes requested by Audit Committee in respect of recommendation monitoring; classification of audit risks/priorities; and formats for reporting to Audit Committee as well as a project to re-establish the audit process in line with lean principles. Action to address these matters was taken in collaboration with Bolton Council and an update is provided below.

## **2 Internal Review of the System of Internal Audit**

### Structure, Staffing and Skills

- 2.1 The Internal Audit Service is led by the Head of Audit and Risk Management, who for 2018/19 performed the same role for Bolton Council and the GM Combined Authority. The arrangement will change in 2019/20 as the GMCA have appointed a Head of Audit and Assurance and will develop an in house service in conjunction with Transport for Greater Manchester. This will mean Manchester' support will cease from the end of June 2019.
- 2.2 This arrangement continued to support the development of collaboration opportunities across teams and sharing of knowledge, skills and experience across the three authorities. The Manchester Audit team is led by an Audit Manager supported by six Lead Auditors with assigned responsibilities for dedicated portfolios which enables engagement with clients as follows:
  - Adults Services, Children's Services, and Education and Skills
  - Neighbourhood Services, Strategic Development and Highways
  - Corporate Core and Data, Information and Systems
  - Procurement, Commissioning and Contracts
  - Counter Fraud and Irregularity
  - GMCA Audit
- 2.3 The Internal Audit Service is an independent, objective, assurance and consultancy activity designed to add value and improve the Council's

operations. It helps the business accomplish its objectives by bringing a systematic and structured approach to evaluation and improvements in the effectiveness of risk management, control and governance processes. To enable this there is an in-house service which seeks to deliver a programme of audits based on its annual audit plan.

- 2.4 The in-house team comprises 18 FTE posts supplemented by up to 50 days per annum of specialist audit support which in 2018/19 was commissioned through the Council's Financial Service Framework. In 2018/19 the actual FTE available for audit work in the service was 16 as the impact of five staff working reduced hours; one maternity leave and two vacancies was balanced in part during the year with the one fixed term appointment and an experienced auditor secured via agency.
- 2.5 The audit team has an appropriate mix of experience and qualifications to support audit and assurance activity in year and where appropriate specialist resources are bought in for some work in line with resourcing plans and budgets. The skill mix in year included five qualified accountants (CCAB), six fully qualified internal auditors (F/CMIIA); four certified internal auditors; one CIPFA trainee awaiting accreditation after passing all exams. In addition, to support Counter Fraud work four members of the team are qualified in investigate techniques (ACFS and ACFT); one holds Government Intelligence Analysis training and three have training and experience the use of data interrogation software (IDEA). All staff have undertaken ongoing training in a range of professional skills as part of the service learning and development plan and requirement for continuing professional development.
- 2.6 For 2019/20 there will be one staff member on maternity leave for quarter one and two vacancies remain held within the structure pending the outcome of the service development review and structure review. This resource gap for 2019/20 will be offset by the extension of a fixed term contract appointment and the retention of an agency auditor for a further six-month period based on assumptions made in the annual audit plan.
- 2.7 In 2019/20 the service will be strengthened through appointment to a new post of Deputy Head of Audit and Risk Management. Interviews for this post were completed in March and an appointment made with proposed start date in early May 2019. The post holder will work across Manchester and Bolton and will play a critical role in supporting the leadership, management, development and delivery of audit services. A timeline for a review of the structure of the Audit and Risk Management Services within Manchester and Bolton, to support further collaboration and application of expertise across both Council, including Internal Audit, will be undertaken in the first half of 2019/20 with intention to agree and implement any required changes to structure from October 2019.
- 2.8 Overall the level of resources available for delivery of the annual audit plan in year was considered to be sufficient to support delivery when supported by some flexibility in the timing and scoping of work and the ability to source some external specialist resource where required.

## Planning, Delivery and Performance

- 3.1 The work of internal audit for 2018/19 was set out in an audit strategy and annual plan discussed with senior managers, approved by Senior Management Team (SMT) and then Audit Committee in June 2018. The approach taken was to provide a range of audit work with different scope and coverage comprising:
- Audit Opinion Reviews (around 50% of plan)
  - Audit Assurance Reviews (around 20% of plan)
  - Advice, Guidance and Support (around 10% of plan)
  - Counter Fraud, Probity and Investigations (around 20% of plan)
- 3.2 Delivery and the outcomes of audit work were reported to Directorate Management Teams (DMTs), Strategic Directors and Audit Committee on a quarterly basis and audit plans refreshed based on the basis of risk assessment.
- 3.3 Whilst performance and impact cannot be assessed solely on the numbers of reports issued, in 2018/19 the majority of the agreed audit plan was delivered or substantially underway by the end of March 2019. Amendments to plans reported to or requested by management were approved by Audit Committee during the year as part of regular delivery progress review. The position at 22 March is as shown below:

### **Audit Outputs Issued to Date (as at March)**

<b>Audit Status</b>	<b>2018/19*</b>	<b>2017/18</b>	<b>2016/17</b>
Final Reports Issued	72	103	111
Additional Work Issued	3	4	11
Draft Reports Issued	15	8	8
Fieldwork Completed or Started	22	7	29
Totals	<b>112</b>	<b>122</b>	<b>159</b>
Cancelled/Deferred	8	9	16

\* Final and draft reports for 2018/19 includes investigation reports that will be reported as part of the Annual Outturn Report and the Annual Fraud Report in June 2019.

- 3.4 There were eight deferred and cancelled audits in the year and all changes to the audit plan were risk assessed and agreed with Audit Committee. This was requested only where the risk or system had fundamentally changed and/or where alternative assurance could be obtained or where timing made the work impractical. There were some delays in agreeing a few final reports because of challenges in agreeing action plans which in some cases spanned organisations. Any concerns were raised with Audit Committee as needed. All dates of issue of draft and final reports are shared with DMTs, SMT and Audit Committee to ensure that any concerns or undue delays arising can be addressed in good time.

- 3.5 Delivery in year was monitored as part of regular review by the audit management team and regular progress reviews were undertaken to support the direct supervision of audit work. Issues for delay on progressing audit work were discussed with escalation where required to seek resolution and resources reassessed as needed to balance work load and skills. The outcomes of progress monitoring were shared with the audit team as a whole as part of the active management process.
- 3.6 Complaints made against the service are addressed as part of the Council's corporate complaints process and the policy requires that any whistleblowing allegations against the service are considered independently by the City Solicitor in line with policy. There was one formal complaint in the year that related to conduct of a fraud investigation case, was investigated at all stages of the corporate complaints process and was not upheld. The complainant made further allegations in relation to Legal Services staff and complaints as part of judicial processes that again were not upheld.

#### Findings and Reporting

- 3.7 The findings of internal audit work were confirmed in draft individual assignment audit reports enabling a review of factual accuracy with clients in line with standards. A two-week window was provided for responses and this was generally met but there were some exceptions which required escalation action to senior officers to ensure that work could be finalised. Usually this was due to the complexity of issues arising and the need to coordinate practical responses and action plans.
- 3.8 For all opinion audits, an assessment of assurance was provided within a five-point scale from "no" to "full" assurance and agreed actions were assigned a priority from "critical" to "minor", again as part of a five point scale. This basis for assessment was reviewed during the year to reassess consistency and usefulness and there is an intention to change the levels of assurance in 2019/20 from five to four levels for 2019/20 as part of the revised audit approach and audit manual.
- 3.9 All final reports including agreed management actions were issued to the (then) City Treasurer, City Solicitor and Chief Executive and shared with External Audit. Summary reports and all opinions issued were reported to SMT and Audit Committee quarterly as part of the assurance reporting framework. The format of summary reports will be revised for 2019/20 to include executive summaries of audit reports.
- 3.10 Agreed service improvement actions required following audits were progressed by service management. Internal Audit discharged its role to monitor progress to implementation on a regular basis with performance and any areas of concern reported to DMTs, SMT and Audit Committee. The implementation of recommendations was also reported to Executive Members to provide them with details of all audit reports and key issues arising.

- 3.11 Audit Committee discharged its role in considering findings and issues arising from audit reports thereby supporting an effective system of internal audit. The Audit Committee met seven times in the year and considered reports from the audit service and the responses from management as part of an assessment of progress and assurance. In the last twelve months this resulted in a number of specific reports being presented to Audit Committee from management and Executive Members on key areas of risk including ICT, Adults Services, Children's Services and Neighbourhoods.

#### 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 97% of the 313 applicable Code requirements were met fully which was a small increase on last year. Action on a further 2% partially met standards formed part of the Quality Improvement Assurance Plan in year. The six statements classed as partial relate to the following and actions to address these are included in the QAIP Development Plan at appendix one (actions 6 and 16)

- 1210 Proficiency
  - Does the internal audit activity collectively possess or obtain the skills, knowledge and other competencies required to perform its responsibilities?
  - Do internal auditors have sufficient knowledge of key information technology risks and controls?
  - Do internal auditors have sufficient knowledge of the appropriate computer-assisted audit techniques that are available to them to perform their work, including data analysis techniques?
- 1230 Continuing Professional Development
  - Do internal auditors maintain a record of their professional development and training activities?
- 2030 Resource Management
  - Does the risk-based plan explain how internal audit's resource requirements have been assessed?
- 2430 Use of 'Conducted in Conformance with the International Standards for the Professional Practice of Internal Auditing'
  - Do internal auditors report that engagements are 'conducted in conformance with the PSIAS' only if the results of the QAIP support such a statement?

- 3.13 The other 1% were assessed as not applicable to the Council and this was acknowledged as such by the External Quality Assurance review carried out in 2017.

- 3.14 The key areas for enhancement of processes and documents were reported to Audit Committee in 2017 following the EQA and were reflected in an action plan which was underway and refreshed as part of the QAIP in year. The Quality Assurance Improvement Programme (QAIP) has been developed to build on the performance monitoring arrangements required by PSIAS and

progress will be reported annually to Audit Committee against key measures. The QAIP Framework 2019/20 is included at appendix one to this report.

- 3.15 The quality of audit work was actively managed in year through formal review by audit management. The achievement of quality standards enabled the Head of Audit and Risk Management to confirm that audit work was completed in conformance with PSIAS and this was reflected on audit reports issued. Individual audits had agreed clear plans and scopes; activity was reviewed and assessed for its effectiveness during and after completion of work; and customer feedback was sought and received on some work using questionnaires. Responses received were generally positive however response rates to customer questionnaires remained very low. Consideration is being given to how effective formal feedback and improved response rates can be secured.

#### Independence and Other Responsibilities

- 3.16 The Internal Audit Service is part of the Audit and Risk Management Division of Corporate Services and its role is defined in the IA Charter (Appendix Three) which also includes risk and resilience; health and safety; and insurance and claims services managed by the Head of Audit and Risk Management. The arrangements support effective collaboration between these teams on key risk areas and major programmes which in year has included Factory; Our Town Hall; health and social care integration; and aspects of information governance. The Internal Audit Service also works closely with other services across the Core including finance, legal, procurement, Human Resources and ICT. Whilst working collaboratively with colleagues, the Service retains its own identity and is managed day to day by the Audit Manager. Any audit work in respect of services for which the Head of Audit and Risk Management is also responsible is reported directly to the City Treasurer by the Audit Manager as needed. In the current year this was the Corporate Risk Governance audit. This was acknowledged as appropriate practice by the EQA 2017 and in the annual PSIAS self- assessment.
- 3.17 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, and Human Resources and the Chair of the Audit Committee. This helps ensure independence and allows for issues to be escalated should the need arise. There were no such requirements in 2018/19.

#### Role of the Audit Committee

- 3.18 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.
- 3.19 The annual officer review of the Audit Committee terms of reference proposes changes to align with Public Sector Internal Audit Standards. This review has included feedback from the External Quality Assurance review; PSIAS self-



assessment and a review of Committee Terms of Reference used in other Core Cities. The refreshed terms of reference are provided at appendix three and subject to Audit Committee comments will be reviewed and confirmed as part of process of annual review of the constitution in May 2019.

- 3.20 Changes have been made to the presentation of the Terms of Reference to reflect the requirements of the PSIAS and more effectively highlight the purpose of the Audit Committee and then specific roles and activities which support it. While most of the content remains the same three additions have been made to clarify the arrangements in place specifically that the Committee:
- Provide free and unfettered access to the Audit Committee Chair for the Head of Internal Audit and Risk Management, including the opportunity to meet privately with the Chair;
  - Consider any impairment to independence or objectivity arising from additional roles or responsibilities outside of internal auditing of the Head of Internal Audit and Risk Management. To approve and periodically review safeguards to limit such impairments; and
  - Receive the results of the Quality Assurance and Improvement Plan annually and the external quality assessment of internal audit that takes place at least once every five years.
- 3.21 Audit Committee discharged its role in considering findings and issues arising from audit reports thereby supporting an effective system of internal audit. The Committee has a defined work programme covering reports in respect of internal audit activity, external audit, risk management, governance and financial reporting. It includes a standing agenda item to receive assurance and updates from senior management and Executive Members. The Committee met seven times in the year and considered reports from the audit service and the responses from management as part of an assessment of progress and assurance. In the last twelve months this resulted in a number of specific reports being presented to Audit Committee from management and Executive Members on key areas of risk including ICT, Adults Services, Health and Social Care Assurance, Children's Services and Neighbourhoods (Events Management).
- 3.22 In discussing health and social care assurance and partnerships with Manchester Clinical Commissioning Group (MCCG) and Manchester Foundation Trust, the Audit Committee has committed to establishing closer liaison with MCCG Audit Committee and the Chair of that Committee has also attended Council Audit Committee meetings as an observer. A meeting to explore opportunities for further alignment and information sharing will take place in 2019/20.
- 3.23 The Committee has remained apolitical in its approach and includes two independent members. The Chair has pre-meetings with senior officers and affords an opportunity for Internal Audit to raise any concerns as appropriate.
- 3.24 Audit Committee have discussed their own development and as part of this engaged in two update and training courses in the year that covered the Role

of the Audit Committee; Role of Internal Audit; Treasury Management; Role of External Audit; and Annual Accounts.

#### **4 Quality Assurance Improvement Programme.**

- 4.1 A key requirement of the PSIAS is to maintain a Quality Assurance Improvement Plan (QAIP).
- 4.2 The service development and improvement actions arising from the internal review, External Quality Assessment (EQA) 2017 and feedback from SMT and Audit Committee are all included in the QAIP attached as appendix one. Positive action has been taken and a number of actions are now completed. The remaining actions will be addressed with the implementation and embedding of the new audit approach including processes defined in the new audit manual which has been developed and goes live April 2019 and will be monitored during the year. This includes implementation of a new assurance reporting format and a structured process for recording management reviews on audit work.
- 4.3 The Audit Charter which confirms 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 defines the scope of Internal Audit activities has been reviewed and updated. The Charter is re-presented at appendix one as part of the requirement for annual review and approval by Audit Committee.
- 4.4 A programme of development work across the audit functions in Manchester, Bolton Council and the GM Combined Authority was completed during the year. This involved engagement of all audit staff across the three organisations to examine and confirm core audit principles and methodologies including a new audit evaluation process and enhancement to the audit reporting arrangements seeking to increase efficiency.
- 4.5 A final version of the approach has now been finalised with audit teams. Implementation was delayed to April 2019 though some elements were already in place such as recommendation monitoring and escalation of risk process and the use of the audit planning templates to create the audit plan 2019/20.
- 4.6 The key changes which will be delivered from this development programme remain:
- A single set of simple quality and performance standards for onward reporting to senior management and Audit Committee.
  - Development of assurance summaries for Heads of Service and Directors to support their assessment of sources of assurance, guide improvement actions and help inform internal audit planning.
  - Refinement of the annual audit planning process, to ensure effective engagement of key stakeholders and timely approval of the annual plan.

- Refinement of the overall audit approach, to minimise elapsed time on audits and further enhance the efficiency of audit teams as well as enhancing and standardising quality assurance requirements.
- New reporting formats 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 governance and ICT; schools and academies; and procurement, commissioning and contracts.

## **7 Conclusions**

- 7.1 The internal review of the effectiveness of the system of internal audit informed by the tool for self-assessment against PSIAS and follow up on key actions from the EQA action plan and integrated in the QAIP have not identified any additional issues which impact on the effectiveness of the Service.
- 7.2 Work continues to progress on development actions already identified to enhance efficiency and effectiveness and there are some areas where action will continue into 2019/20.

## **8 Recommendations**

- 8.1 The Committee is requested to:
- Consider the level of assurance provided by the review of effectiveness and progress on management improvement actions from the QAIP 2018/19 and planned actions for 2019/20 (appendix one);
  - Review and comment on the proposed refresh of the Audit Committee Terms of Reference (appendix two);
  - Review and approve the Internal Audit Charter (appendix three).