

BURNLEY BOROUGH COUNCIL

**PEER REVIEW OF INTERNAL AUDIT AGAINST THE UK
PUBLIC SECTOR INTERNAL AUDIT STANDARDS**

JUNE 2017

Final Report – Issued 19th July 2017

Review Team

Mark Beard, Head of Audit and Investigations, Hyndburn Borough Council

Farhan Khaliq, Audit Manager, Pendle Borough Council

1 Introduction

- 1.1 All principal local authorities and other relevant bodies subject to the Accounts and Audit (England) Regulations 2015 (amended), the Accounts and Audit (Wales) regulations 2005, section 95 of the Local Government (Scotland) Act 1973 and the Amendment to the Local Government (Accounts and Audit) Regulations (Northern Ireland) 2006 must make provision for internal audit in accordance with the Public Sector Internal Audit Standards (PSIAS) as well as the (CIPFA) Local Government Application Note.
- 1.2 A professional, independent and objective internal audit service is one of the key elements of good governance in local government.
- 1.3 The PSIAS require that an external assessment of an organisation's internal audit function is carried out once every five years by a qualified, independent assessor or assessment team from outside of the organisation. External assessments can be in the form of a full external assessment, or a self-assessment with independent external validation.
- 1.4 The Lancashire Districts Chief Auditor Group (LDCAG) has established a 'peer-review' process that is managed and operated by the constituent authorities. This process addresses the requirement of external assessment by 'self-assessment with independent external validation' and this report presents the summary findings of the review carried out on behalf of Burnley Borough Council.
- 1.5 "An independent assessor or assessment team" means not having either a real or an apparent conflict of interest and not being a part of, or under the control of, the organisation to which the internal audit activity belongs." This review has been carried out by the Heads of Internal Audit at Hyndburn and Pendle Borough Councils. Their 'pen pictures', outlining background experience and qualifications, are included at **Appendix A**.

2 Approach/Methodology

- 2.1 The LDCAG has agreed a detailed Memorandum of Understanding (MoU) that outlines the broad methodology for the conduct of this review. A copy of the MoU is available upon request. However, in summary, the key elements of the process are:
 - The peer review is undertaken in three stages: pre-review; on-site review; post-review and covers audit activity during the period covered in the latest Head of Internal Audit Annual Report and Opinion. For this review the Internal Audit Annual Report for the year ending 2015/16 has been considered and so the time scale is from 1st April 2015 to 31st March 2016 although evidence demonstrating key points or aspects of the Standards has been considered from examples relating to year ending 2016/17.
 - Burnley Borough Council has completed and shared its self-evaluation of the Internal Audit service together with any relevant supporting

evidence/documentation in advance of on-site review commencement. The LDCAG has agreed that the self-assessment will use the **CIPFA Local Government Application Note (LGAN)** questionnaire. Typically, supporting evidence will include the Internal Audit Plan & Charter, The Head of Internal Audit Annual Report and Opinion, Quality Assurance and Improvement Programme and examples of final audit reports.

- To support the on-site review, a customer survey form has been issued to key personnel within the authority being reviewed.
- The review itself comprised a combination of ‘desktop’ and ‘actual on-site’ review.
- The review cannot reasonably consider all elements of the LGAN self-assessment and the review team used the ‘desktop’ period to determine strengths, weaknesses and subsequent key lines of enquiry in order that the review itself is risk-based, timely and adds real value. Burnley’s Internal Audit has been assessed against the three broad themes of: Purpose and Positioning; Structure and Resources; and Audit Execution. Impact is considered an overarching theme within these areas.
- Upon conclusion, the Review team offers a ‘true and fair’ judgement and each Authority will be appraised as **Conforms**, **Partially Conforms** or **Does Not Conform** against each thematic area of the LGAN, from which an aggregation of the three themed scores gives an overall Authority score.

3 Summary Findings

3.1 Following a detailed examination process, the review team has concluded the following judgements:

Area of Focus	Judgement
Purpose & Positioning	Conforms
Structure & Resources	Conforms
Audit Execution	Conforms
Overall Judgement:	Conforms

Assessment against the individual elements of each area of focus is included in the table at **Appendix B**.

Within the checklist there are 327 questions on CIPFA LGAN Checklist with the Standards. The Peer Review identified only 4 points for consideration into the service’s QAIP (Quality Assurance & Improvement Programme). Whilst there are only 4 areas these do collectively impact on 14 of the standards.

This is a significant and remarkable level of compliance with the Standards in excess of 95%.

Whilst not specifically covered by the Peer Review there were some specifically positive points of action. The service's benchmarking outcomes indicate an economic and efficient service. The auditors were experienced and knowledgeable on the audit areas which enables this and the audit process is streamlined to achieve tight delivery timescales. The assurance coverage was tailored to the requirements of the organisation and the Audit Manager is providing significant added value to numerous processes and areas for the Council which go beyond the Internal Audit role he has. However, this could create risk to internal audit independence and the ability to independently audit these areas with plans to move the Senior Auditor into Accountancy Team in September 2017. It must also be noted that all interviewees spoke in extremely high regard of the Audit Manager too.

The audit working papers and documenting process was well organised and provided a clear audit trail. The reports were found to be concise yet the reader was able to fully understand the issues arising and reasons for recommendations.

3.2 Significant Observations (i.e leading to a 'does not conform' judgement)

There are no significant observations

3.3 Minor Observations (i.e areas for improvement/development, minor elements of non-conformance, gaps in 'good practice' statement)

The minor observations are detailed in 3.3.1 to 3.3.10 below.

Purpose and Positioning

3.3.1 The Peer Review Team identified the potential for conflict of interest / priorities arising from the Chief Audit Executive also being the Head of Finance and s151 Officer, therefore the needs of the s151 role could clearly outweigh the needs of the CAE role. This is closely linked to independence which is set out in 3.3.2 below.

3.3.2 The Peer Review Team identified potential independence conflicts arising from the Head of Finance also acting as the Chief Audit Executive. Some functions of the CAE are not carried out by him but are in reality carried out by the Audit Manager. The CAE cannot claim that they are truly independent when responsible for the organisations financial affairs, aspects of which fall within the Internal Audit work remit. It is recognised that this structure has only existed since January 2017. The Peer Review Team must highlight this as a

potentially significant area that could impact on the Audit Team's ability to conform with the Standards in future.

Audit Execution

- 3.3.3** The Peer Review Team found that the Quality Assurance & Improvement Programme (QAIP) whilst technically in existence lacked detail. The QAIP could contain more information including more detail on how issues that do not conform with the Standards are going to be addressed to enable future compliance.
- 3.3.4** The Standards state that certain documents produced by an Audit Team should be presented to Senior Management and the Board which in Burnley's case would be the Management Team and Audit & Standards Committee. Whilst the key documents referred to in the Standards exist, not all had been to both Management Team and Audit & Standards Committee. This should be addressed to ensure continued conformity with the Standards going forwards.

Aspects of the Audit Process

- 3.3.5** The Peer Review Team believes the Audit Charter could be updated to include some areas currently not detailed and expand some of the other areas slightly with more detail. The Charter has not been updated in line with the changes to the Standards which came into effect on 1st April 2017 which include the Mission and 10 Core Principles. These changes reflect the changes to the mandatory elements of the International Professional Practices Framework which came into effect on 1st January 2017. Inclusion of these elements would link bank to the Standards and would improve the quality of the Audit Charter itself.
- 3.3.6** The Audit Manager stated that only high risks are monitored as part of the follow-up process but also stated that there have been no high-risks identified in audit work during recent financial years. This in effect means that no-follow work takes place. Follow-up work is defined within the Standards and this could lead to non-conformance with the Standards in the future.
- 3.3.7** An issue highlighted to the Peer Review Team was the scoping of an Audit Engagement. We were told that Audit only include parts of some areas and it was felt that they miss the obvious or key parts of an area out of the scoped work on some occasions. The Peer Review Team realise that there are potential explanations for this but include the issue in this report to enable the Audit Team and Management to be satisfied that no issues on scoping could impact on future conformity with the Standards.

Audit Presence & Visibility

- 3.3.8** The interview process highlighted comments that whilst the Audit Team is certainly not invisible within the Council which is very positive, there were comments that it was not clear of what else the Audit Team can do or provide

in addition to the anticipated scheduled Audit Engagements which could help and support Services in achieving their objectives.

- 3.3.9** The Peer Review Team also believes that the Audit Team is not easily visible to the Council's Senior Management Team. This is not a criticism of the Council's Management Team and we recognise that the Council's Head of Finance also acts as the Chief Audit Executive. However, it was clear that the day to day decisions and running of the Audit Team is carried out by the Audit Manager and whilst it was clear reports do go to Audit & Standards Committee it was not as clear as to what does or doesn't go to the Council's Management Team.

Future Risks to the Audit Team

- 3.3.10** The Peer Review Team became aware that there are plans to move the Senior Auditor to the Accountancy Team in September 2017. The Peer Review Team are not commenting on that decision as this clearly is a decision for Management. However, the Peer Review Team felt that they must highlight to Management that this decision could weaken the level of compliance with the Standards after that move takes place. Independence is maintained currently by being able to bypass the Audit Manager and utilise the Senior Auditor with support of the Audit Assistant to carry out audit work that the Audit Manager is unable to do due to independence conflicts as he has been a key part of systems design, contract support & evaluation, bid writing/support etc. This could not be maintained after the move which will in turn reduce Standards compliance.

3.4 PSIAS Action Table

This details suggested actions to improve the service, its status or impact and quality of the service provided. The points raised in 3.3 above are contained in this action table at **Appendix C**.

Review Team

Mark Beard

Mark has been Head of Audit and Investigations at Hyndburn Borough Council for 15 years but has over 26 years Audit experience. He has a wealth of experience in the management and operation of internal audit in district councils and is a fully qualified member of the Chartered Institute of Internal Auditors. His expertise in counter fraud is well respected in the Lancashire District Chief Audit Group.

Farhan Khaliq

Farhan is currently the Audit Manager for Pendle Borough Council and has worked with Pendle's Internal Audit Team for 16 years gaining a variety of experience during that time. He is a fully qualified member of the Association of Chartered Certified Accountants.

Detailed Assessment

PSIAS Ref		Conforms	Partially conforms	Does not conform	Comments
Purpose & positioning					
1000	• Remit	X			See 3.3.1 above
1000	• Reporting lines	X			
1110	• Independence	X			See 3.3.2 above
2010	• Risk based plan	X			
2050	• Other assurance providers	X			
Structure & resources					
1200	• Competencies	X			
1210	• Technical training & development	X			
1220	• Resourcing	X			
1230	• Performance management	X			
1230	• Knowledge management	X			
Audit execution					
1300	• Quality Assurance & Improvement Programme	X			See 3.3.3 above
2000	• Management of the IA function	X			
2200	• Engagement planning	X			
2300	• Engagement delivery	X			
2400	• Reporting	X			See 3.3.4 above
2450	• Overall opinion	X			

Conforms	X	Partially Conforms		Does Not Conform	
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Burnley Borough Council Internal Audit Service – PSIAS Action Table

Appendix C

The following points for consideration to develop the Audit Function arise from the review undertaken:

PSIAS Ref	Report ref	Point For Consideration	Responsible	Action
Definition of Internal Audit 1110 Organisational Independence 1130 Impairment to Independence or Objectivity 1210 Proficiency	3.3.1	The Peer Review Team identified the potential for conflict of interest / priorities arising from the Chief Audit Executive also being the Head of Finance and s151 Officer, therefore the needs of the s151 role could clearly outweigh the needs of the CAE role. This is closely linked to independence.		
Definition of Internal Audit 1000 Purpose, Authority & Responsibility 1110 Organisational Independence	3.3.2	The Peer Review Team identified potential independence conflicts arising from the Head of Finance also acting as the Chief Audit Executive. Some functions of the CAE are not carried out by him but are in reality carried out by the Audit Manager. The CAE cannot claim that they are truly independent when responsible for the organisations financial affairs, aspects of which fall with the Internal Audit remit. It is recognised that this structure has only existed since January 2017. The Peer Review Team must highlight this as a potentially significant		

PSIAS Ref	Report ref	Point For Consideration	Responsible	Action
1300 Quality Assurance & Improvement Programme 1310 Requirements of the Quality Assurance & Improvement Programme 1320 Reporting on the Quality Assurance & Improvement Programme 1321		area that could impact on the Audit Team's ability to conform with the Standards in future.		
	3.3.3	The Peer Review Team found that the Quality Assurance & Improvement Programme (QAIP) whilst technically in existence lacked detail. The QAIP could contain more information including more detail on how issues that do not conform with the Standards are going to be addressed to enable future compliance.		
2020 Communication & Approval	3.3.4	The Standards state that certain documents produced by an Audit Team should be presented to Senior Management and the Board which in Burnley's case would be the Management Team and Audit & Standards Committee. Whilst the key		

PSIAS Ref	Report ref	Point For Consideration	Responsible	Action
		documents referred to in the Standards exist, not all had been to both Management Team and Audit & Standards Committee. This should be addressed to ensure continued conformity with the Standards going forward.		
N/A Identified by Observations	3.3.5	The Peer Review Team believes the Audit Charter could be updated to include some areas currently not detailed and expand some of the other areas slightly with more detail. The Charter has not been updated in line with the changes to the Standards which came into effect on 1 st January which include the Mission and 10 Core Principles. Inclusion of these elements would link bank to the Standards and would improve the quality of the Audit Charter itself. Management should therefore consider whether they are satisfied with current Charter and whether to ask for it to be updated.		
N/A Identified by Interviews	3.3.6	The Audit Manager stated that only high risks are monitored as part of the follow-up process but also stated that there have been no high-risks identified in audit work during recent financial years. This in effect means that no-follow work takes place. Follow-up work is defined within the Standards and this could lead to non-conformance with the Standards in the		

PSIAS Ref	Report ref	Point For Consideration	Responsible	Action
		<p>future.</p> <p>Management should consider whether follow-up of other risks should take place if no risks are deemed high risk which automatically results in follow-up.</p>		
N/A Identified by Interviews	3.3.7	<p>An issue highlighted to the Peer Review Team was the scoping of an Audit Engagement. We were told that Audit only include parts of some areas and it was felt that they miss the obvious or key parts of an area out of the scoped work on some occasions. The Peer Review Team realise that there are potential explanations for this but include the issue in this report to enable the Audit Team and Management be satisfied that no issues on scoping could impact on future conformity with the Standards..</p> <p>Management and the Audit Manager should consider whether they are satisfied with current arrangements on scoping of audit work or if some change in processes is required.</p>		
N/A Identified by Interviews	3.3.8	<p>The interview process highlighted comments that whilst the Audit Team is certainly not invisible within the Council which is very positive, there were comments that it was not clear of what else the Audit Team can do or provide in addition to the anticipated scheduled Audit Engagements which could help and</p>		

PSIAS Ref	Report ref	Point For Consideration	Responsible	Action
N/A Identified by Interviews		support Services in achieving their objectives. Management should consider whether they are satisfied with the current position of whether the Audit Team should make Services more aware of how they could support Services.		
	3.3.9	The Peer Review Team also believes that the Audit Team is not easily visible to the Council's Senior Management Team. This is not a criticism of the Council's Management Team and we recognise that the Council's Head of Finance also acts as the Chief Audit Executive. However, it was clear that the day to day decisions and running of the Audit Team is carried out by the Audit Manager and whilst it was clear reports do go to Audit & Standards Committee it was not as clear as to what does or doesn't go to the Council's Management Team. Management and the Audit Manager should consider whether they are satisfied with current arrangements and what could be done to change these perceptions which could impact on future conformance with the Standards.		
N/A Identified by Interviews	3.3.10	The Peer Review Team became aware that there are plans to move the Senior Auditor to the Accountancy Team in September 2017. The Peer Review Team		

PSIAS Ref	Report ref	Point For Consideration	Responsible	Action
		<p>are not commenting on that decision as this clearly is a decision for Management. However, the Peer Review Team felt that they must highlight to Management that this decision could weaken the level of compliance with the Standards after that move takes place. Independence is maintained currently by being able to bypass the Audit Manager and utilise the Senior Auditor with support of the Audit Assistant to carry out audit work that the Audit Manager is unable to do due to independence conflicts as he has been a key part of systems design, contract support & evaluation, bid writing/support etc. This could not be maintained after the move which will in turn reduce Standards compliance.</p> <p>Management should consider how they will maintain the necessary levels of independence with the Audit Team to enable continuing conformance with the Standards in this area.</p>		