

To: Audit, Risk and Scrutiny Board

On: 19 March 2018

Report by: Chief Auditor

Heading: Internal Audit Reporting to Board

1. Summary

- 1.1 In line with the Public Sector Internal Audit Standards (PSIAS), Internal Audit must communicate the results of each engagement to the Board.
- 1.2 In March 2017, our external quality assessment, undertaken as part of a peer review process, by West Lothian Council's Audit, Risk and Counter Fraud Manager, identified that there was scope to improve the information provided to the Board in relation to finalised audit engagements and follow up work. The recommendation was reiterated in Audit Scotland's annual review of the adequacy of Internal Audit for the period to 31 March 2017.
- 1.3 The Chief Auditor undertook to review the information provided to Board in relation to completed audit engagements by September 2017 and the arrangements for reporting on follow up work by March 2018. Enhanced reporting arrangements for completed audit engagements were put in place in August 2017 and a further enhancement was made in November 2017, to include a section on each committee summary for management commentary.
- 1.4 The Board requested that in relation to those recommendations that are critical, the Chief Auditor gives consideration as to whether more detailed information could be provided to the Board.

- 1.5 This report outlines the details and outcome of those considerations in relation to the Board reporting arrangements for completed engagements and follow up work.

2. Recommendations

- 2.1 Members are requested note the reporting arrangements put in place to communicate the results of Internal Audit work to the Board.

3. Background

3.1 Communicating the results of audit engagements

- 3.1.1 In line with the Public Sector Internal Audit Standards (PSIAS), Internal Audit must communicate the results of each engagement to the Board.

- 3.1.2 Prior to the establishment of the Audit, Risk and Scrutiny Board, the predecessor Audit, Scrutiny and Petitions Board received a quarterly summary of findings report which highlighted the main issues arising from each finalised audit engagement. The internal audit annual report also included the overall implementation statistics for all audit recommendations that had been reviewed as part of the annual follow up exercise.

- 3.1.3 The external quality assessment report, identified two findings and recommendations in relation to the information presented to the Board:

- 1) *The Audit, Scrutiny and Petitions Board (ASPB) receives quarterly summaries of audit reports issued.*

Section 2060 of the PSIAS states that reporting must include significant risk exposures and control issues.

In order to fully comply with this requirement, more detailed information should be provided to the Board, particularly where the Chief Auditor concludes that the assurance level is limited.

This may be achieved by submitting selected internal audit reports to the Board, or by submitting more detailed information on risk exposures and control issues, including the management response.

- 2) *The annual report contains summary information in relation to the implementation of follow up recommendations.*

The local government application note, which was developed as a local government specific set of requirements within the PSIAS, requires the effective involvement of the Board in the follow up process.

Consideration should therefore be given to reporting details of the specific outstanding recommendations to the Board, particularly those which are ranked “A”, the highest category of importance.

- 3.1.4 To comply with the requirements of the PSIAS, and to address recommendation 1 above, the Chief Auditor enhanced the quarterly reporting arrangements, to include an overview report detailing the overall assurance level for each engagement as either, substantial, reasonable, limited or no assurance and the number of recommendations in each recommendation category as either, critical, important, best practice or service improvement.
- 3.1.5 This overview report is supported by a more detailed committee summary for each engagement which details the objectives of the audit, the scope of the work undertaken, the key assurances that can be provided to the Board and any key risks that need to be brought to the attention of the Board along with the Chief Auditor’s overall opinion in relation to those objectives reviewed. It should be noted that there is no direct correlation between the number of key risks recorded on the committee summary and the number of recommendations rated as critical, as there could be several recommendations made to address a single risk. There is also a section included on the committee summary for service management to provide assurance to the Board on the steps being taken to address any key risks identified.
- 3.1.6 The Board requested that in relation to those recommendations that are rated as critical, the Chief Auditor gives consideration as to whether more detailed information could be provided to the Board. In making those considerations the Chief Auditor took account of the professional requirements as detailed in the PSIAS, CIPFA guidance “Audit Committees, Practical Guidance for Local Authorities” and legislative requirements such as the Data Protection Act, and the assessed risks to the Council.
- 3.1.7 The PSIAS encompass the mandatory elements of the Institute of Internal Auditors (IIA) International Professional Practices Framework (IPPF) and has been issued by CIPFA, who set the internal auditing standards for UK Local Authorities. The Chief Auditor has a professional duty under the PSIAS to report the results of engagements to senior management and the Board, although the PSIAS does not prescribe any specific format that should be adopted for reporting.
- 3.1.8 The PSIAS places certain professional obligations on the Chief Auditor in relation to the confidentiality and disclosure of the information they receive during the course of each audit engagement.

- 3.1.9 The PSIAS states that “the chief audit executive must control access to engagement records. The chief audit executive must obtain the approval of senior management and/or legal counsel prior to releasing such records to external parties, as appropriate”.
- 3.1.10 It also states that:
“Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.”

If not otherwise mandated by legal, statutory, or regulatory requirements, prior to releasing results to parties outside the organisation the chief audit executive must:
- assess the potential risk to the organisation
 - consult with senior management and/ or legal counsel as appropriate, and
 - control dissemination by restricting the use of the results.”
- 3.1.11 The Chief Auditor has a critical role in delivering the council’s strategic objectives by promoting best practice in governance, objectively assessing the adequacy of governance and management of existing risks, commenting on responses to emerging risks and proposed developments; and giving an objective and evidence based opinion on all aspects of governance, risk management and internal control.
- 3.1.12 The Audit, Risk and Scrutiny Board fulfils the role of the Audit Committee within the Council. An Audit Committee is a key component of good governance and they are an important source of assurance about the organisation’s arrangements for managing risk and maintaining an effective control environment. The role of members is to ensure that the planned programme of audit work provides sufficient coverage to inform the Chief Auditor’s annual opinion, consider the assurances and risks arising from the work of Internal Audit, seek assurance that the risks are being adequately addressed and monitor the performance of the Internal Audit function.
- 3.1.13 Members of the Audit, Risk and Scrutiny Board need to be provided with enough information to allow them to undertake their role as “audit committee” members and to understand any significant risk exposures to the council’s internal control environment identified through the work of Internal Audit.
- 3.1.14 The CIPFA “Audit Committees, Practical Guidance for Local Authorities” publication, defines that role as “The audit committee’s role in relation to reviewing the work carried out will include formal consideration of summaries of work done, key findings, issues of concern and action in hand as a result of audit work.”
- 3.1.15 In assessing the potential risk to the organisation of further disclosure of those recommendations rated as critical, it is the Chief Auditor’s opinion that, it would not be in the interests of the Council to disclose the

detailed recommendations to the Audit, Risk and Scrutiny Board for the following reasons:

- Further disclosure would expose the most significant weaknesses identified through the internal audit process in the public domain, presents a risk of exploitation of those weaknesses, exposing the council to the risk of fraud or other malicious acts.
- The most significant weaknesses are often identified through the investigation of suspected wrongdoing and may involve employees, community groups or contractors. Full disclosure could breach data protection legislation if individuals can be identified from the information that goes into the public domain.
- Internal Audit investigations are occasionally referred to the Police or other investigative agencies, disclosure could prejudice those investigations.
- Further disclosure would compromise the Chief Auditor's accountability for confidentiality, as the Chief Auditor would lose control over the dissemination and use of the information.
- Members of the Audit, Risk and Scrutiny Board have direct and unfettered access to the Chief Auditor and can obtain further briefings in relation to any matter reported to the Board. Members also have rights of access to information relating to matters being considered by the Board, although those rights are subject to restrictions.

3.1.16 The Chief Auditor is satisfied that the enhanced reporting to Board put in place along with enhanced representation from service management at Board meetings fully supports the Board in their role as the audit committee, complies with the PSIAS and meets the best practice standard as set out in the CIPFA "Audit Committees, Practical Guidance for Local Authorities" publication.

3.2 Monitoring the progress of management actions

3.2.1 The PSIAS places the responsibility for monitoring progress with the Chief Auditor to ensure that management actions have been effectively implemented, or, if not, that senior management have accepted the risk of not taking action.

3.2.2 The Chief Auditor must implement a follow-up process for ensuring the effective implementation of audit results or ensuring senior management are aware of the consequences of not implementing an action point and are prepared to accept the risk of such consequences occurring. The results of this process should be communicated to the Board.

3.2.3 There is also a requirement for the Chief Auditor to develop escalation procedures for cases where agreed actions have not been effectively

implemented by the date agreed. These procedures should ensure that the risks of not taking action have been understood and accepted at a sufficiently senior management level. The effective involvement of the Board in the follow-up process is critical to ensuring that it works.

3.2.4 Internal Audit undertakes an annual follow up exercise. The focus of each annual follow up exercise can vary depending on the audit resources available. All critical recommendations followed up must be supported by evidence to demonstrate that they have been implemented.

3.2.5 The outcome of the annual follow up exercise is communicated to Service Directors with details of all partially implemented, redundant and outstanding recommendations. The Chief Auditor currently reports, for the Council as a whole, the number of recommendations followed up, and the current status of those recommendations in the Internal Audit annual report.

3.2.6 It is the Chief Auditor's opinion that there is an opportunity to enhance the escalation procedures for cases where agreed actions have not been effectively implemented by the date agreed. The currently reported information will be split by service and details of outstanding critical recommendations will be provided to the Board. The Chief Auditor would still need to preserve the confidentiality of the information in cases where it may breach legislation or where the risk of the weakness being exploited be of such significance that she would seek to have the report heard in private, to protect the Council's interests.

3.2.7 It is our intention to develop the audit management system to facilitate 'self-service' within the services, in relation to updates on the progress of implementing recommendations. This development would facilitate more regular reporting of outstanding actions in the future.

3.3 Communicating the acceptance of risks

3.3.1 The PSIAS places certain professional obligations on the Chief Auditor to report to the Board when in the Chief Auditor's opinion management have accepted an unacceptable level of risk. The PSIAS states, "when the chief audit executive concludes that management has accepted a level of risk that may be unacceptable to the organisation, the chief audit executive must discuss the matter with senior management. If the chief audit executive determines that the matter has not been resolved, the chief audit executive must communicate the matter to the board."

3.3.2 Although instances where the Chief Auditor and senior management are unable to reach an agreement on actions to mitigate a significant risk to an acceptable level are rare. However, should such an instance arise the Chief Auditor will bring a report outlining the risk exposure to the Board.

Implications of the Report

1. **Financial** – Any financial implications will be negligible.
2. **HR & Organisational Development** - None
3. **Community Planning –
Safer and Stronger** - effective internal audit service and audit committee arrangements is an important element of good corporate governance.
4. **Legal** – Any legal implications are detailed in the report
5. **Property/Assets** - None
6. **Information Technology** - None
7. **Equality & Human Rights** - None
8. **Health & Safety** – None
9. **Procurement** - None
10. **Risk** – The risk implications have been detailed in the report.
11. **Privacy Impact** – None
12. **COSLA Implications** - None

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