

# Internal Audit Strategy for 2022/23

This document sets out the matters supporting the annual audit plan and the process by which it has been developed for 2022/23.

## 1. Statutory and professional requirements relating to internal audit

- 1.1. Internal audit's function is established by the Accounts and Audit Regulations 2015, which are supported by professional standards for internal audit in the public sector and an advisory note specifically for local government in the United Kingdom. The key requirements of the regulations and of the Public Sector Internal Audit Standards (PSIAS) are set out below.

### Relevant regulations

Internal audit: "A relevant authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance."  
*Regulation 5. (1)*

Review of internal control system: "A relevant authority must, each financial year (a) conduct a review of the effectiveness of the system of internal control [...] and (b) prepare an annual governance statement."

*Regulation 6. (1)*  
*Accounts and Audit Regulations 2015*

### Definition of internal auditing

"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."

"The provision of assurance services is the primary role for internal audit in the UK public sector. This role requires the chief audit executive to provide an annual internal audit opinion based on an objective assessment of the framework of governance, risk management and control."

"Internal auditors must incorporate knowledge of controls gained from consulting engagements into evaluation of the organisation's control processes."

*Public Sector Internal Audit Standards, 2017*  
*published by the Relevant Internal Audit Standard Setters*

- 1.2. The regulations therefore establish the requirement for an internal audit function and its provision of an opinion on the council's governance, risk management and control processes, following public sector internal auditing standards. Professional standards likewise mandate the provision of such an opinion. They also recognise that internal audit involves the provision of both assurance and consultancy services, but assurance is its primary function and any consultancy work must inform the assurance opinion.

## 2. Planning principles

- 2.1. Following the requirement to provide an overall opinion on governance, risk management and control process, a number of principles guide the decisions regarding the work to include in the annual audit plan. These are set out below and address the practical interpretation and application of professional requirements within the county council.

## Internal audit coverage to support an annual overall opinion

- 2.2. An internal audit plan designed to provide the evidence necessary to support an opinion on governance, risk management and control should arguably encompass the following:
- Coverage of the key components of each part of the opinion: aspects of the council's governance, risk management and control.
  - Sufficient coverage of controls across the council's operations as a whole, so that a fair assessment may be made across the organisation.
  - Coverage of the controls that serve to mitigate the council's most significant risks to an acceptable level, and particularly those that operate most widely across the council.
  - Assessment of the actions being taken to develop improved controls in the areas of greatest unmitigated risk.
- 2.3. It is therefore necessary as a minimum to audit aspects of the council's governance and risk management processes, as well as a range of control processes. However, information will also be available from less formal sources than planned audit engagements and this will also inform the overall opinion for the organisation.
- 2.4. The council's governance, risk management and control framework is shown in the diagram below. The internal audit plan is designed to address, proportionately, the coverage required across this controls framework to cover the whole organisation. Where the council achieves its objectives in conjunction with partners, we will also seek assurance over the work of those key partnerships.

A framework for governance, risk management and control						
<b>Governance and democratic oversight</b>						
Corporate governance		Decision-making		Oversight and scrutiny		Policy setting
<b>Business effectiveness</b>						
Risk management	Performance management	Organisational design	Financial governance and planning		Working in partnership	
<b>Service delivery</b>						
Growth, Environment & Transport		Education & Children's Services	Adult Services and Health & Wellbeing		Resources	
<b>Service support</b>						
Legal services	Skills, learning & development	Core ICT systems	Property management	Health & safety	Programme management	Customer access
<b>Business processes</b>						
Financial systems & processes		Procurement		Facilities management	Human resources	
Information management		Contract monitoring & management		Investment	Payroll processing	
Business continuity					ICT systems	

## Relationship to the risk management process

- 2.5. A risk-based audit plan will take into consideration the risks assessed as most significant by the organisation's managers and should seek to provide assurance over the operation of the controls that serve to reduce the most significant risks to the greatest degree.
- 2.6. Working with the council's managers and using risk registers prepared by individual services, we have sought to identify the areas with the greatest inherent risk where these risks are regarded as having been effectively mitigated by strong controls. These are the controls on which the council is placing the greatest reliance and over which it therefore needs the greatest assurance.

- 2.7. The outcome of our audit work is primarily assurance that controls are adequately and effectively designed to mitigate risks to the council's objectives, but also pragmatic action plans intended to mitigate unacceptable degrees of risk. The judgement regarding what degree of risk is acceptable is for the council's managers rather than the Internal Audit Service to make. Where action plans are agreed we will follow them up and assure the Audit, Risk and Governance Committee that action is being taken.
- 2.8. The audit plan is therefore focussed on the key areas of risk to the council, although these may alter during the course of the year. It will be flexible and individual assignments may be added to it or removed from it over time.
- 2.9. The corporate risk register provides a snapshot at any point in time of the matters that present the greatest unmitigated risks to the council. They are therefore matters that the council's senior leadership team will be working most actively to manage but they will not yet be regarded as adequately or effectively controlled. These may be more appropriately subject to advisory input from the Internal Audit Service rather than assurance work.

### **The audit response to significant risks known to be not acceptably mitigated**

- 2.10. The requirement for audit assurance arguably depends on whether or not risks are regarded by management as being mitigated to an acceptable degree. An internal audit function would normally aim, as a minimum, to substantiate assertions by management that an organisation's risks are adequately and effectively controlled but, where a management team is unable to make such an assertion it is highly unlikely that internal audit work would conclude any more positively. Similarly, where risks are recorded on the corporate risk register as being inadequately mitigated they are subject to focussed effort by the organisation's most senior managers and any internal audit assurance work is unlikely to conclude that the service, system or process is as yet subject to adequate or effective control.
- 2.11. Therefore, where management is unable to provide favourable assurance, the Internal Audit Service does not plan to undertake any other assurance work, although this will inform the head of internal audit's overall opinion. Rather than assurance, the Internal Audit Service may provide advisory support to the organisation and its managers in these cases, as set out in paragraph 3.4 below.
- 2.12. Since the drive for improvement is constant and change continues across the organisation, the plan will need to be flexible and is likely to be amended during the year.

### **The council's 'lines of defence' and other sources of assurance**

- 2.13. The Internal Audit Service is only the council's third line of defence in a model that represents management as the first line, responsible for directly assessing, controlling and mitigating risks; and any in-service compliance activity that confirms these controls as the second. For example, the social care services impose independent compliance checks on front-line staff and their managers to ensure that social work is adequately supervised, and its quality regularly checked. Where such 'second line' compliance functions are available, we focus our audit work on assessing the control exerted by them rather than on repeating their work.
- 2.14. Other sources of assurance may be available from external organisations, for example the external auditor or Ofsted. We actively seek to understand what other sources are available and will take it into account if it is relevant to the overall opinion on governance, risk management and control. We will ensure as far as possible that the committee is made aware of such assurance.

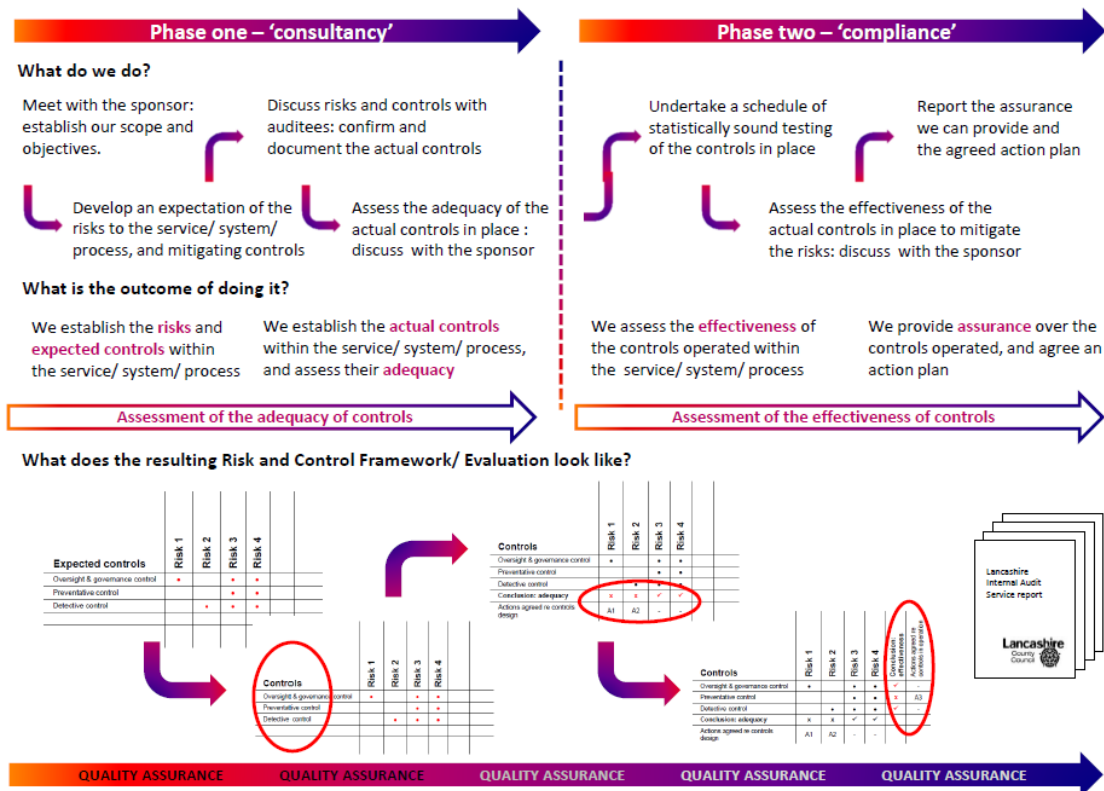
## Internal audit sponsorship and auditors' engagement with management

- 2.15. We need to direct our audits to senior individuals who are able to sponsor the work and take responsibility for any remedial action required to mitigate any unacceptable risks: these will normally be the council's directors. We therefore need to work with the council's directors, but also the heads of service and key managers, to scope our work and agree its outcomes.
- 2.16. Some business processes are the responsibility of more than one service area and, where processes span more than one service, we may plan a short series of individual but connected audits. These may in turn require sponsorship at a more senior level within the organisation and we will consult the Corporate Management Team on the best way to approach such work.
- 2.17. The Internal Audit Service has no specific in-house expertise in the specialist area of technical ICT audit work but has appointed an external provider to undertake a programme of specialist ICT audit work for the council.

### 3. The audit approach adopted by the county council's Internal Audit Service

- 3.1. The Internal Audit Service follows a risk-based audit methodology, working closely with the council's managers to understand the risks to services, systems and processes and then testing the controls in place that mitigate these risks. The audit process therefore involves two phases: establishing a framework of risks and controls, and then testing those controls. During the first phase we work closely with the service's managers to document a risk and control framework for a service, system or process which enables us to assess the adequacy of the controls designed to mitigate the risks identified. During the second phase we test the effectiveness of the controls in operation. This approach is show diagrammatically below.

#### A risk-based audit methodology in two phases



- 3.2. The way this approach is applied to any audit varies depending on what assurance can firstly be given by the council's managers that risks are adequately and effectively mitigated.

### **Full audit including both phases of work: risk and control evaluation**

- 3.3. Where assurance is required over a control system that has not previously been audited in its present form, for example because it is new or has been recently changed, but its managers believe that the risks are adequately and effectively controlled, we undertake a full review including both audit phases. We will provide an opinion on the basis of this work.

### **Work on phase one only: consultancy**

- 3.4. Where the managers of a service, system or process are aware that there are matters to address and are unwilling to assert that risks are adequately and effectively controlled, they may seek support to design and implement appropriate controls. The first phase of any audit may be regarded as advisory work or consultancy as we work with a service's managers to consider the controls, they operate to manage the risks to their service's objectives. This analysis can be undertaken at any time, particularly whilst a service is in the process of transformation and can assist managers to design effective procedures. We can use this approach to add value to the organisation without providing any further assurance but, although it would need to be checked and revised, this work may serve as the first phase of a full audit at a later date, perhaps in the following year.

### **Work on phase two only: compliance**

- 3.5. The second phase of an audit is intended to provide assurance that control systems that have already been assessed as being adequately designed are also operating effectively. This may follow immediately after the first phase as part of a full audit, or where the service, system or process has been audited before but is of such significance to the council that further assurance is required that it continues to operate effectively, we will undertake repeated compliance testing of key controls.

### **Follow-up work**

- 3.6. Where managers can confirm that action has been taken as agreed during a previous audit to mitigate any high or medium risks identified we will seek evidence to support this, but we will not generally follow up actions designed to mitigate only low risks.

### **Degrees of assurance**

- 3.7. The assurance we will provide falls into four categories: substantial, moderate, limited and none.
- Substantial assurance: the framework of control is adequately designed and/ or effectively operated overall.
  - Moderate assurance: the framework of control is adequately designed and/ or effectively operated overall, but some action is required to enhance aspects of it and/ or ensure that it is effectively operated throughout the service, system or process.
  - Limited assurance: there are some significant weaknesses in the design and/ or operation of the framework of control that put the achievement of the service, system or process' objectives at risk.
  - No assurance: there are some fundamental weaknesses in the design and/ or operation of the framework of control that could result in failure to achieve the service, system or process' objectives.

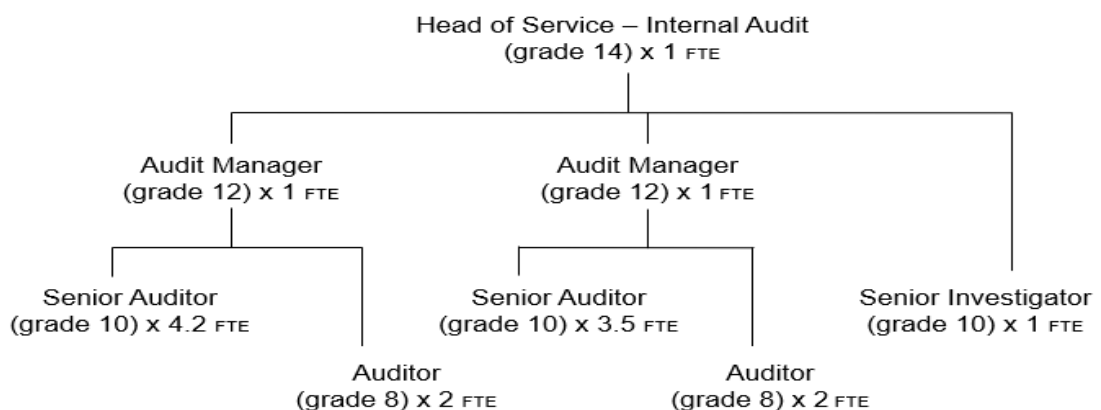
#### 4. Inputs to the planning process

- 4.1. Members of the Internal Audit Service have consulted members of the Corporate Management Team, Directors and Heads of Service to ensure a reasonable understanding of the risks to the council's services and the areas that will be most appropriately subject to detailed audit work.
- 4.2. The Internal Audit Service has access on request to the papers of the council's various management teams, including service risk registers. The Cabinet regularly considers financial reports from the director of finance which set out the expenditure in each of the council's services, and these provide an indication of the scale of the services as well as the council's financial position. Information from the team that monitors the council's staff resources likewise provides an indication of the scale of the council's services in terms of the numbers of staff employed, identifying the services that are inherently the most significant to the council in terms of their budgets and numbers of staff.
- 4.3. We have previously given full assurance over the design and operation of the council's risk management process. We have reviewed the risk registers for each of the council's services, as well as the corporate register and this has supported discussions with directors and managers. These have identified the risks that individual services assess as most significant and the controls that mitigate these.

#### Audit resources

- 4.4. Resource requirements are reviewed each year as part of the audit planning process. The current establishment for the audit team enables sufficient resource to deliver the risk-based plan. The service employs 17 staff in the structure which equates to 15.7 full-time equivalent (FTE) as set out below:

#### Lancashire County Council: Internal Audit Service



- 4.5. The Internal Audit Service also provides an out-sourced internal audit function to the Office of the Police and Crime Commissioner and Lancashire Constabulary, Lancashire Fire and Rescue Service and Rossendale Borough Council, as well as some additional support to some of the other district councils. This work accounts for approximately 2.4 full-time equivalent staff although it is undertaken by individuals across the service.