

# **Warwick District Council – Internal Audit**

## **A Review of the Effectiveness of the Service**

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## **1. Introduction**

- 1.1 Every local authority needs to know that it has strong arrangements for controlling their resources and for delivering their objectives. Internal audit has an important role to play in achieving this.
- 1.2 Internal audit is one of the cornerstones of effective governance. Therefore, an effective internal audit function is paramount if Warwick District Council is going to demonstrate it has embedded the principles of good governance. Through the leadership of the Audit and Risk manager, the internal audit team is responsible for reviewing and reporting on the adequacy of the authority's control environment, including the arrangements for achieving value for money. The Audit and Risk Manager gives assurance to the Council through his annual internal audit opinion and also makes recommendations for improvement through the work of internal audit.
- 1.3 The effectiveness of internal audit needs to be judged by looking at the contribution it makes and the assurance it provides. Internal audit is most likely to be effective in shaping and supporting the outcomes listed below:
  - Effective control and risk enabled
  - Good governance
  - Quality of service
  - Innovation and continuous improvement
  - Ethical behaviour
  - Goal realisation
  - Value for money
  - Public accountability

The relative importance of these outcomes is reflected by the organisation and there may be other outcomes that are also relevant to Warwick DC.

## **2. Scope of review**

- 2.1 The review was based on the framework guide developed by the Chartered Institute of Public Finance and Accountancy (CIPFA) Better Governance Forum which aims to provide practical support to help make internal audit more effective.
- 2.2 This has been achieved by assessing the internal audit function against the building blocks for effective internal audit identified in the guidance. The building blocks are:
  - Leadership
  - Governance and relationships
  - Customer focus
  - People
  - Systems and processes
  - Professional Standards

The contribution internal audit makes to the outcomes listed in 1.3 have been taken into account throughout the assessment.

2.3 The review has not assessed the effectiveness of those areas of the internal audit service that have been contracted out i.e. IT audit.

2.4 Evidence to support my findings has come from a number of sources:

- Interviews with
  - the Audit and Risk Manager
  - Internal audit staff
  - Head of Finance
  - Service Heads
  - Members of the Finance and Audit Scrutiny Committee
- Internal audit Working papers/files
- Internal audit reports
- Reports to Finance and Audit Scrutiny Committee
- Information held on the Warwick DC website

### **3. Findings**

#### **3.1 Leadership**

The role of the Audit and Risk Manager should be more than just the management of the internal audit team. Leadership and representation of internal audit are vital components. To be effective the Audit and Risk Manager needs to establish the right strategy for the internal audit service, build relationships with stakeholders and gain the necessary support for the internal audit role. Leadership impacts on a number of the building blocks for an effective internal audit in that it plays a pivotal role that makes the most of people, develops the best systems and processes and ensures compliance with professional standards.

One of the key documents for Internal Audit is the audit strategy. This identifies the priorities for internal audit based on an assessment of the key risks to the authority and the extent of alternative sources of assurance, as well as the resources and skills needed to deliver it. The responsibility for effective governance arrangements (including risk management) remains with managers; the Audit and Risk Manager cannot be expected to prevent or detect all weaknesses or failures in internal control nor can the internal audit strategy cover all areas of risk across the authority.

There is there a clear vision for Internal Audit which is laid down in the Internal Audit Strategy. The strategy document is taken to Finance and Audit Scrutiny Committee on an annual basis. The Audit team believe that the profile and status of Internal Audit has been raised within the organisation through the strategy and the role and responsibilities of the Finance and Audit Scrutiny Committee.

It is always difficult to demonstrate how Internal Audit contributes directly to organisational objectives. However, the work that Internal Audit does as part of the

annual audit plan contributes directly to the organisational development within the Council.

The Audit and Risk Manager has set realistic performance standards and they are relevant to the internal audit service. The performance standards are reported to Audit Committee. These are based on:

- quality of work (measured through post audit questionnaires)
- productivity

The Audit and Risk Manager aims to complete the audit plan each year. My review found that this is nearly always the case.

There was evidence to show that the Audit and Risk Manager has extensive formal communication with the team. There are team meetings every 4 weeks which last about 2 to 2.5 hours. Minutes are produced of these meetings. The staff benefit from these meetings as they gain an understanding of what is happening within the authority.

The Audit and Risk Manager makes every effort to promote innovation and continuous improvement. He is in touch with new developments and initiatives in internal audit and risk management through his membership of the CIPFA Technical Information Service Editorial Board, the Midland District Chief Internal Auditors Group and CIPFA's continuing professional development (CPD) scheme and his own personal development. The internal audit staff believe that the audit function has developed and moved forward under the current Audit and Risk Manager. It is evident that the section has taken on board best practice in order to demonstrate continuous improvement. This can be seen in the audit processes that are embedded in the methodology used by the team.

The Audit and Risk Manager has a "fairly hands-off managerial approach" in that he is detached from the day to day work of the team. The team are responsible for planning their work load.

### **3.2 Governance & Relationships**

Although Internal Audit is not responsible for good governance, it does have an important role to play in helping to raise standards. This can be done by promoting the benefits of good governance as well as reporting on system failures. Internal Audit needs to assess the state of the authority's governance and then decide how it can make most impact.

The internal audit staff have an understanding of the principles of good governance, but I have seen little evidence to demonstrate that a proactive approach to raising awareness of the principles is part of the audit remit. The staff have said that they have little involvement in governance issues and that there is limited coverage in the internal audit plan. Although areas of governance are reviewed through individual audits and there is a 5 day allocation for governance in the plan, this is not co-ordinated to provide assurance that the governance framework of the Council is working as intended. I believe that governance work

by Internal Audit needs to be further developed and be more targeted in the internal audit plan.

### **Recommendations**

**Set out Internal Audit's role in good governance and how this fits with the role of others, in particular the CFO, the Monitoring Officer and the Head of Paid Service.**

**Ensure that Internal Audit plays an active role in promoting good governance. This can be achieved through training at all levels within the authority and the use of case studies to get the message across.**

**Ensure that Internal Audit is consulted on all proposed major projects, programmes and policy initiatives.**

**The Audit and Risk Manager should assess the value to Warwick DC and Internal Audit of joining CIPFA's Better Governance Forum as a means of accessing best practice in governance.**

The Finance and Audit Scrutiny Committee is very supportive of Internal Audit, and there is a good working relationship between the Committee and the Audit and Risk Manager. Those Members of the Committee with whom I made contact believe that there is an excellent relationship between the Committee and Officers. One member of the Committee stated that the effectiveness of internal audit was enhanced by the existence of the Finance and Audit Scrutiny Committee, in that the Committee provided more strength to the internal audit function. The main conclusion I drew from talking to Members was that they feel that the Internal Audit service has shown a lot of improvement over the last few years and that the Audit and Risk Manager is moving the service forward.

While the Finance and Audit Scrutiny Committee provides constructive challenge to internal audit on the scope of audit, I found insufficient evidence to demonstrate that all Members of the Committee have been provided with a good understanding of internal audit issues to enable them to offer a robust challenge. At the time of my review, the Audit and Risk Manager stated that he had not carried out any relevant training on audit with the Committee for 2 to 3 years.

I also found insufficient evidence to show that the Finance and Audit Scrutiny Committee understood the extent of the Council's assurance framework and how it could provide them with the comfort they needed as a committee on governance issues.

### **Recommendation:**

**The Audit and Risk Manager needs to provide more regular and relevant training to the Committee, particularly around the role of Internal Audit and the assurance that internal audit provide. It may be useful to identify the gaps in knowledge amongst the Committee members and target training on those issues.**

From my discussions with Members of the Finance and Audit Scrutiny Committee, I can conclude that there is confidence in internal audit from the Committee. The Chair of the Committee is satisfied that she is fully briefed on significant findings or developments prior to committee meetings and that internal audit promptly advise the committee about significant issues and significant developments, including on special projects such as fraud investigations. It is also clear that the Audit and Risk Manager has made himself available to members for consultation outside of the committee meetings. In instances where the Audit and Risk Manager does not have the answer to members' questions in Committee, he will endeavour to provide a response the following day, usually by e-mail. Members are keen not to be "swamped" with paper at Committee meetings and they are satisfied that the Audit and Risk Manager has addressed these issues to their satisfaction.

Occasionally, changes to the internal audit plan are required. In such cases the Audit and Risk Manager will advise the Finance and Audit Scrutiny Committee of the details in his quarterly report.

Internal Audit is line-managed by the Head of Finance who is the Council's s151 Officer. I do not see that this positioning of the Internal Audit function within the Council has a detrimental impact on Internal Audit's independence in carrying out its duties.

Internal Audit receives a varying level of support from management within the Council. This is normal at any local authority.

I understand that the team has established a good working relationship with the council's External Auditor. The key element when assessing the effectiveness of Internal Audit is that the External Auditor can place reliance on the work of internal audit. External Audit confirms this on an annual basis. I am satisfied from the available evidence that there is effective liaison between internal and external audit. This is demonstrated by quarterly meetings between the External Auditor and the Audit and Risk Manager.

### **3.3 Customer focus**

- 3.3.1 Customer focus is essential not just for the manner in which internal audit is approached, but also to ensure that internal audit understands the organisation and focuses on the current and future risks to the organisation and supports the achievement of the organisation's objectives.

Internal audit has developed a framework for consulting with clients. Officers find this an effective way to discuss their audit needs with the Audit and Risk Manager. It provides them with an opportunity to put forward ideas for audit work, and to discuss the areas of their business which they feel has the higher risk and would benefit from an independent audit review.

The Officers within the council that I met as part of the review felt that Internal Audit now understands the future challenges and risks facing the Council, although this has not always been the case. Internal Audit has shown over the past year or so, that it can adapt its approach to meets the needs of a differing

range of clients and is now moving towards meeting the challenges. Officers now want a non-traditional approach on a more frequent basis. Internal Audit has shown that it is able to accommodate such requests and is becoming more geared to providing a service that Section heads want.

The overall opinion on internal audit output was that the reports were timely, clear and concise. The recommendations were clear and practical, with a clear action plan developed and focused by an understanding of the Council and its business. One of the shortcomings of the recommendations put forward was that there was a big reliance on client delivery with no indication of any assistance that Internal Audit could offer. This would have to be balanced with the need for Internal Audit to be independent of the systems and controls which it audits. Officers are also looking for how internal audit recommendations can add value to the systems, processes and controls. There was also the view that some recommendations made by Internal audit are fine in theory, but do not take into account the operational or financial issues within the solution. There needs to be more dialogue on the recommendations before they are finalised. Some officers were concerned that internal audit was still “hung up” on lower risk issues; however, they had seen a shift towards internal audit looking at the bigger risks in the last year or so.

Both audit staff and officers I spoke to expressed a concern about the repetitive nature of internal audit reviews. However, this has to be balanced against the size of the organisation and the inherent risks within certain systems that warrant internal audit coverage.

Evidence gathered during the review demonstrates that internal audit adequately responds to the requirement to investigate financial irregularities and special investigations.

In relation to dealing with difficult or contentious issues raised by Managers, I have concluded that Internal Audit is sensitive to the needs of the client and sufficiently flexible in its approach to provide the service required.

My review found that there are officers in the Council who do not understand Internal Audit’s role. This is not helped by the “behind closed doors” impression given by the internal audit staff – they need to be more approachable and more visible than at present. It was felt that the Audit and Risk Manager was approachable and keen to assist.

**Recommendation:**

**The Audit and Risk Manager needs to explore methods of improving the accessibility to internal audit.**

**The Audit and Risk Manager should explore suitable methods of raising awareness of the role of internal audit.**

Officers would welcome a more pro-active approach from Internal Audit, particularly around the sharing of knowledge and audit staff making themselves

more accessible. The message from officers was that Internal Audit must recognise the need to change and be responsive to what the services want and the way Council services are being delivered.

The overall opinion is that Internal Audit provides a professional service, which is becoming flexible to client needs. The team is thorough in its approach and the reports and ad hoc advice provided are normally good. The impression I got from talking to staff at the Council was that Internal Audit is well respected, particularly at management level in the Council.

### **3.4 People**

Internal audit needs internal auditors with appropriate knowledge, skills, experience and aptitude. Good team working is also key to ensuring effective performance.

The Internal Audit team consists of 4 very experienced auditors. It is clear from my review that they possess the necessary knowledge, skills, experience and aptitude to deliver a good audit service to the District Council. There is a good blend of skills within the team which I conclude are appropriate to their specific roles and responsibilities. The team came across as well motivated and displayed a good attitude to their audit work. From the evidence I compiled, I believe that there is good team working evident in the Section. The culture of the team has developed over a number of years and in my opinion is capable of supporting and encouraging innovation and improvement in the work they perform.

I also reviewed whether the internal audit team has an appropriate programme of continuing development/education. There is no specific team development plan produced, with the focus for learning and development being generated via individual appraisals. The Internal Audit strategy does not contain a people element to demonstrate how individual development of members of the team will be monitored and developed. However, given the size and experience of the section, the restricted budget for training and the fact that personal development does occur (e.g. staff attend the CIPFA in the Midlands Audit Training Seminars), I have concluded that the arrangements for training are adequately developed. However, given the ad hoc nature of planning individual auditor's development and the fact that there is no overall formal documentation for the section, I would advise that a 3 year training and development strategy be included in the Internal Audit Strategy.

#### **Recommendation:**

**The Audit and Risk Manager should consider the merits of producing a 3 year team development plan for internal audit and also formally records the actual training and development that has taken place.**

Given the size and nature of the authority, I believe that the internal audit function is appropriately resourced to meet the needs of Warwick District Council.

### 3.5 Systems and processes

The working practices of an internal audit team support the achievement of objectives, efficiency and flexibility. Some aspects are defined by professional standards.

The annual audit opinion is the most important output from the Audit and Risk Manager. All of internal audit's systems and processes need to be designed to enable the Audit and Risk Manager to give proper comfort/sound assurance to those who ask for it, and to improve governance arrangements. This means that internal audit planning must be well focused, comprehensive and consider the whole control environment, so that the opinion is based on a picture of the whole organisation. Individual audits must be carried out in a logical and systematic way, based on sufficient, relevant and reliable evidence and with the work being subject to proper supervision and review. Internal Audit must also ensure that their reports are balanced, focusing on key risks and issues and making practical recommendations.

The report to Committee states that the audit plan is risk based and the annual plan is derived from a 3 year rolling strategic plan. The strategic audit plan taken to Committee on 16 March 2010 has a traditional feel to it, in that it details functions/systems and the level of risk for each area is not highlighted in the plan. I would have expected that Committee were given the level of risk of each area to give them an understanding of why there is a need for an audit review.

#### **Recommendation:**

**The Audit plan provides an indication of the level of risk within each area to be audited.**

The audit work carried out concentrates on the controls in place rather than the risks that need to be mitigated. Given that the plan is risk based, it would enhance effectiveness of the audit product if the audit methodology was also risk based. The key elements of a risk based audit approach should be to identify the risks to the achievement of the business objective and evaluating measures designed to mitigate them. The audit should focus on the broad headings of governance, risk management and internal control as each of these elements plays a part in supporting the achievement of the business objective and weaknesses in any of them may result in the objective not being fully achieved in the most efficient, effective or economic way.

#### **Recommendation:**

**The Audit and Risk Manager reviews the current approach to audit work to ensure that the scope of the work reflect more elements of governance and risk.**

Audit work is allocated by the auditors not the Audit and Risk Manager. Each auditor has their own programme of work which is scheduled for the audit year.

The Audit and Risk Manager monitors the individual programmes through the team meetings held every 4 weeks.

There is a standard format for audit working papers, but flexibility in the usage prevails. There is no laid down structure for audit files, other than the inclusion of the control sheet, the assignment brief and the audit programme. All audit files have a cover sheet and the evidence/working papers are filed behind that. Test control sheets are used for the audit of the key fundamental systems. One or two audits do not lead themselves to scoping in the usual way. Overall there is a flexible approach adopted by the audit staff, as there is no rigid process to follow.

One area of concern that I have with the audit process, revolves around the review of audit files. While the monitoring and review process is consistent, I feel that the lack of documented review points means that the individual auditors are not provided with adequate feedback on the working papers and report. It is unclear whether any factual inaccuracies, misunderstandings and so on are being picked up at this stage, or whether it is reliant on what is presented in the draft report. Internal audit staff have said that feedback on individual audits is infrequent. They will receive some queries from the Audit and Risk Manager on the report and there will be some re-wording of the content. The formal documentation that the review process has occurred is that the audit assignment control sheet is signed and dated by the Audit and Risk Manager.

**Recommendation:**

**The Audit and Risk Manager introduces a formal review and feedback process for all audits.**

My review highlighted that there is potential for the section to develop its use of IT management tools. The section benefits from the use of IDEA within its audit work. Although, it was clear from talking to individual staff that the usage of IT as a tool for auditing varies considerably between auditors. The efficiency of the section would benefit from the use of electronic working papers, as some staff still hand write their working papers. Individual audit files are still kept in paper format.

**Recommendation:**

**Auditors should be encouraged to produce electronic working papers for all audit work.**

**The Audit and Risk Manager considers the benefits of moving to electronic storage of all audit work rather than paper files.**

I have looked at a sample of internal audit reports and can conclude that they are of a suitable standard. Based on the scope of those audits, I believe that overall the content of the reports are focussed appropriately. However, I believe the risk around each control weakness could be made clearer to the recipient.

**Recommendation:**

**The Audit and Risk Manager considers the benefits to the recipient of the report of providing a clearer explanation of the risk(s) associated with the control weakness identified.**

Audit reports provide an opinion on the level of assurance provided by the controls within each area. The team has defined 3 categories of assurance for its opinion, which I believe are appropriate.

Each auditor has their own individual style of auditing. There is no prescribed formula/format that they must rigidly follow. This does mean that the output (the final audit report) does vary in style from auditor to auditor, but not to a degree that would cause concern.

The Audit and Risk Manager has identified specific quality standards that he expects to find in each audit report. He also seeks to implement best practice through process benchmarking (CIPFA Benchmarking Club) and networking with other Heads of Internal Audit.

Effectiveness of the service could be improved further by the implementation of an electronic audit management system to help monitor the day to day workings of the team and provide a more efficient solution for generating data and information for senior management.

**Recommendation:**

**The Audit and Risk Manager should consider the benefits of implementing an electronic management system.**

**3.6 Professional Standards:**

Standards provide a consistent framework of professional practice. Standards shape the application of other inputs and define the key relationships with the organisation. They are the fundamental building block for effectiveness and the starting point for any internal audit team.

When considering other inputs to effective internal audit, such as leadership or customer focus, professional standards will provide essential guidance, direction and consistency.

Compliance with professional standards is a responsibility of the organisation but also an individual responsibility for an internal auditor. Continuing professional development is essential to fulfil that responsibility.

Internal Audit has been reviewed against the CIPFA "Code of Practice for Internal Audit in Local Government in the UK" every 3 years by the External Auditor.

#### **4. Conclusions**

My overall conclusion is that Warwick District Council has an Internal Audit service that is fit for purpose. I have made a number of best practice recommendations that I believe if implemented will improve the effectiveness of the team.

**Better Governance Forum:  
Establishing Effectiveness of Internal Audit – Summary Assessment Table**

**Leadership**

Criteria	Yes	Partial	No
Establishes a clear vision for internal audit which is understood by the internal audit team and endorsed by the organisation.	√		
Offers strategic thinking on issues around governance and control.		√	
Champions good governance and good management.		√	
Maps how internal audit contributes to the achievement of organisational objectives.		√	
Forms effective relationships with senior managers, audit committee, external audit and other stakeholders.	√		
Embodies integrity.	√		
Influences, persuades and negotiates to support improvement and the achievement of the organisation's objectives.		√	
Influences, persuades and negotiates to raise the profile of internal audit and foster understanding.		√	
Recognised as a professional.	√		
Establishes performance standards and ensures delivery.	√		
Applies professional standards to the benefit of the internal audit service and the organisation.	√		
Communicates well with the internal audit team and encourages good communication within the team and by the team.	√		
Establishes the values of the audit team.	√		
Promotes innovation and continuous improvement in the internal audit team and across the organisation.		√	

**Governance & Relationships**

Criteria	Yes	Partial	No
The organisation has identified and adopted a comprehensive assurance framework and is clear about the role of internal audit within it.		√	
A fit for purpose audit committee has been established that complies with appropriate best practice with trained and effective members.		√	
The audit committee both supports internal audit and provides constructive challenge.	√		
Understanding of the principles of good governance throughout the organisation and governors and managers provide leadership and commitment to improving governance.		√	
Positioning and profile of internal audit within the organisation that includes clarity of internal audit's role and relationship with the rest of the organisation.	√		
Support for internal audit from senior management and a positive approach that sets the tone for the rest of the organisation.	√		
Reporting and management arrangements that support the independence of internal audit.	√		
Resourcing of internal audit that is realistic and appropriate for the assurance needs of the organisation.	√		
Good communications between the internal audit team and external stakeholders.	√		
Relationships between external audit and internal audit are professional and cooperative; meet the needs of both for good planning and coordination. Audit functions work together in the interests of public accountability and stewardship.	√		
The need for openness, honesty and a role free from conflict is vital to maintain internal audit independence and ensure effective use of internal audit resources.	√		

## Customer Focus

Criteria	Yes	Partial	No
Links internal audit and its work to the achievement of the organisation's objectives, the management of its risks, and its need for assurance.		√	
Consults with clients and stakeholders to develop an appropriate strategy, plan and approach to audit.	√		
Demonstrates an understanding of other assurances within the organisation.		√	
Auditing what matters.	√		
Understand current and future challenges, risks and opportunities to the organisation and its services.	√		
Clearly identifies its range of clients and stakeholders within the organisation and, where appropriate, adapts its approach to meet their various needs.	√		
Ensures that the principles of value for money are incorporated into the audit strategy.		√	
Focus on delivery of audit to defined standards of quality & timeliness.	√		
Focus on customer feedback & satisfaction to improve the service.	√		
Balances the organisation's and individual customer's needs and manages expectations in a realistic way.	√		
Provides practical recommendations and solutions through understanding the environment within which the organisation operates and the challenges faced.	√		

## People

Criteria	Yes	Partial	No
The people strategy for the internal audit service needs to align with the internal audit strategy.			√
The people strategy should contain appropriate people management arrangements for the recruitment, training, performance management and professional development of internal auditors.			√
According to their role, internal auditors should have the appropriate technical skills and knowledge to perform effectively and access to training and other material to maintain their skills.		√	
Behavioural skills such as communication, assertiveness, negotiation and influencing skills are key to the delivery of audit work, building relationships and fostering understanding of audit, control and governance issues.	√		
Both team and auditor must focus on the achievement of objectives, including professional standards, quality and timeliness.	√		
Personal qualities of internal auditors, including integrity, objectivity and honesty are key for establishing trust and respect in the service.	√		
Well motivated staff, with the right attitude to internal audit, are invaluable.	√		
The culture of the internal audit team should support, encourage and recognise innovation and continuous improvement in the team.	√		
A supportive team ethos will help the team to maximise its talents and resources for the benefit of the organisation and for the individual.	√		

## Systems & Processes

Criteria	Yes	Partial	No
Ways of working that support the delivery of high quality internal audit will be regularly reviewed to maintain efficiency, relevance and effectiveness.		√	
Quality standards for audit methodology help to ensure consistency and adherence to professional standards.		√	
High quality, focused reports can help communicate the output of the audit and improve impact of audit.	√		
Monitoring and review processes help to ensure consistency and achievement of performance standards.		√	
Quality review processes also support the learning and development of staff.		√	
Work allocation takes account of the skills and experience required for the audit but also encourages staff development and a fresh perspective.		√	
IT management tools may improve the efficiency of audit working and provide a more extensive service to the client.		√	
IT analysis tools may extend the range and depth of internal audit work and enhance the assurance provided by the audit.		√	
A performance management approach should be adopted to include the economy and efficiency of internal audit and to drive improvement over time.	√		
Audit recommendations and other guidance should be realistic, achievable and practical for the benefit of the organisation.	√		