

## **GOVERNANCE & AUDIT COMMITTEE: 24 JANUARY 2023**

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### **DRAFT INTERNAL AUDIT CHARTER AND DRAFT AUDIT PLAN 2023/24**

#### **REPORT OF THE AUDIT MANAGER**

#### **AGENDA ITEM: 7.2**

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#### **Reason for the Report**

1. The Terms of Reference for the Governance and Audit Committee sets out its responsibility:
  - To approve the Internal Audit Charter.
  - To approve the risk-based Internal Audit Plan, containing internal audit's resource requirements, the approach to using other sources of assurances and any work required to place reliance upon those other sources.
2. The Governance and Audit Committee has a responsibility to review its Terms of Reference annually.
3. This report has been prepared to provide Governance and Audit Committee Members with the Draft Internal Audit Charter for 2023/24 and appendices, including a draft Committee Terms of Reference. The report also provides the Draft Summary Audit Plan for 2023/24.

#### **Background**

4. At the commencement of each financial year, consideration is given to updating key documents which form part of the Internal Audit function. The draft documents are submitted to Governance and Audit Committee at the January meeting to enable members of the Committee to consider and feed in comments which will support the development of final documents to be approved on 21 March 2023 in respect of the new financial year.
5. Under the PSIAS (standard 1110 – organisational independence), the Governance and Audit Committee is required to approve the Internal Audit Charter and the risk based Internal Audit Plan. These documents are attached for 2023/24 in draft form, with the audit plan presented at a summary level of detail prior to the detailed review and population of audit engagements in quarter four 2022/23. Accompanying the Charter is a draft version of the proposed Committee Terms of Reference for 2023/24.
6. The Local Government and Elections (Wales) Act 2021 placed new responsibilities on the Governance and Audit Committee that were incorporated into its Terms of Reference as approved by Council on 27 May 2021. A particular responsibility of the Committee is to review and make recommendations on the Annual Wellbeing Report (the Council's statutory self-assessment report) each year, and the Panel Performance

Assessment Report including the Council's draft response, required at least once during an electoral cycle.

7. In updating the Committees Terms of Reference for the municipal year 2021/22, consideration was given to the new responsibilities arising from the Act, and the responsibilities and remit of the Council's Scrutiny Committees. The Governance and Audit Committee's focus of the above reviews relates to a high-level consideration of issues around securing performance requirements using the governance infrastructure of the Council, rather than on service area performance issues dealt with by Scrutiny Committees.
8. In considering its Terms of Reference for 2022/23, the Governance and Audit Committee was informed in its meetings in January and March 2022 of forthcoming updated guidance from the Chartered Institute of Public Finance and Accountancy (CIPFA), and Welsh Government statutory guidance relating to matters including Constitutions, Executives, Scrutiny, Overview and Scrutiny and Governance and Audit Committees. A proposal was agreed by Committee for a further review and update of its Terms of Reference to await the publication of the above guidance, to take place in sufficient time for the municipal year 2023/24.
9. The Updated CIPFA guidance and Welsh Government statutory guidance has subsequently been published and is reflected upon in the draft updated Terms of Reference proposed for the Governance and Audit Committee, as contained within Appendix D of the Audit Charter.

## Issues

### Audit Charter

10. The Draft Internal Audit Charter set out in **Annex 1** is a formal document which establishes the Internal Audit Service's position within the organisation, the Audit Manager's functional reporting relationship with the Governance and Audit Committee, authorises access to records, personnel, physical properties relevant to the performance of engagements, and defines the scope of internal audit activities. Governance and Audit Committee formally approved the Internal Audit Charter 2022/23 on 15 March 2022.
11. The Draft Audit Charter 2023/24 has been reviewed and updated. The areas in the Draft Audit Charter that have been adjusted are shown in red font. Contained within the Draft Internal Audit Charter are six appendices, which detail the parameters within which Internal Audit and the Governance and Audit Committee operate.
12. Appendix A sets out the Code of Ethics for Internal Auditors and is focussed on the four key principles of Integrity, Objectivity, Confidentiality and Competence. This appendix is formally used in the quality assurance process as part of each audit, and as part of ongoing performance reviews.
13. Appendix B sets out the Core Principles which taken as a whole, articulate internal audit effectiveness. These Core Principles underpin the Mission of the Internal Audit service *'To enhance and protect organisational value by providing risk based and objective assurance, advice and insight'* in recognition of best practice from the IIA.
14. Appendix C sets out the staffing resources allocated to the Internal Audit function as well as outlining the reporting lines between the Audit Manager, the Section 151 Officer

and the Governance and Audit Committee. This section also outlines the skill base of the team and the commitment to developing staff further through Audit or Investigation qualifications.

15. Appendix D suggests the Terms of Reference for the Governance and Audit Committee 2023/24, which has been updated to reflect both the best practice CIPFA guidance, and the Welsh Government statutory guidance following their publication in recent months. The proposed Terms of Reference shows the suggested changes from the current version. Suggested new wording is shown in red, and wording suggested for removal is shown in grey and crossed through. The pertinent proposed updates to the Committee's Terms of Reference are:
  - A short introductory paragraph, setting out the nature of the Committee and to whom it reports, in accordance with CIPFA guidance.
  - An updated Statement of purpose, incorporating the updated best practice CIPFA wording, as well as a point of clarification on the separate demarcation between Governance and Audit and Scrutiny Committees, in accordance with Welsh Government statutory guidance.
  - Expanded details on the Committee's Treasury Management responsibilities and remit based on the CIPFA guidance. Details are also provided on Council Treasury Management delegations and responsibilities.
  - Further minor changes in wording in accordance with CIPFA guidance.
16. Appendix E sets out the Quality Assurance and Improvement Programme (standard 1300), which is designed to enable an evaluation of the Internal Audit section's conformance with the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The programme also assesses the efficiency and effectiveness of the internal audit activity and is used to identify and deliver opportunities for improvement. The QAIP is built around a performance management approach which involves 'setting expectations', 'reviewing performance', and 'reporting performance' at individual auditor and team levels.
17. Appendix F contains the Audit Protocol, which represents an outline of the audit process from planning to reporting.

### **Audit Plan, 2023/24**

18. Contained within both the Draft Internal Audit Charter and the Terms of Reference are sections outlining the submission of a risk-based audit plan to be approved by Committee. **Annex 2** contains the preliminary draft plan for 2023/24, which will be developed into further detail over the financial quarter to be submitted for approval by Governance and Audit Committee on 21 March 2023.
19. The draft Audit Plan for 2023/24 is based on a team of 7.82 operational auditors overseen by the Audit Manager and supported by an Audit Assistant. The available auditor time is 0.46 FTE auditors less than in the previous financial year, which is in accordance with the restructure reported to Governance and Audit Committee on 29 November 2022, whereby the decision was taken to invest in an additional principal auditor post, to enhance a solid core of senior officers within the team, subject to a successful recruitment campaign and to not fill vacant posts at lower grades. Further to this, a flexible retirement request has been approved for the Group Auditor through which their hours will reduce by 10 hours per week (from 37 to 27) from 1 April 2023. The available time also accounts for an Auditor's request to continue to work 11.5 additional hours (from 18.5 to 30 hours), and a Senior Auditor's request to make a permanent reduction to their hours from 37 to 32 hours per week, which has been

agreed following agreements in 4 consecutive years for these reduced working hours on a temporary basis.

20. The Audit Team benefits from CIPFA Trainee support during placements, and subject to a successful recruitment exercise for the academic year 2023/24, a CIPFA Trainee may be placed in Internal Audit. For prudence, no expectation of this additional resource is built into the Plan.
21. The number of available operational audit days has decreased (from 1555 to 1495) since last year, largely due to the headcount in the team being slightly lower, as referred to above. The main changes to time allocations since last year are as follows:
  - A greater proportion of time is being allocated to audits of fundamental systems than service specific audits, this follows a base-line approach to auditing such systems every other year, with the exception of creditor payments and processing, payroll and HR systems which are subject to annual audit.
  - A time allocation has been established for recommendation follow-up, consultation and guidance given the importance of audit support and engagement in these areas.
  - A time allocation has been established for participation in corporate wellbeing initiatives for the benefit of officers.
  - The time allocated to non-audit duties has increased, as the Audit Assistant has been allocated clerical support roles across the wider finance function as a greater proportion of their time, and three Members of the team have a combination of Employee Network and Trade Union roles.
  - A time allocation for COVID related absences has been removed, with such absences to now be recorded as general sickness.
22. The Investigation Team Plan is based on 2.42 FTEs. The available resource continues to reflect the ongoing wishes from an investigator to work 34 hour per week (3 hours less than their substantive post). Planning adjustments have been made in respect of non-chargeable time on a consistent basis to the Audit Team.
23. Members will note that the Audit Manager has not been included in the head count of FTE for either team, as this work focusses on strategy, and overseeing the quality, delivery and output across both audit and investigations teams.
24. The draft Audit Plan has been prepared at a summary-level following consideration of a risk-based methodology. The detailed components of the audit planning approach take place throughout quarter four, and will result in the full risk-based audit plan for 2023/24. The approach is designed to be risk based and co-ordinated in application of an assurance mapping exercise based on the IIAs “three lines model”.
25. The audit planning process involves the application of three basic review principles as follows:
  - (a) **Informed Inherent Risk** - The starting point is the development of an inherent audit need / risk score as a product of the nature of the potential audit area, and the results of Senior Management Assurance Statement (SMAS) responses from Directors.
    - Audit category - There are three broad audit categories which are audited with an inherent frequency in the following priority order from highest to lowest (1) Fundamental systems, (2) Governance functions (e.g., Health and Safety, Performance Management etc.) and (3) Operational audits, such as a school or standard system audit.

- **SMAS submissions** - The Directorate self-assessments of maturity in a number of core areas of governance, risk management and internal control are considered and used to moderate the inherent prioritisation of audit engagements.
- (b) **Coordination and Reliance** - After considering the inherent need for an audit, further sources of assurance and indicators of risk are accounted for, such as:
- Information on risk registers
  - Planned and programmed projects, scrutiny and management activities
  - Existing levels of Internal Audit assurance, and
  - Planned and actual work and findings from wider audit, regulatory and consultancy activities.
- (c) **Extensive and Appropriate Audit Coverage** - In consideration of the above two stages, audits will be programmed and typically delivered through a combination of Control Risk Self-Assessment (CRSA), thematic and full audit engagements. The above two stages are in the process of development through relationship management and audit link officer mechanisms in directorates.
26. Section 2010 of the PSIAS specifies that the risk-based plan takes into account the organisation's assurance framework and that the work of Internal Audit addresses both local and national issues. This is achieved through the approach as summarised above, with the assurance available from both within and outside the Council assessed to enable informed decisions regarding the audits to be undertaken in 2023/24. The Governance and Audit Committee will be aware that the Audit Plan is responsive to emerging risks and issues as they arise during the year, and these changes are brought to the Governance and Audit Committee as they arise.
27. The "three lines model" is an important part of the Council's internal control environment. Senior managers, as the first line of defence, have a joint and individual responsibility for risk management, governance and the control environment within their directorate; they use their SMAS as a primary disclosure of their delivery of the management controls and report and disclose on the management of their risks and performance. The second line of defence consists of the arrangements in place to monitor and support internal governance through functions which develop, embed and monitor policies and strategies, such as Risk Management, ICT, Information Governance and Health and Safety functions.
28. As the third line of defence, Internal Audit accounts for the assurance of the first two lines of defence together with external audit and regulatory sources of assurance and indicators of risk (e.g., Audit Wales and Estyn work), in developing a risk-based audit plan. The Summary Plan, as set out in Annex 2, will be fully developed during quarter 4 and supported by an assurance map to recognise and account for the respective internal and external sources of assurance and allocate audit resources to enable the Audit Manager to provide a comprehensive opinion on the overall Council control environment.
29. It is proposed to undertake fundamental audits in 2023/24 in relation to creditor payments and processing, payroll and HR, National Non-Domestic Rates (NNDR), Treasury Management, Main Accounting, Income and Debtors, Asset Management and Housing Rents. However, if there are any major system or operational changes during the year in systems that are not included in the plan, an audit of that system will be added to the Audit Plan (and this change reported to a meeting of this Committee).

