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**REPORT TO:** OVERVIEW AND SCRUTINY COMMITTEE

**DATE:** 8 APRIL 2010

**REPORT OF THE:** CORPORATE DIRECTOR (s151)  
PAUL CRESSWELL

**TITLE OF REPORT:** INTERNAL AUDIT - TERMS OF REFERENCE

**WARDS AFFECTED:** ALL

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## **EXECUTIVE SUMMARY**

### **1.0 PURPOSE OF REPORT**

1.1 This is a report to committee to present Terms of Reference for the Audit Partnership in delivering the Internal Audit for Ryedale DC.

### **2.0 RECOMMENDATIONS**

2.1 It is recommended that the Internal Audit Terms of Reference set out in the attached report for 2010/11 be approved.

### **3.0 REASON FOR RECOMMENDATIONS**

3.1 To more clearly define the relationship between the Council and the Partnership. Secondly to resolve one of the outstanding matters from the self-assessment undertaken as part of the Accounts & Audit regulation 6 review (of the Effectiveness of the System of Internal Audit)

### **4.0 SIGNIFICANT RISKS**

4.1 There are no significant risks.

## **REPORT**

### **5.0 BACKGROUND AND INTRODUCTION**

5.1 The Accounts and Audit Regulations 2003 require all Councils to annually review their systems of internal control and to provide an adequate and effective Internal Audit function.

5.2 The last review identified that the Partnership, whilst in a well established and mature relationship with the Council does not have formal Terms of Reference.

5.3 Part of the CIPFA Code of Practice for Internal Audit in Local Government is guidance that the Council should have terms of reference for its internal audit. This report now presents Terms of Reference for the Partnership in its provision of internal audit to the Council.

5.4 The Council's External Auditors will be undertaking their tri-ennial review of the work of the North Yorkshire Audit Partnership during 2009/10. To date they have been able to place reliance on the Partnership's work as part of their audit of the Council's activities. So far they have not made reference to the lack of formal Terms of Reference and have been satisfied that the relationship is working well.

## **6.0 POLICY CONTEXT**

6.1 This report supports the Council's requirement to comply with all legislation. It also supports the Corporate Strategic Objective to know our communities and meet their needs.

## **7.0 CONSULTATION**

7.1 As the report is to the Overview and Scrutiny (Audit) Committee, no consultation other than discussions with the Corporate Director (s151) has taken place. As the NYAP client officer for the Council and as the Chief Financial Officer of the Partnership he is the principal point of contact and thereby has a keen interest in developing the relationship through these Terms of Reference.

## **8.0 REPORT DETAILS**

8.1 The Terms of Reference (ToR) have been drafted and are attached as an appendix to this report.

8.2 They set out a number of areas, including Responsibilities & Objectives; Reporting Lines & Relationships; Independence & Accountability; amongst others.

8.3 These ToR define the working relationship between the Council and NYAP (North Yorkshire Audit Partnership).

8.4 The Internal Audit Strategy is attached as an Appendix.

8.5 The ToR together with the IA strategy have enabled the development of the IA plan for 2010/2011 and through to 2013/2014. The IA plan was reported to the last Overview and Scrutiny Committee.

8.6 The approval of the Terms of Reference for Internal Audit is an important function for the committee and is an outcome that is tangible. Best practice recommends that the ToR are reviewed annually and are presented to the committee for approval each year. As there is a link to the IA strategy and IA plan it is logical that the documents and plan are considered together.

8.7 Therefore it is anticipated that from next year the Terms of Reference, Strategy and Internal Audit Plan will be presented in a single report.

## **9.0 IMPLICATIONS**

9.1 The following implications have been identified:  
a) Financial

There are no financial implications.

- b) Legal  
There are no legal implications.
- c) Other (Equalities, Staffing, Planning, Health & Safety, Environmental, Crime & Disorder)  
None.

**Paul Cresswell**  
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**Background Papers:**

CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006

**Background Papers are available for inspection at:**

Available for inspection from the Head of Partnership and a copy is with the Audit team in Ryedale House.

# North Yorkshire Audit Partnership

## Ryedale District Council ~ Internal Audit

### Terms of Reference

#### 1.0 Responsibilities and Objectives

- 1.1 Internal Audit is an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment comprising risk management, control, and governance by evaluating its effectiveness in achieving the organisations objectives. It objectively examines, evaluates, and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient, and effective use of resources.
- 1.2 The Corporate Director (s151) has responsibility to ensure that there is an effective system of internal control and determines the level of internal audit work undertaken in any year.

#### 2.0 Reporting Lines and Relationships

- 2.1 Internal Audit is provided through the North Yorkshire Audit Partnership (NYAP; or Partnership), a joint service arrangement.
- 2.2 The Head of Partnership is ultimately responsible for Internal Audit at Ryedale DC. There is also an Audit Manager who manages internal audit at Ryedale DC. The Head of Partnership and Audit Manager liaise with the Corporate Director (s151).
- 2.3 The Council has an Overview & Scrutiny (Audit) Committee and the Partnership reports to the Overview & Scrutiny (Audit) Committee on a quarterly and annual basis, through reports from the Corporate Director (s151). The reports include an 'opinion' from the Partnership on the adequacy and effectiveness of risk management and internal control within the authority.
- 2.4 The Overview & Scrutiny (Audit) Committee is responsible for endorsing the Annual Audit Plan. The quarterly and annual reports from the Partnership show progress against the Plan and include a summary of audit work over the period.
- 2.5 The Overview & Scrutiny (Audit) Committee Chairman is able to meet separately and privately with the Partnership, when requested.

#### 3.0 Independence and Accountability

- 3.1 Internal Audit will remain sufficiently independent of the activities that it audits to enable auditors to perform their duties in a manner which facilitates impartial and effective professional judgements and recommendations, are free from any conflicts of interest and do not undertake any non-audit duties. To this end, the Partnership has adopted a **Policy Statement on Auditors' Independence**, which is included as an appendix to these terms of reference.
- 3.2 Internal Audit is involved in the determination of its priorities in consultation with those charged with governance. The Partnership needs to have continual direct access to Council records, officers and reports and the ability to report independently and impartially if required
- 3.3 Accountability for the response to the advice and recommendation of Internal Audit lies with Directors and Heads of Service, who either accept and implement the advice or choose another course of action on a risk assessed basis.

#### **4.0 Statutory Role**

4.1 Internal Audit is a statutory service in the context of the Accounts and Audit Regulations 2003 (as amended in 2006), which state in respect of Internal Audit that:

“A relevant body shall maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control.

Any officer or member of a relevant body shall, if the body requires—

(a) make available such documents of the body which relate to its accounting and other records as appear to that body to be necessary for the purpose of the audit; and

(b) supply the body with such information and explanation as that body considers necessary for that purpose.”

4.2 The statutory role is recognised and endorsed within the Council’s Constitution, which provides the Partnership with authority for access to all staff, records and property of the Council at all times, and right to require such explanations as are considered necessary to satisfy the Partnership of the correctness of any matter under examination. In addition, the Partnership shall have the right of access to any Chief Officer of the Council, members of the Council and to any Committee of the Council.

4.3 This authority is deemed to extend to all joint working arrangements, private funds, records etc that relate to the Council or are held on any of the Council’s premises and upon which employees of the Council work, during their working hours or as part of their duties.

4.4 In addition, the Council’s Constitution contains the following provision, which requires that every formal contract shall contain a clause: “securing the right of the Internal Audit Service to properly discharge its duties generally and as may be prescribed in the Financial Procedure Rules.”

#### **5.0 Consultancy or Advisory Reviews**

5.1 Internal Audit perform consultancy or advisory reviews on an ad hoc basis outside of the annual audit plan, as requested by management. Reports from this type of work contain findings, audit views, and recommendations and inform the overall opinion on the adequacy and effectiveness of internal controls.

#### **6.0 Internal Audit Standards**

6.1 There is a statutory requirement for Internal Audit to work in accordance with the ‘proper audit practices’. These ‘proper audit practices’ are in effect ‘the Standards’ for local authority internal audit. The guidance accompanying the Accounts and Audit Regulations 2003 (as amended in 2006), makes it clear that the Standards are those shown in the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006. The CIPFA Standards have been adopted by Internal Audit.

#### **7.0 Internal Audit Scope**

7.1 The scope for Internal Audit is ‘the control environment comprising risk management, control, and governance’. This means that the scope of Internal Audit includes all of the Council’s operations, resources, services, and responsibilities in relation to other bodies. This description shows the very wide potential scope of Internal Audit work.

- 7.2 In order to turn this generic description into actual subjects for audit, the Partnership uses a Risk Assessment Method, which allows all high-risk subjects to be identified. This risk assessment includes an assessment of the effectiveness of the systems of internal audit, reviewing the adequacy and effectiveness of risk management and reviewing corporate and directorate risk registers. Although this process inevitably identifies the Council's fundamental financial systems as being 'high risk', other non-financial systems and functions are also identified as important areas for review by Internal Audit, for example Information Governance.

## **8.0 Internal Audit Resources**

- 8.1 The Cipfa Code of Practice recommends that Internal Audit must be appropriately staffed in terms of numbers, grades, qualification levels, and experience, having regard to its objectives and to the Standards. Internal Auditors need to be properly trained to fulfil their responsibilities and should maintain their professional competence through an appropriate ongoing development programme.

The Partnership is responsible for appointing its staff and will ensure that appointments are made in order to achieve the appropriate mix of qualifications, experience and audit skills. The Partnership undertakes a continuous review of the development and training needs of its entire staff in order to identify any necessary in-service training covering both internal and external courses, reading, research and on-job training. Staff are encouraged to pursue qualifications relevant to their work.

- 8.2 The Partnership is responsible for ensuring that it provides adequate resources to meet its responsibilities and achieve its objectives. If a situation arises whereby it is concluded that resources are insufficient, this will be formally reported to the Corporate Director (s151) and to the Overview & Scrutiny (Audit) Committee.
- 8.3 Where necessary, to provide an adequate, effective and professional service, the Partnership may request appropriate specialists from other sources to advise in connection with any audit of VFM or study requiring specialist knowledge, or buy in resources from external sources to supplement internal resources.

## **9.0 Fraud and Corruption**

- 9.1 Managing the risk of fraud and corruption is the responsibility of Chief Officers. Audit procedures alone, even when performed with due professional care, cannot guarantee that fraud or corruption will be detected. Internal Audit does not have responsibility for the prevention or detection of fraud and corruption. Internal auditors will, however, be alert in all their work to risks and exposures that could allow fraud or corruption. Internal Audit may be requested by management to assist with fraud related work, and has auditors with appropriate fraud investigatory skills.
- 9.2 The Partnership advises Directors and Heads of Service on fraud and corruption issues.
- 9.3 There are arrangements in place to ensure the Partnership is informed of all suspected or detected fraud, corruption or improprieties so that they can consider the adequacy of the relevant controls, and evaluate the implication of fraud and corruption for the opinion on the internal control environment.

## **10.0 Reporting Accountabilities**

- 10.1 All audit plan assignments will be the subject of formal reports, and include an 'opinion' on the adequacy and effectiveness of risk management and internal controls in the area that has been audited. Such reports will be issued by the Partnership.

- 10.2 Draft reports will be sent to management responsible for the area under review for agreement to the factual accuracy of findings, for consideration of any audit recommendations therein and in order that a plan of action to address any agreed recommendations may be formulated.
- 10.3 After agreement, the reports will be issued to the relevant Head of Service with copies sent to relevant managers and to the Corporate Director (s151). The Overview & Scrutiny (Audit) Committee may request sight of planned audit reports.
- 10.4 All audit reports issued are accompanied by a recommendation proforma, which managers are required to complete and return to Internal Audit, confirming the implementation of recommendations, and providing evidence of their implementation as necessary.
- 10.5 Where a recommendation is not accepted, this will be reported to Overview & Scrutiny (Audit) Committee with an explanation of the reason for not accepting it, for the Committee's consideration.
- 10.6 Any reports containing a recommendation (essential or above) are subject to follow-up at the agreed implementation date, and the results reported to Overview & Scrutiny (Audit) Committee.
- 10.7 Recommendations (useful) are subject to a follow-up audit, normally within six months of its issue (if the recommendation proforma has not been returned), in order to ascertain whether the action stated by the responsible managers in their response to the report has been implemented.
- 10.8 Results of the follow-up of audit recommendations are reported to Corporate Management Team (this proposal to be confirmed).

#### **11.0 Responsibilities**

- 11.1 In meeting its responsibilities, Internal Audit activities will be conducted in accordance with Partnership standards. In addition, internal auditors shall comply with the Code of Ethics and the Code of Practice for Internal Audit in Local Government issued by the Chartered Institute of Public Finance and Accountancy and other such professional bodies of which internal auditors are members.
- 11.2 Co-operation between Internal Audit and the Council's external auditors will be encouraged, and joint working arrangements which respect the different objectives of the two sets of auditors will be established, to maximise the benefit of the combined resource. Internal Audit will co-ordinate with the work of the external auditors for audit planning and assisting the external auditors as required ensuring that appropriate reliance can be placed on Internal Audit's activities.
- 11.3 Internal Audit will work in partnership with other bodies to secure robust internal control that protect the Council's interests.

#### **12.0 Amendments to the Terms of Reference**

These terms of reference will be reviewed annually to ensure their relevance is maintained. Amendments will be subject to the approval of the Overview & Scrutiny (Audit) Committee.



## **North Yorkshire Audit Partnership**

### **Internal Audit Service**

### **Policy Statement ~ Auditors' Independence**

#### **Introduction**

In compliance with the Code of Practice for Internal Audit in Local Government, internal auditors must at all times maintain and be able to demonstrate their independence. They must be fair and must not allow prejudice or bias, conflict of interest or the influence of others to override their judgement and actions.

To do this, auditors need to be objective. Objectivity is exercised when auditors make judgments based upon all the available evidence, not depending on, or influenced by, personal opinions or prejudices, or by inappropriate pressure or influence.

#### **Relationships**

Some relationships may allow the prejudice, bias, or influence of others to threaten that objectivity. It is impossible to define and prescribe all such situations and relationships where these possible pressures exist. Reasonableness should prevail in identifying circumstances and relationships that are likely to, or appear to, impair an auditor's objectivity.

For this reason, when being allocated to an audit assignment auditors should inform their supervisor of situations

- Where a member of the client's staff is their spouse or partner
- Where a member of the client's staff is related to them or to their spouse or partner
- Where a member of the client's staff is a friend or neighbour
- Any other circumstances in which an outside person could prejudice the auditor's independence.

The supervisor, together with the Audit Manager will then determine whether that member of staff should carry out the planned assignment or whether the impairment to their objectivity is such that another auditor should undertake that assignment.

#### **Previous duties**

Objectivity may also be impaired where audit staff have previously worked within the section whose work is being reviewed, or have had authority or responsibility for the section. Therefore, auditors will not be permitted to undertake audit duties until a reasonable period of time has elapsed. A 'reasonable period' of time will normally be taken to be twelve months, or any such period as the Chief Internal Auditor shall decide in any particular circumstances.

#### **Rotation of duties**

In order to ensure objectivity the work assignments of internal auditors should be rotated from time to time where this is possible.



# North Yorkshire Audit Partnership

## Internal Audit Strategy

- 1.1 The objectives of Internal Audit have been set out in the Internal Audit Terms of Reference. Each year Internal Audit undertakes an annual audit risk assessment and planning process culminating in a plan which is then agreed with the Corporate Director (s151) and submitted for the endorsement of the Overview & Scrutiny (Audit) Committee.
- 1.2 The purpose of the audit strategy is to put in place an approach that will enable Internal Audit to be managed in a way, which will facilitate:
- How the service is delivered to the Council to ensure a value for money service.
  - The provision to the Section 151 officer and the Overview & Scrutiny (Audit) Committee of an overall opinion each year on the Council's risk management, control and governance, to support the Annual Governance Statement.
  - Audit of the Council's risk management, control, and governance systems through annual audit plans in a way, which affords suitable priority to the Council's strategic ambitions, values, objectives, and risks.
  - The identification of adequate audit resources with the appropriate skills required for delivering an audit service, which meets required professional standards. This could be achieved by the use of partnership and/or external resources.
  - The relative allocation of resources between assurance, fraud related and consultancy services provided by internal audit.
- 1.3 The current strategy:
- The strategy is risk driven, derived from a risk based audit needs assessment model – the audit 'universe' consists of a mix of budget centres, cross directorate or corporate risk and financial audits, where processes such as payments, payroll and so on are separately identified for audit.
  - The current plan is based on 4 year cycles based on an underlying risk assessment.
  - The inherent risks existing within each area are then identified for audit as part of the audit planning process.
  - The traditional financial systems identified above are audited using a systems based approach with the addition of a high level assessment of any other risks that impinge on the area, including specific work the External Auditors (Deloitte) seek to place reliance on.
  - Separate time is allowed in the audit plan for fraud, consultancy activities, and follow up of audit recommendations.
  - An element of contingency is allowed for unplanned issues such as whistleblowing, which need to be investigated.
  - The plan is prepared on the basis of audit need, and is then compared to existing audit resources to identify whether any shortfalls exist.

#### 1.4 The strategy for 2010-11 and beyond:

- In future, more of the audit plan will become based around the Council's Corporate and Service risk registers rather than the Internal Audit risk based audit needs assessment model, as risk processes mature and the risk registers become more robust. However, Internal Audit will still use its own knowledge to moderate the risk registers in focussing the audit work.
- The annual plan will be increasingly based on a risk assessment based on current risks, their impact and residual risk ratings, which will replace the programmes of cyclical audits.
- Cross-cutting corporate themes such as governance, risk management, performance management, strategic and service planning, project management and partnership working will be included in annual audit plans to an increasing extent.
- Internal Audit supports and contributes to the Council's strategic ambitions. It helps to deliver the Council's Plan by providing value for money in its internal audit.

#### 1.5 Developing the audit plan:

- The Internal Audit plan will be kept under review through regular assessment by the Partnership (the Head of Partnership and the local Audit Manager) and will be discussed with the Corporate Director (s151), and amended as appropriate to reflect changing priorities and emerging risks.
- The Overview & Scrutiny (Audit) Committee will be informed of any significant changes to the plan. The plan will be flexible and contain a level of contingency to reflect the changing priorities and structures of the Council.