

# Review of --- Internal Audit

Metropolitan Police Authority

Audit 2008/09

August 2009



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## Status of our reports

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors/ members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
  - any third party.
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# Introduction and background

- 1 The Metropolitan Police Authority (the Authority) is responsible for the implementation of proper systems of internal control and governance. Key to these systems should be an effective internal audit function that objectively examines and evaluates the adequacy of internal control within the Authority and within the Metropolitan Police Service (MPS). The importance of an internal audit function has been further emphasised by the requirement for an annual governance statement to be included in the Authority's financial statements.
- 2 The annual governance statement needs to be supported by assurance that appropriate controls are in place and operating effectively. One of the key mechanisms by which the Chief Officer's annual review of effectiveness is informed is the Director of Internal Audit's Annual Report, which for 2008/09 will be received by the MPA's Corporate Governance Committee at its June 2009 meeting.
- 3 As external auditors, at least every three years we are required to carry out a full review of Internal Audit's compliance with CIPFA standards as set out in CIPFA's 2006 Code of Practice for Internal Audit in Local Government (the CIPFA Code). We are also required to review the work of Internal Audit where we seek to place reliance on its review of key financial systems for our final accounts work. Our last triennial review was carried out in 2005/06, so a review is due in 2008/09.
- 4 The Authority's Internal Audit function is provided by an in-house directorate of 35 staff. Internal Audit's remit is to audit the internal control and risk management arrangements in place within the MPA and MPS. Its work comprises systems audits, reviews at local command unit level, controls advice for new and developing systems, forensic audits to investigate potential fraud and, from 2008/09 a fraud prevention and advice service.
- 5 This report is addressed to the MPA and summarises the findings of the review we carried out in March and April 2009. This review has focused principally on the processes Internal Audit had in place for the year to 31 March 2009. It also considers the findings from our review of a sample of Internal Audit files selected from the 2008/09 Internal Audit plan

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# Audit approach

- 6 Our work has been tailored to meet the requirements of the International Standards on Auditing (UK and Ireland) and the Code of Audit Practice. ISA (UK & I) 610 requires external audit to carry out an overall assessment of Internal Audit. Where external auditors seek to place reliance on the work of Internal Audit, ISA (UK & I) 610 requires them to gain assurance over the quality and scope of that work, the reporting arrangements in place, and, the governance and effectiveness of the internal audit function.
- 7 To meet the requirements of ISA (UK & I) 610, our review involved:
  - carrying out a high-level assessment of Internal Audit's arrangements against the requirements of the CIPFA Code; and
  - reviewing a sample of completed Internal Audit files to assess the extent to which these arrangements are securing quality in audit work performed.
- 8 We used this review to update our assessment of risk at the Authority, the level of reliance that we choose to place on Internal Audit and the level and nature of procedures we perform on specific pieces of Internal Audit work on which we seek to place reliance in the future.
- 9 The CIPFA Code sets out standards of professional practise and defines how an internal audit service should undertake its functions. The Code is formed of 11 standards and our detailed report considers each in turn:
  - Scope of Internal Audit;
  - Independence;
  - Ethics for Internal Auditors;
  - the Audit Committee, the function fulfilled by the Corporate Governance Committee at the MPA;
  - Relationships;
  - Staffing, Training and Continuous Professional Development;
  - Audit Strategy and Planning;
  - Undertaking Audit Work;
  - Due Professional Care;
  - Reporting; and
  - Performance, Quality and Effectiveness.
- 10 As part of our review we interviewed Internal Audit staff and reviewed Internal Audit plans, a sample of its reports and detailed working papers.

# Main conclusions

- 11 We reviewed the Authority's Internal Audit service against each of the standards in the CIPFA Code of Practice and found that Internal Audit were compliant with each. We have reviewed three Internal Audit files so far this year and found the work to be of a good quality, with only minor areas for improvement noted.
- 12 On the basis of this assessment, we have concluded that the Internal Audit service is effective, and that we are able to place reliance on Internal Audit's work in 2008/09. Our findings indicate that improvements have been made since our last full review in 2005/06, when we noted scope for improvement in the quality of recording and evidencing of Internal Audit work.
- 13 Particular areas of strength identified by our review include:
  - a comprehensive annual plan based on a robust risk assessment and needs analysis covering all significant areas of the MPA's and MPS's risk management and internal control framework on a cyclical basis;
  - a high level of satisfaction in the quality and ethical standards of the service evident from post-audit questionnaires completed by the manager being audited;
  - good arrangements for training and development, including regular performance appraisals, a training and qualifications database, and the provision of anti-fraud training to all Internal Audit staff; and
  - the fostering of wider links with other internal auditors and regulators to help spread good practice and share knowledge.
- 14 We have identified some areas for improvement, particularly in relation to how auditor independence is formally documented and monitored, as the current arrangements meet the minimum requirements of the Code only. Whilst Internal Audit is appropriately independent of management in practice, we recommend that all audit staff complete a declaration of interest form periodically. There is also scope to improve arrangements where audit staff provide advice on the development of systems, policies and procedures and then carry out subsequent audits of these areas.
- 15 Our detailed findings are set out below, with our recommendations and the related action plan included at Appendix 1.

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# Detailed report

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## Scope of Internal Audit

- 16 The terms of reference of Internal Audit are contained within the Authority's Financial Regulations. The Financial Regulations form part of the Standing Orders, which were approved by the Full Authority most recently on 27 November 2008. The Financial Regulations broadly meet the requirements of the CIPFA Code although there are some omissions relating to:
- the establishment of the independence of Internal Audit;
  - the requirement of the Head of Audit to deliver an annual opinion;
  - the role of Internal Audit in any fraud-related or consultancy work; and
  - details of how Internal Audit's resource requirements will be met.
- 17 We recognise that the majority of these aspects are appropriately reflected in the Internal Audit Strategy 2008-2011, which has been approved by Corporate Governance Committee, and in information on the Authority's website. There is however, scope to clarify how the organisational independence of Internal Audit is maintained in the terms of reference themselves.

### Recommendation

- R1** The terms of reference should formally set out the arrangements for ensuring the independence of Internal Audit.

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## Independence

- 18 The Internal Audit function is provided by a separate directorate within the Authority, and is free from executive responsibilities which helps to maintain its independence from the rest of the Authority and the MPS. As stipulated in the Financial Regulations, the Director of Internal Audit reports directly to the MPA Chief Executive and has direct access to the MPS Commissioner. The Director of Internal Audit has the freedom to report formally to Members through the Corporate Governance Committee.

## Detailed report

- 19 The CIPFA Code requires that declarations of interest are made by Internal Audit staff in line with the Authority's requirements, which, at the MPA, only require declarations from MPA Members, MPA Senior Management Team and MPS Management Board and their direct reports. The Director of Internal Audit completes an annual declaration of interest return, and in doing so we recognise that Internal Audit is complying with the organisation's requirements and thus the CIPFA Code. However, given that Internal Audit needs to be seen to be independent of executive responsibilities, and given the size of the audit team at the MPA, we recommend that declarations of interest are obtained from all audit staff periodically to allow Internal Audit management to monitor its independence and to comply with good practice.
- 20 Internal Audit's 2008/09 Annual Audit Plan includes 690 days for advisory work, for example providing controls advice for new and developing systems. Auditors involved in advisory work are not in all cases precluded from carrying out audits of the system they have advised on, particularly where a senior auditor has developed an expertise in an area. Internal Audit management recognise that auditors often have specialist expertise that can add value to the MPA/S in an advisory capacity. Management have taken some steps to put in place safeguards to ensure auditors' independence is not compromised as a result, but these could be better formalised.
- 21 The CIPFA Code states that audit advice and recommendations, including where Internal Audit has been consulted about significant changes to the internal control systems, should be given without prejudice to the right of Internal Audit to review and make further recommendations at a later date.
- 22 Currently, all systems development and subsequent systems audit work is overseen by an Assistant Director or the Deputy Director of Internal Audit. We recommend that Internal Audit document in writing how it has considered risks to its independence, and the actions taken to mitigate those risks, for each instance where Internal Audit staff have advised on a system, policy or procedure's development and are involved in subsequent audit work.

### Recommendations

- R2 Declarations of interest should be obtained from all Internal Audit staff on a regular basis, and this information should be taken into account as part of the audit planning process.
- R3 Internal Audit should document how it has considered risks to independence, and the actions taken to mitigate those risks, for each instance where Internal Audit staff have advised on a system, policy or procedure's development and are involved in subsequent audits of these areas.

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## Ethics for Internal Auditors

- 23** The Internal Audit Directorate Audit Manual provides guidance to all audit staff on standards of conduct and refers to corporate policies on ethical conduct. The Audit Manual stipulates that staff must not audit areas where they have had operational responsibilities within the previous two years. Post-audit questionnaires are sent requesting feedback on staff conduct during the audit. The feedback obtained in 2008/09 show a strong performance in this area. On average, where questionnaires were completed, Internal Audit was awarded a score of 4.69 for ethical conduct, on a scale of 1-5 where 5 represents the highest satisfaction rating.
- 24** The Audit Manual provides detailed guidance on scoping each audit and the risk-based planning process. Terms of reference are prepared for each audit assignment and a team briefing is held at the start of each audit to discuss the audit objectives, and audit risks. Internal Audit also receive updates on new legislation, regulations and the organisation's latest decisions through directorate meetings, Chief Executive briefings and MPA Committee meetings.

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## Corporate Governance Committee

- 25** The Authority's Corporate Governance Committee has an independent role overseeing the arrangements for Internal Audit. Its terms of reference cover all the expected functions of an audit committee as set out by CIPFA. It approves the Internal Audit strategy and annual plans and considers progress reports from the Director of Internal Audit at each committee meeting. The Director of Internal Audit presents an annual report to the committee, to provide Members with Internal Audit's assessment of the robustness of the MPA/S's internal control environment and to allow Members to challenge the executive. Both External Audit and Internal Audit attend the committee meetings. The Director of Internal Audit meets with the Chair of the committee on a monthly basis and leads the agenda setting and work planning meetings for the Committee.

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## Relationships

- 26** Internal Audit maintains appropriate working relationships with all key MPA officers and Members and the Director of Internal Audit meets regularly with the MPS Director of Resources and with other Management Board members as required, which helps inform the programme of work for the year. Internal Audit seeks feedback from staff through the use of post-audit questionnaires. Completed questionnaires from 2008/09 show a high level of customer satisfaction with the performance of Internal Audit. For example, Internal Audit were awarded an average score of 4.10 for satisfaction with the level of customer consultation throughout the audit process, and 4.54 for the value to the customer of the audit recommendations (on a scale of 1 to 5 where 5 represents highest satisfaction). Internal Audit's performance is reported annually to the Corporate Governance Committee by the Director of Internal Audit.



## Detailed report

- 27 Relationships with external audit are good. We have monthly meetings with the Director and Deputy Director of Internal Audit to discuss our respective work programmes and emerging findings. We co-ordinate our audit risk assessments and planning activities and we are working with Internal Audit to finalise a protocol setting out how we will work together to ensure optimum audit coverage and effective co-ordination of audit activity.
- 28 Internal Audit has fostered strong links with other internal auditors and regulators, for example through the GLA Head of Internal Audit Group and the Police Audit Group for police authority internal auditors. Internal Audit has maintained working relationships with Her Majesty's Inspectorate of Constabulary (HMIC) and the Home Office. However, we found that the Memorandum of Understanding between Internal Audit and the Home Office has not been updated for several years.

### Recommendation

- R4** Review and update the Memorandum of Understanding between MPA Internal Audit and the Home Office.

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## Staffing, Training and Continuous Professional Development

- 29 The Director of Internal Audit is professionally qualified and has over 30 years' experience of Internal Audit and management. There are satisfactory arrangements for ensuring all audit staff have appropriate qualifications and mix of skills. The directorate has a dedicated Forensic Unit which includes a number of accredited counter fraud specialists. All staff receive annual and interim performance appraisals in which development needs are reviewed. All staff also receive anti-fraud training. A training and qualifications database is maintained within the directorate and is reviewed at monthly SMT meetings.
- 30 Job descriptions for all staff are published in the Audit Manual. We understand the job description for the Director of Internal Audit is currently being updated. As a result, it was not available at the date of our review.

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## Audit Strategy and Planning

- 31 The Internal Audit Strategy 2008-2011 is a comprehensive document setting out the responsibilities and objectives of Internal Audit, its strategic priorities for the 3-year period, and expected outcomes. The strategy makes clear links to the Authority's corporate strategic priorities. It was approved by the Corporate Governance Committee on 14 March 2008.

32 The annual audit plan is underpinned by a robust risk assessment, the Audit Needs Assessment, which covers all key systems within the MPA and MPS and prioritises audits using a detailed risk-based scoring matrix. The annual plan estimates the resources needed and where there is an imbalance between the planned work and the resources available, this is reported to the Corporate Governance Committee for consideration. Additional Internal Audit resources have in the past been funded following these discussions. The annual plan is approved by the Corporate Governance Committee before the start of each financial year.

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### Undertaking Audit Work

- 33 In general, Internal Audit has good quality assurance arrangements in place to ensure work is of a good standard.
- 34 To inform our judgement in this area we reviewed a sample of four Internal Audit files completed as part of the 2008/09 Internal Audit plan:
- Accounts receivable;
  - Accounts payable;
  - Payroll; and
  - Budgetary control.
- 35 The purpose of our review was to assess the quality of the work performed and whether we are able to place reliance on the work to reduce our own testing of controls as part of our opinion audit work. In particular our review considered whether:
- audit tests has been designed appropriately to address identified risks;
  - sample sizes appear appropriate and the sampling methodology robust;
  - audit work was clearly recorded and supported by evidence to allow us to re-perform tests of control; and
  - there was evidence of review of the work by an appropriate senior auditor.
- 36 We found that Internal Audit's work was generally well presented allowing us to re-perform audit tests as necessary. In particular, in the follow-up systems audits it was very easy to identify which key controls were tested. In all audit files there was evidence of review by senior staff, but in one audit file it was unclear whether the review had covered all areas of the audit as some working papers were not signed off by the reviewer.
- 37 For accounts receivable, accounts payable and budgetary control, we have concluded that we are able to place reliance on the work of Internal Audit for our 2008/09 opinion audit. Our review of Internal Audit's work on payroll is not yet complete; we aim to complete our review in June 2009.

### Recommendation

**R5** All working papers should be signed off by the reviewer, to evidence robust quality assurance arrangements are in place.

### Due professional care

- 38 As reported above, the Internal Audit Strategy 2008-2011, Audit Manual and the Authority's policies set out the requirements on audit staff to behave in a fair and objective manner. This appears to be applied in practice and we have no matters to report other than that covered above relating to declarations of interest.
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### Reporting, performance, quality and effectiveness

- 39 The Audit Manual sets out the reporting standards for Internal Audit reports. We receive final Internal Audit reports and our review of these indicates they meet the requirements of the CIPFA Code. Each report sets out the scope of the audit, includes an audit opinion, and includes an action plan prioritising recommendations according to risk. Implementation of all recommendations is considered annually by the Corporate Governance Committee via the Director of Internal Audit's annual report. This report also supports the Authority's Annual Governance Statement. The MPS Inspection Liaison and Analysis Unit (ILAU) also monitors implementation of audit recommendations and receives periodic updates from internal and external audit and HMIC at its External Audit and Inspection Partnership meetings.
- 40 Internal Audit performance against targets is reported on a monthly basis within the directorate, and at MPA Business Management team meetings, and on a quarterly basis to MPA Senior Management Team. Performance is reported to Corporate Governance Committee on an annual basis. By April 2009, 91 per cent of the systems audit programme for 2008/09 had been completed to report stage, exceeding the 90 per cent target, and 89 per cent of the B/OCU programme had been completed, just below the 90 per cent target.
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### Next steps

- 41 We recommend Internal Audit review our action plan at Appendix 1 and take steps to address the points raised. We would like to thank MPA Internal Audit for the information they have provided us with to allow us to complete this year's review, and for their cooperation during the review. We look forward to continuing to work with them in 2009/10.

# Appendix 1 – Action plan

Page no.	Recommendation	Priority	Responsibility	Agreed	Comments	Date
6	R1 The terms of reference should formally set out the arrangements for ensuring the independence of Internal Audit.	Medium	Director of Internal Audit	Yes	The amendments will be included in the next revision of the Authority's Financial Regulations.	August 2009
7	R2 Declarations of interest should be obtained from all Internal Audit staff on a regular basis, and this information should be taken into account as part of the audit planning process.	High	Director of Internal Audit	Yes		September 2009
7	R3 Internal Audit should document how it has considered risks to independence, and the actions taken to mitigate those risks, for each instance where Internal Audit staff have advised on a system, policy or procedure's development and are involved in subsequent audits of these areas.	Medium	Deputy Director Internal Audit/Assistant Directors of Internal Audit	Yes	This will be implemented with immediate effect.	June 2009
9	R4 Review and update the Memorandum of Understanding between MPA Internal Audit and the Home Office.	Low	Director of Internal Audit	Yes		September 2009
10	R5 All working papers should be signed off by the reviewer, to evidence robust quality assurance arrangements are in place.	Low	Assistant Directors of Internal Audit	Yes	This will be implemented with immediate effect.	June 2009

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