

## **Internal Audit Strategy and Annual Plan 2022/23**

### **Report by Chief Internal Auditor**

### **Report for Decision**

#### **1 Recommendations**

The Audit Committee is invited to:

- a) Note the changes to the Internal Audit Strategy outlined in section 4 of this report;
- b) Note the outline of the Internal Audit planning process outlined in section 5 of this report;
- c) Approve the Internal Audit Strategy (Appendix 1); and
- d) Approve the Internal Audit Annual Plan 2022/23 (Appendix 2).

#### **2 Purpose of Report/Executive Summary**

The purpose of this report is to gain approval from the Audit Committee to the proposed Internal Audit Strategy and Annual Plan 2022/23 to enable the Chief Internal Auditor to prepare annual opinions on the adequacy of the overall control environment for Midlothian Council, and Midlothian Health and Social Care Integration Joint Board (MIJB).

The Internal Audit Strategy at Appendix 1 outlines the strategic direction for how Internal Audit will achieve its objectives, which are set out in the Internal Audit Charter, in conformance with PSIAS. It guides the Internal Audit function in delivering high quality internal audit services to Midlothian Council and the MIJB.

The Internal Audit Annual Plan 2022/23 at Appendix 2 has been developed by the shared Chief Internal Auditor and the Principal Internal Auditor. It sets out the proposed range and breadth of audit activity and sufficient work within the audit programme of work to enable the Chief Internal Auditor to prepare the independent and objective audit opinions for Midlothian Council and MIJB. A separate Internal Audit Annual Plan 2022/23 for the MIJB will be presented to its Audit and Risk Committee. Key components of the audit planning process include a clear understanding of each organisation's functions, associated risks, and assurance framework.

**Date 3 March 2022**

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### **3 Background**

- 3.1** The Local Authority Accounts (Scotland) Regulations 2014 that came into force on 10 October 2014 require a local authority to operate a professional and objective internal auditing service. This service must be provided in accordance with recognised standards and practices in relation to internal auditing. Recognised standards and practices are those set out in the *Public Sector Internal Audit Standards: Applying the IIA International Standards to the UK Public Sector* (PSIAS). The standards require internal audit to have suitable operational independence from the organisation.
- 3.2** The Midlothian Council Internal Audit function follows the professional standards as set out in Public Sector Internal Audit Standards (PSIAS) effective 1 April 2013 (updated 2017) which requires the Chief Audit Executive (CAE) to establish risk-based plans to determine the priorities of the Internal Audit activity, consistent with the organisation's goals. The plans also require to be sufficiently flexible to reflect the changing risks and priorities pertaining to each organisation.
- 3.3** A fundamental role of the Council's Internal Audit function is to provide senior management and members with independent and objective assurance, which is designed to add value and improve the organisation's operations. In addition, the CAE is also required to prepare an Internal Audit annual opinion on the adequacy of each organisation's overall control environment.
- 3.4** Internal Audit assurance resources and services are also provided by Midlothian Council's Internal Audit team to the Midlothian Health and Social Care Integration Joint Board (MIJB), including the appointed MIJB Chief Internal Auditor. The Internal Audit Charter and Strategy are applicable to each organisation.

### **4 Internal Audit Strategy**

- 4.1** The key standards within the PSIAS which relate to Managing the Internal Audit Activity are summarised below:

"The chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organisation.

The internal audit activity is effectively managed when:

- The results of the internal audit activity's work achieve the purpose and responsibility included in the internal audit charter;
- The internal audit activity conforms with the Definition of Internal Auditing and the Standards; and
- The individuals who are part of the internal audit activity demonstrate conformance with the Code of Ethics and the Standards.

The internal audit activity adds value to the organisation (and its stakeholders) when it provides objective and relevant assurance, and contributes to the effectiveness and efficiency of governance, risk management and control processes."

**4.2** The Chief Internal Auditor (CAE) and the Principal Internal Auditor have developed the Internal Audit Strategy at Appendix 1. It outlines the strategic direction for how Internal Audit will achieve its objectives, which are set out in the Internal Audit Charter, in conformance with PSIAS. It guides the Internal Audit function in delivering high quality internal audit services to Midlothian Council and Midlothian Health and Social Care Integration Joint Board (MIJB).

**4.3** The Internal Audit Strategy, since its previous approval by the Audit Committee on 9 March 2021, reflects the following:

- The mutual opt out of the shared Internal Audit services with Scottish Borders Council, noted by the Audit Committee on 25 January 2022, and the associated change in approach for the provision of Internal Audit resources;
- The prioritisation of audit activity deferred from the previous year and with greatest risk within the approach to delivery of the Internal Audit Programme of Work; and
- Greater clarity on the PSIAS requirement for an annual Internal Self-Assessment and an External Quality Assessment (EQA), the latter which is scheduled during 2022.

**4.4** The Internal Audit Strategy:

- Outlines the assurance framework, providing clarity of the respective responsibilities of Management for designing and monitoring governance and control systems and of the role of Internal Audit in providing independent assurance thereon;
- States how the key themes which are integral to the assurance gathering process across the organisation's activities will be covered to inform the annual Internal Audit opinion statement;
- Describes the approach to the development of the risk based Internal Audit annual plan;
- Sets out the relative allocation of Internal Audit resources;
- Outlines how the Internal Audit programme of work will be delivered to add value; and
- Describes the monitoring and reporting of the Internal Audit findings from its work and progress with its plans to the relevant organisation's audit committee/board.

## **5 Internal Audit Annual Plan 2022/23**

**5.1** The key standards within the PSIAS which relate to the preparation of the internal audit plan are summarised below:

- Standard 2010 – Planning which states that “the chief audit executive must establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organisation's goals”
- Standard 2020 – Communication and Approval which states that “the chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.”

- 5.2** The CIPFA Publication ‘Audit Committees: Practical Guidance for Local Authorities and Police – 2018 Edition’ states that “The audit committee should seek to make best use of the internal audit resource within the assurance framework. In particular, the audit committee should seek confirmation from internal audit that the audit plan takes into account the requirement to provide an annual internal audit opinion that can be used to inform the Annual Governance Statement. Specific activities will include:
- Approving (but not directing) the risk-based plan, considering the use made of other sources of assurance.”
- 5.3** The CIPFA Publication also states that “The committee will wish to seek assurance from the HIA that appropriate risk assessment has been carried out as part of the preparation of the internal audit plans when they are presented.”
- 5.4** The Chief Internal Auditor (CAE) and the Principal Internal Auditor have developed the Internal Audit Annual Plan 2022/23 at Appendix 2, based on the Internal Audit staff resources set out in 6.1. It sets out the proposed range and breadth of audit activity to be undertaken to provide the independent and objective audit opinions to Midlothian Council and MIJB.
- 5.5** As part of the Internal Audit planning process it was necessary to consider each organisation’s priorities, plans, strategies, objectives, risks and mitigating controls, and the internal and external assurances provided to determine the priorities of the Internal Audit activity consistent with the organisation’s goals, as follows:
- Analysis was undertaken of Internal Audit work during the past 5 years against the Audit Universe which has been significantly revised and realigned by the Principal Internal Auditor to reflect the current strategic and operational management arrangements and approach to service delivery to ensure appropriate coverage;
  - The Strategic Risk Profile was checked to confirm coverage on key strategic risks, as reliance is placed on the risk assessments carried out by the Risk Owners taking account of the risk ratings and mitigations; and
  - Account was taken of known external audit and inspection activities to avoid duplication of assurance work.
- 5.6** It is envisaged that 2022/23 will continue to be a year of change for the Council and other partner organisations. Therefore the Internal Audit Annual Plan 2022/23 should be considered to be flexible and will be periodically reviewed, and amended as required, to reflect any new arrangement or changing risks and priorities or available resources. Any amendments relating to the Council will be brought to the Corporate Management Team and the Audit Committee for approval.
- 5.7** The Non MLC days reflect the Council’s partnership working commitment to provide Internal Audit resource and services to the Midlothian Health and Social Care Integration Joint Board (MIJB). A separate Internal Audit Annual Plan 2022/23 will be presented to MIJB Audit and Risk Committee for approval.

## **6 Report Implications (Resource, Digital, Risk and Equalities)**

### **6.1 Resource**

The Local Authority Accounts (Scotland) Regulations 2014 that came into force on 10 October 2014 require a local authority to operate a professional and objective internal auditing service.

Internal Audit must have sufficient staff and other resources to enable it to carry out the objectives of the Charter and to deliver a programme of independent and objective audit assurance work alongside other available sources of assurance to enable the Chief Audit Executive to prepare annual opinions on the adequacy of the overall control environment for Midlothian Council, and MIJB.

The Internal Audit staff resource totalling 4.72 FTE comprises Chief Internal Auditor (1 FTE), Principal Internal Auditor (0.72 FTE), Internal Auditor (2.0 FTE), and AN Other Internal Audit resource (1 FTE). Each member of the current Internal Audit team has a professional internal audit or accountancy qualification, and has suitable experience, knowledge, skills and competencies (such as the Code of Ethics set out in PSIAS and the Seven Principles of Public Life) needed to deliver the Plan. After deduction for estimated annual leave, public holidays, absence including staff turnover, learning and development, and management and supervision, this equates to a total of 751 days available for Internal Audit activity (2021/22 775 days).

There is budget provision for the staff and other resources set out above within the Revenue Financial Plans which were approved by the Council on 15 February 2022.

The establishment of the new Chief Internal Auditor post has been completed and advertising for recruitment is expected to commence shortly. The establishment of the AN Other Internal Audit resource and recruitment will commence once the former is appointed and in post. With this in mind and the staff resource requirements in the Internal Audit Annual Plan 2022/23, an interim shared services arrangement for the 1<sup>st</sup> quarter 2022/23 (April to June 2022) will be agreed between Management in Midlothian and Scottish Borders Council for the continuation of the shared Chief Internal Auditor and the Interim Senior Auditor at a similar level of audit days to previous quarters in 2021/22.

### **6.2 Digital**

There are no digital implications arising from this report.

### **6.3 Risk**

The Objectives of Internal Audit are set out in its Charter, including “As part of Midlothian Council’s system of corporate governance, Internal Audit’s purpose is to support the Council in its activities designed to achieve its declared objectives and to do so: As a contribution to the Council’s corporate management of risk.”

Key components of the audit planning process include a clear understanding of the Council's functions, associated risks, and potential range and breadth of audit activity for inclusion within the plan. As in previous years, to capture potential areas of risk and uncertainty more fully, reference has been made to the Strategic Risk Profile and key stakeholders have been consulted.

The PSIAS require Internal Audit to evaluate the effectiveness of the Council's Risk Management arrangements and contribute to improvements in the process. The work of Internal Audit (including its opinion on the control environment) shall contribute to the Council's review of its corporate governance arrangements the outcome of which is published in the Annual Governance Statement.

At all times, Management's responsibilities (led by the Corporate Management Team) include:

- Designing and maintaining proper risk management, governance and internal control processes and systems for which they have responsibility to ensure probity in systems and operations, including the prevention, detection and resolution of fraud and irregularities. These are not fixed but evolve as the Council changes.
- Checking that these governance arrangements and internal controls are operating effectively and obtaining assurances from internal compliance, risk, inspection, quality, and control functions. (The above are known as the first and second lines.)
- Engaging with Internal Audit (the third line) in a positive way to achieve shared goals for robust internal control and governance, best value and improvement, and ensuring that Internal Audit can properly fulfil its role.
- Considering and acting upon Internal Audit findings and recommendations, including implementation of audit recommendations within agreed timescales and updating Pentana performance system, or accepting responsibility for any resultant risk from not doing so.
- Seeking advice and consultancy support from Internal Audit on existing controls and on changes to and transformation of governance, processes and procedures.

#### **6.4 Ensuring Equalities**

This report does not relate to a new or revised policy, service or budget change, which affects people (the public or staff), so an Integrated Impact Assessment (IIA) is not an applicable consideration.

The Internal Audit work is carried out in accordance with the appropriate legislation and professional standards. The latter includes compliance by those within the Internal Audit function with the Code of Ethics set out in the PSIAS. This is of particular importance and relevance for the profession of Internal Audit founded as it is on trust placed in its independent and objective assurance about risk management, internal control and governance.

#### **6.5 Additional Report Implications (See Appendix A)**

## **APPENDIX A – Additional Report Implications**

### **A.1 Key Priorities within the Single Midlothian Plan**

Although this report does not relate directly to the key priorities within the Single Midlothian Plan to which Midlothian Council and its Community Planning Partners have made a commitment (Reducing the gap in economic circumstances; Reducing the gap in learning outcomes; Reducing the gap in health outcomes; and Reducing the impact of climate change), good governance is important to enable Midlothian Council to deliver its key priorities in support of achieving the Council's objectives.

### **A.2 Key Drivers for Change**

Key drivers addressed in this report:

- ☒ Holistic Working
- ☒ Hub and Spoke
- ☒ Modern
- ☒ Sustainable
- ☒ Transformational
- ☒ Preventative
- ☒ Asset-based
- ☒ Continuous Improvement
- ☒ One size fits one
- ☐ None of the above

Midlothian Council is committed to creating a great place to grow supported by the 9 drivers for change. Implementing the 9 drivers for change in practice is applicable to the Council's Internal Audit service provision to assist the Council in achieving its objectives.

### **A.3 Key Delivery Streams**

Key delivery streams addressed in this report:

- ☒ One Council Working with you, for you
- ☒ Preventative and Sustainable
- ☒ Efficient and Modern
- ☒ Innovative and Ambitious

### **A.4 Delivering Best Value**

The definition of Internal Auditing within the Public Sector Internal Audit Standards (PSIAS) is "Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes."

Internal Audit is a key element of good governance which is important to enable Midlothian Council to achieve its objectives.

Recommendations made by Internal Audit underpin the Council's own continuous improvement arrangements to enhance its effectiveness, thus supporting the delivery of the Council's best value duties.

#### **A.5 Involving Communities and Other Stakeholders**

The Chief Audit Executive is accountable to the Audit Committee which, in fulfilling its governance role, acts as a bridge between the Council and other stakeholders. The Audit Committee remit includes "To approve the risk-based internal audit plan, including internal audit's resources requirements, the approach to using other sources of assurance and any work required to place reliance upon those other sources".

The Corporate Management Team (CMT) on 2 March 2022 has been consulted on the Internal Audit resources, risk-based audit approach and the resultant planned Internal Audit coverage to ensure it will provide assurance on controls and governance relating to the key risks facing the Council and to assist them in discharging their roles and responsibilities.

#### **A.6 Impact on Performance and Outcomes**

Applying the framework of the PSIAS will give the Audit Committee assurance that the Internal Audit function is compliant with legislative requirements and current best practice.

The delivery of the Internal Audit strategy and annual plan assists the Council in improving its performance and outcomes.

#### **A.7 Adopting a Preventative Approach**

The PSIAS are applicable from 1 April 2013 (amended 2017) which means the Internal Audit Service has taken steps to be fully compliant.

Specific audits within the 2022/23 plan will include assessments on when a preventative approach can be adopted by the Council.

#### **A.8 Supporting Sustainable Development**

This report does not relate directly to supporting sustainable development. Internal Audit is a key element of good governance which is important to enable Midlothian Council to achieve its objectives including sustainable outcomes.