

SOUTHAMPTON CITY COUNCIL – INTERNAL AUDIT STRATEGY

4. DEVELOPING THE AUDIT PLAN

4.1. The audit universe

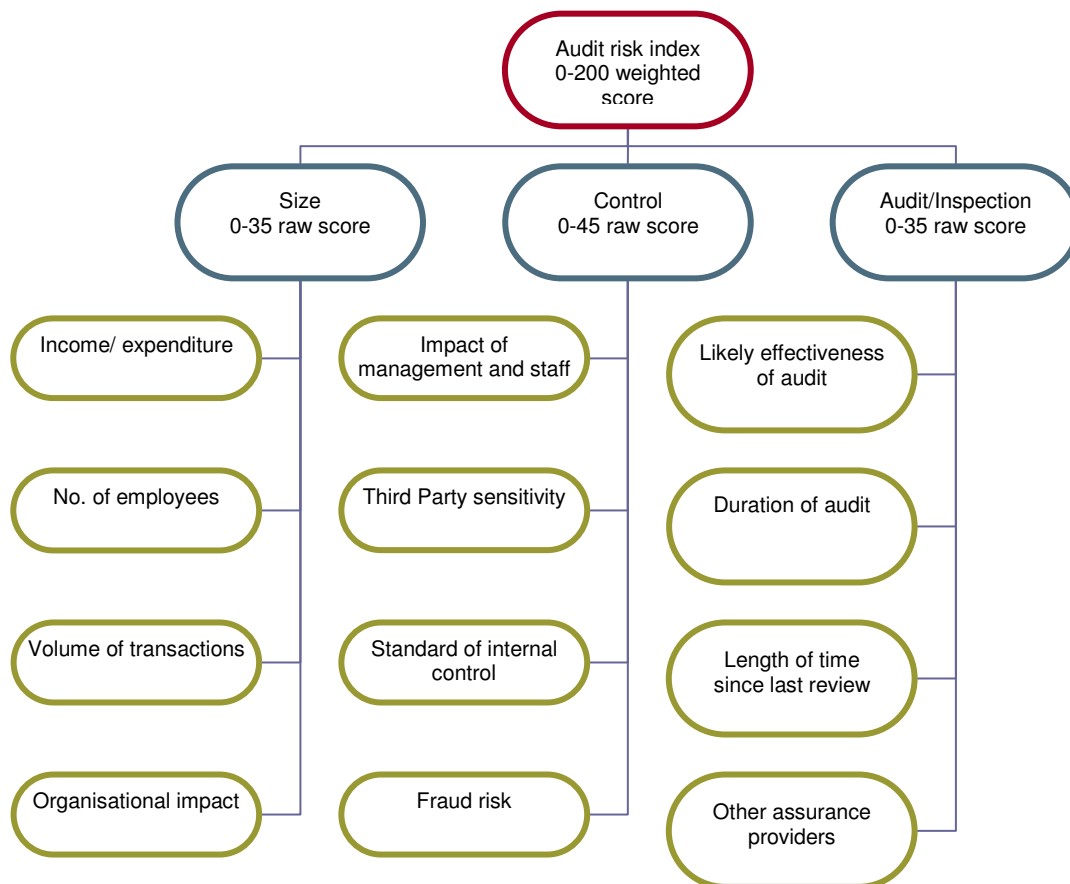
- 4.1.1. The requirement for internal audit to provide a clear opinion on internal control, risk management and governance arrangements, flowing from the Council's key objectives, provides a clear focus for the audit approach.
- 4.1.2. Internal audit will define the 'audit universe', from the Council's key priorities and delivery framework (Community Strategy, Medium Term Plan, Corporate Improvement Plan, Directorate and Divisional Business Plans, Risk Register), ensuring it contains the main business processes, projects, assets, performance and compliance issues significant to the Council's strategic direction, risk environment and goals. Definition of the audit universe will enable internal audit to demonstrate support to the annual corporate governance statement and will encompass the following core principles:
- focus on the Council's defined purpose and outcomes;
 - effective performance in clearly defined functions and roles;
 - promoting values that underpin good governance through upholding high standards of conduct and behaviour;
 - taking informed and transparent decisions within a framework of controls and managing risk;
 - developing the capacity and capability of members and officers to be effective; and
 - engaging stakeholders to ensure robust public accountability.
- 4.1.3. The audit universe will be subject to ongoing review and adjustment, to ensure it remains aligned with significant delivery objectives and risks and is responsive to the priorities and concerns of the management team. Amendments will be identified through internal audit's ongoing contact and liaison with those responsible for the governance of the Council (i.e. audit committee, chief officers, policy coordinators, heads of service).

4.2. Identifying audit needs

- 4.2.1. Internal audit will include biennial assessments of the effectiveness of the corporate risk management and performance management frameworks within its programme of work, to support the Council's development of risk and performance management and to identify the extent to which internal audit is able to rely on these assurance functions.
- 4.2.2. The corporate risk register and performance framework will be used to inform the risk assessment of the audit universe, but will be supplemented with internal audit's own assessment of risk and materiality. Over time, this assessment will draw more extensively from the Council's risk register.
- 4.2.3. Internal audit's assessment of risk will be broadly based on a best practice audit risk methodology (the Stanford University Model) which provides for a systematic appraisal of the elements of the audit universe to enable auditable areas to be risk scored and indexed relative to all other areas.

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Figure 1
Audit risk index



4.2.4. The risk profile of the audit universe will be presented to senior management and the Audit Committee, identifying the specific services, activities, processes or projects that present the highest inherent risks. This profile will form the basis of a three-year strategic plan of internal audit work and will be updated at least annually to take cognisance of changing priorities within the Council.

4.3. Producing the audit plan

4.3.1. An annual operational plan will be derived from the three year strategic plan using a cycle-based risk approach, whereby audits will be selected based on greatest perceived inherent risk. A timing algorithm will be included to ensure that most effort is focused on inherently high risk areas while, at the same time, not totally ignoring the potential for problems to materialise within the rest of the audit universe.

4.3.2. Whilst internal audit will adopt a risk based approach to determine relative risk, there will remain areas where a purely cyclical approach will still be required, i.e. the audit of key financial systems. Such audits will be undertaken on an annual basis, largely to satisfy the requirements of the external auditors who seek to place reliance on the work of internal audit.

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- 4.3.3. Other review work, based on criteria other than risk, may also be built into the plan. These may include grant certification work, Financial Management Standard in Schools (FMSiS) external assessment or other mandatory audits. They may also include audits or reviews requested by management or the Audit Committee, but will not include the direct delivery of executive responsibilities or functions.
- 4.3.4. A contingency allocation will also be built into the plan for consultancy work, investigations, reactive counter fraud work and other unplanned enquiries. Any commissioned review work must be able to clearly demonstrate contribution to the audit opinion on risk management, control and governance. Any displacement of a previously planned review by unplanned work will be clearly justified.
- 4.3.5. Any organisational demands that cannot be met through contingencies (e.g. as a result of a significant fraud investigation or special assignment), will be supported through the external audit provision or through diversion of effort from planned work and will be funded directly by the sourcing department or service.
- 4.3.6. The annual operational plan will identify the resources required to complete the work, thereby highlighting sufficiency of available resources. The Chief Internal Auditor can propose an increase in audit resource or a reduction in the number of audits if there are insufficient resources. Management and the audit committee will be advised where, for whatever reason, internal audit is unable to provide assurance on any significant risks within the timescale envisaged by the risk assessment process.
- 4.3.7. The annual operational plan will be submitted to the Executive Director of Resources and the Audit Committee for approval. The Chief Internal Auditor will be responsible for delivery of the plan. The plan will be kept under review to ensure it remains responsive to the changing priorities and risks of the Council. Significant matters that jeopardise the delivery of the plan or require changes to the plan will be identified, addressed and reported to the Executive Director of Resources and the Audit Committee.
- 4.4. **Relationship with other assurance providers**
 - 4.4.1. The availability of objective assurance from other assurance providers will be considered in determining audit needs.
 - 4.4.2. A formal Audit Protocol document has been agreed between Internal Audit and the Audit Commission in line with good practice. The purpose of the protocol is to clarify the respective responsibilities between the external auditors and the Council's internal audit function to support an effective working relationship and to facilitate coordination of work. The Chief Internal Auditor will meet regularly with the Audit Commission to consult on audit plans, discuss matters of mutual interest and to seek opportunities for cooperation in the conduct of audit work. The Audit Commission will have the opportunity to rely on the work of internal audit where appropriate.
 - 4.4.3. Where internal audit needs to work with the internal auditors of other organisations, a practice which is expanding with the development of more organisational strategic partnerships, the roles and responsibilities of each party will be clearly defined, agreed and documented.
 - 4.4.4. Internal audit will also seek to establish a dialogue and develop effective working relationships with other review bodies such as the Department of Work and Pensions, HM Inspector of Schools, the Social Work Inspectorate,

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Benefit Fraud Inspectorate, etc., or at least be aware of work being undertaken within the Council by such review bodies. Where appropriate, internal audit will seek to share appropriate information, having regard to rights of access and confidentiality considerations.

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6. DELIVERING THE AUDIT

6.1. Accountability for risk

- 6.1.1. Management and Members define the Council’s “risk appetite” by articulating the level of risk they are prepared to accept in respect of any activity or objective. Internal audit will consider the defined risk appetite in their evaluation of the framework of internal control, risk management and governance and will advise management where they consider that risk is not being controlled within the defined parameters. Management may either accept the advice and implement actions to address weaknesses or deficiencies in controls; or formally reject it.
- 6.1.2. Where internal audit believes that the defined risk appetite falls outside usually accepted parameters or that the rejection of their advice and the absence of satisfactory mitigating action leave the Council exposed to significant risk, they will bring the matter to the attention of the relevant Executive Director. If the Director elects to accept the risk, the Chief Internal Auditor will ensure the Audit Committee is appropriately informed.

6.2. Assignment reporting

- 6.2.1. All formal internal audit assignments will result in a published report. The primary purpose of the audit report is to provide an independent and objective opinion to the Council on the framework of internal control, risk management and governance in operation and to stimulate improvement.
- 6.2.2. Any key (serious) issues arising during the course of the audit review will be promptly reported to the Chief Internal Auditor to determine impact on the scope of the review. Key issues will also be promptly brought to management’s attention during the course of the review to enable appropriate remedial action to be taken prior to being formally published in the audit report.
- 6.2.3. The ‘level’ of opinion provided in the formal report will be based on the following definitions:

Opinion		Framework of governance, risk management and management control
Green	Substantial assurance	A sound framework in place that is operating effectively. Some immaterial evidence of inconsistent application.
Amber	Adequate assurance	Basically a sound framework in place but with repeated evidence of inconsistent application
Amber	Limited assurance	Critical weakness (es) identified within the framework or significant evidence of inconsistent application.
Red	No assurance	Fundamental weaknesses have been identified or the framework is ineffective or absent.

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6.2.4. Action plans will form an integral part of the report and will be used to record:

- those risks considered to be inadequately controlled by the internal control, risk management and governance framework in place at the time of the audit review;
- audit’s observations or findings that led it to its conclusion on the effectiveness of risk management;
- management’s definition of the acceptable level of risk exposure (risk appetite); and
- the actions management propose to bring the risks within acceptable parameters, the officer(s) responsible for those actions and the dates for completion.
- a prioritisation of the actions using the following categories:

Priority Ratings	Current Risk	Action required
High	A significant risk of: failure to achieve objectives; fraud or impropriety; system breakdown; loss; or qualification of the accounts by Audit Commission. Such risk could lead to adverse impact on the Council or expose the Council to criticism	Immediate action required
Medium	A serious, but not immediate risk of: failure to achieve objectives; system breakdown; or loss.	Appropriately timed action required
Low	Areas that individually have no major impact, but where management would benefit from improved risk management and/or have the opportunity to achieve greater efficiency and/or effectiveness.	Action recommended to enhance standards of control

6.2.5. The auditor will draft action plans from significant points arising and arrange to meet with management, to ensure factual accuracy of the audit observations and findings and to ensure a proper understanding of the risks to which any action plan relates. These meetings should take place in accordance with dates agreed in the terms of reference or within two weeks of completion of the audit fieldwork, whichever is the sooner. “Low priority” actions may be reported in the form of memorandum.

6.2.6. The auditor will discuss management’s risk appetite and will advise on the appropriateness of established and planned controls. Management will be required to provide details of actions to be taken to bring the risk within the parameters of the defined risk appetite for inclusion in the audit report. Management will be required to provide a response to the action plans within one week of meeting with the auditor.

6.2.7. Any areas of disagreement between the auditor and management, regarding audit’s observations and/or the auditor’s assessment of current risk exposure, which cannot be resolved by discussion, will be recorded in the action plans.

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- 6.2.8. Within one week of receipt of all action plans, the auditor will draft a clear, concise and constructive executive summary report, following a standard format, outlining:
- the overall level of assurance opinion, based on the auditor's professional judgement of the effectiveness of the framework of internal control, risk management and governance;
 - the auditor's evaluation of the key risks to the achievement of the management objectives, identified at the outset of the review; and
 - a brief narrative summary of assurance in respect of each key risk identified, to include:
 - ◆ areas of good practice identified;
 - ◆ any opportunities for efficiency gains identified including any examples of "over management" of risk; and
 - ◆ a summary of findings/observations, to include an explanation of the risk, its potential impact and the identified control weaknesses.
- 6.2.9. Following review by the lead auditor, the draft report together with completed action plans will be submitted to the Chief Internal Auditor for approval of issue. The auditor will seek to arrange an exit meeting to brief the audit sponsor on the conclusions of the review.
- 6.2.10. The final report will be issued in the names of the auditor conducting the review and the Chief Internal Auditor. Final reports will be copied to:
- the audit sponsor;
 - the audit client;
 - the relevant policy coordinator;
 - the Executive Director of Resources, as proper officer;
 - all 'management action' owners related to the review;
 - the 'final reports' folder; and
 - copies may also be provided to the External Auditor as requested.
- 6.3. **Action tracking**
- 6.3.1. Management is accountable for any actions agreed within the action plans and responsible for ensuring actions are properly implemented within the agreed timescales and that this is reported to internal audit on a timely basis.
- 6.3.2. Internal audit will request progress reports from management, including evidence of actions taken where appropriate, within a timeframe that reflects delivery dates for agreed actions. The auditor will consider management's response and evidence submitted, and exercise judgment as to whether any further action (e.g. a follow up visit) is required by internal audit.
- 6.3.3. Any responses judged to be inadequate will be escalated by the Chief Internal Auditor to the audit sponsor (i.e. relevant Executive Director), the Chief Officers' Management Team (COMT) and finally, the Audit Committee, as deemed appropriate.
- 6.3.4. Actions will be tracked by internal audit to implementation or, as occasionally happens in times of rapid change, to obsolescence. The audit sponsor will be notified through the COMT report (see below) that an audit has been closed.

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6.4. Reports to Chief Officers Management Team and the Audit Committee

6.4.1. A status report on internal audit work will be presented to COMT and the Audit Committee on a quarterly basis (approximately). This report will include a summary of:

- audit opinion and current status of all 'live' internal audit reports, i.e. those where internal audit work is completed and actions are planned to improve the framework of governance, risk management and control;
- executive summaries of all internal audit reports published since the last report where critical weaknesses or unacceptable levels of risk were identified;
- latest positions statements from management in addressing issues raised in reports where critical weaknesses or unacceptable levels of risk were identified, including high priority actions where implementation is overdue;
- a summary of internal audit performance, planning and resourcing issues; and
- an update on progress of the annual audit plan.

6.5. Annual audit opinion

6.5.1. A formal annual report to the Audit Committee, Chief Officers Management Team and Executive Director of Resources (as proper officer), presenting the Chief Internal Auditor's opinion on the overall adequacy and effectiveness of the framework of governance, risk management and control, will be published to enable it to be taken into account within the annual review of the effectiveness of the system of internal audit and in preparing the Corporate Governance Statement.

6.5.2. The format of the Chief Internal Auditor's report will follow that set out by the CIPFA Code and will include:

- an opinion on the overall adequacy and effectiveness of the Council's framework of internal control, risk management and governance;
- disclose any qualifications to that opinion, together with the reasons for qualification;
- present a summary of the audit work from which the opinion is derived, including reliance placed on work by other assurance bodies;
- any issues considered by the Chief Internal Auditor to be particularly relevant to the Corporate Governance Statement;
- a comparison of work undertaken with that planned, with a summary of internal audit performance for the year; and
- comment on compliance with the CIPFA Code and internal audit's quality assurance programme.