

## Draft Strategy for Internal Audit 2013/14 – 2015/16

Including the Periodic Audit Plan for  
2013/14



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## A Quick guide to the Audit Planning process

### Step 1- Audit Universe/Auditable Areas

Identify the Audit Universe (i.e. a list of areas that may require auditing) using a variety of methods:

- Areas of risk identified by the Fire Authority as having the potential to impact upon its ability to deliver its objectives.
- Mandatory areas, such as the Key Financial Systems work we do on behalf of the external auditors etc.
- Areas where we use auditors knowledge, management request and past experience etc.



### Step 2 – Ranking

Score each auditable area as high, medium or low risk using the CIPFA scoring methodology: Materiality/Business Impact/Audit Experience/Risk/ Potential for Fraud



### Step 3 – Three Year Strategy

List the medium and high risk auditable areas in the three year Strategy for Internal Audit. High risk areas will be audited annually, medium risks once in a three year cycle, while a watching brief will remain on the low risks.

Appendix A



### Step 4 - Next Years Plan

List the areas that will be subject to an audit review in 2013/14 in the Periodic Audit Plan.

Appendix B

## A Glossary of Terms

### Governance

The arrangements in place to ensure that the Authority fulfils its overall purpose, achieves its intended outcomes for citizens and service users and operates in an economical, effective, efficient and ethical manner.

### Control environment

Comprises the systems of governance, risk management and internal control. The key elements include:

- establishing and monitoring the achievement of the Authority's objectives
- the facilitation of policy and decision-making ensuring compliance with established policies, procedures, laws and regulations – including how risk management is embedded
- ensuring the economical, effective and efficient use of resources and for securing continuous improvement
- the financial management of the Authority and the reporting of financial management
- the performance management of the Authority and the reporting of performance management.

### System of internal control

The totality of the way an organisation designs, implements, tests and modifies controls in specific systems, to provide assurance at the corporate level that the organisation is operating efficiently and effectively.

### Risk management

A logical and systematic method of establishing the context, identifying, analysing, evaluating, treating, monitoring and communicating the risks associated with any activity, function or process in a way that will enable the organisation to minimise losses and maximise opportunities.

### Risk based audit

An audit that:

- identifies and records the objectives, risks and controls
- establishes the extent to which the objectives of the system are consistent with higher-level corporate objectives
- evaluates the controls in principle to decide whether or not they are appropriate and can be reasonably relied upon to achieve their purpose, addressing the organisation's risks
- identifies any instances of over and under control and provides management with a clear articulation of residual risks where existing controls are inadequate
- determines an appropriate strategy to test the effectiveness of controls i.e. through compliance and/or substantive testing
- arrives at conclusions and produces a report, leading to management actions as necessary and providing an opinion on the effectiveness of the control environment.

### Audit Committee

The governance group charged with independent assurance of the adequacy of the internal control environment and the integrity of financial reporting.

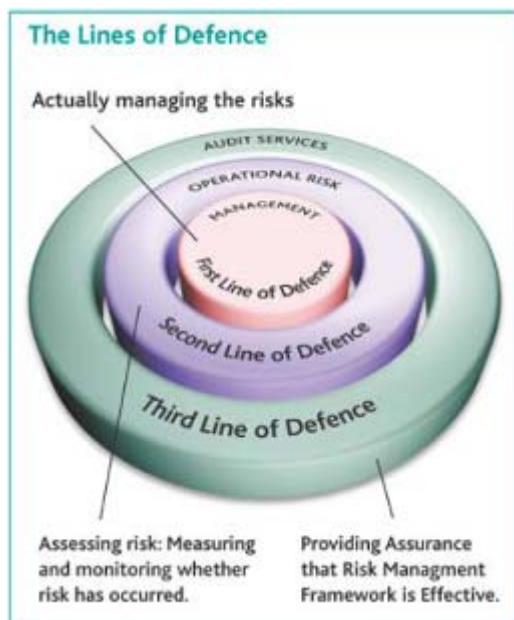
## Internal audit

An assurance function that provides an independent and objective opinion to the Authority on the control environment, by evaluating its effectiveness in achieving the Authority's 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.

## Assurance

A confident assertion, based on sufficient, relevant and reliable evidence, that something is satisfactory, with the aim of giving comfort to the recipient. The basis of the assurance will be set out and it may be qualified if full comfort cannot be given. The Head of Audit may be unable to give an assurance if arrangements are unsatisfactory. Assurance can come from a variety of sources and internal audit can be seen as the 'third line of defence' with the first line being the Authority's policies, processes and controls and the second being managers' own checks of this first line.

## The Three Lines of Defence



### The first line of defence

The day to day business operations and controls.

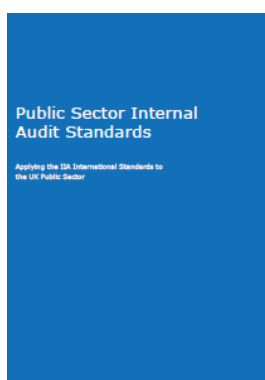
### The second line of defence

Management supervision and oversight.

### The third line of defence

Independent challenge and assurance (including Internal Audit).

## Internal Audit standards



The Internal Audit team comply with the standards as laid out in the new Public Sector Internal Audit Standards that come into effect on 1 April 2013.

## 1 Introduction

The purpose of internal audit is to provide the West Midlands Fire & Rescue Authority with an independent and objective opinion on risk management, control and governance and their effectiveness in achieving the Authority's agreed objectives. In order to provide this opinion, we are required to review annually the risk management and governance processes within the Authority. We also need to review on a cyclical basis, the operation of internal control systems within the Authority. Internal audit is not a substitute for effective internal control. The proper role of internal audit is to contribute to internal control by examining, evaluating and reporting to management on its adequacy and effectiveness.

The purpose of this document is to provide the Authority with a Strategy for Internal Audit, based upon an assessment of the Authority's audit needs. The Assessment of Assurance Need exercise is undertaken to identify the systems of control and determine the frequency of audit coverage. The Assessment will be used to direct internal audit resources to those aspects of the Authority which are assessed as generating the greatest risk to the achievement of its objectives.

## 2 Assessing the effectiveness of Risk Management and Governance

The effectiveness of risk management and governance will be reviewed annually, to gather evidence to support our opinion to the Authority. This opinion is reflected in the general level of assurance given in our Annual Report and within separate reports covering risk management and governance. This review will cover the elements of the risk analysis which we regard as essential for annual review in order to provide a positive, reasonable assurance to the Authority.

## 3 Assessing the effectiveness of the system of control

In order to be adequate and effective, management should:

•	Establish and monitor the achievement of the Authority's objectives and facilitate policy and decision making
•	Identify, assess and manage the risks to achieving the Authority's objectives.
•	Ensure the economical, effective and efficient use of resources.
•	Ensure compliance with established policies, procedures, laws and regulations.
•	Safeguard the Authority's assets and interests from losses of all kinds, including those arising from fraud, irregularity or corruption.
•	Ensure the integrity and reliability of information, accounts and data.

These objectives are achieved by the implementation of effective management processes and through the operation a sound system of internal control. The annual reviews of risk management and governance will cover the control environment and risk assessment elements, at a high level. The programme of work developed as the outcome of the exercise will cover the system level control activities.

The Internal Audit Strategy contained within this report is our assessment of the audit work required in order to measure, evaluate and report on the effectiveness of risk management, governance and internal control.

#### 4 Assessment of assurance need methodology

Internal audit should encompass the whole internal control system and not be limited only to financial control systems, the scope of internal audit work should reflect the core objectives of the Authority and the key risks that it faces. As such, each audit cycle starts with a comprehensive analysis of the whole system of internal control that ensures the achievements of the Authority's objectives.

Activities that contribute significantly to the Authority's internal control system, and also to the risks it faces, may not have an intrinsic financial value necessarily. Therefore, our approach seeks not to try and measure the level of risk in activities but to assign a relative risk value. The purpose of this approach is to enable the delivery of assurance to the Authority over the reliability of its system of control in an effective and efficient manner.

We have undertaken the assessment using the following process:

- We identified the core objectives of the Authority and, where available, the specific key risks associated with the achievement of those objectives.
- We then identified the auditable areas that impact significantly on the achievement of the control objectives.
- We assigned risk values to the auditable areas, based on the evidence we obtained.

The Internal Audit Strategy is drawn out of the assessment of audit need. The proposed plan covering the period 2013/14 to 2015/16 is detailed at Appendix A.

#### 5 The assessment of internal audit assurance needs

##### **Identifying the core Authority objectives and the associated risks**

The strategic objectives of the Authority are targeted at four key priorities areas Communities and Partnerships, Response, People and Value for Money.

Value for Money recognises the need to respond to external influences and challenges faced by the Authority in delivering, with fewer resources, the high quality services expected by the community. As a result it is an over-riding priority in each of the key priorities areas:

	<u>Communities And Partnerships</u>
1	To improve the safety of our communities at risk from fire
2	To improve road safety through targeted action
3	To improve the quality of life and economic prosperity of local communities.
4	To advise and enforce on fire safety issues across the West Midlands to comply with fire safety legislation
	<u>Response</u>
5	To deliver a safe, economic, efficient and effective emergency response service.
	<u>People</u>
6	To ensure that we have the right staff, with the right skills, in the right place, at the right time



The key risks to the Authority, as identified through its risk management process are as follows:

	Risk
1	The Fire Authority would be unable to maintain the positive engagement of its employees, resulting in an inability to deliver its key priorities and objectives.
2	The Fire Authority would be unable to maintain an effective ICT provision (excluding mobilising and communications), resulting in significant disruption to the organisation's ICT functionality.
4	The Fire Authority would be unable to ensure that proper controls are established whilst working in partnership with other agencies/groups, resulting in a significant impact upon the organisation's financial standing, reputation and ability to deliver key objectives.
5	The Fire Authority would be unable to deliver the core objectives of preventing, protecting and responding effectively as a result of extensive disruption to normal working methods.
6	The Fire Authority would be unable to ensure that operational incidents are dealt with safely and effectively using appropriate levels of resources and personnel.
7	The Fire Authority would be unable to deliver the core objectives of preventing, protecting and responding effectively as a result of insufficient or ineffective key assets such as buildings and vehicles.
8	The Fire Authority would be unable to deliver the core objectives of preventing, protecting and responding effectively due to a lack of funding or the misuse of funds, e.g. fraudulent activity.
9	The Fire Authority would be unable to deliver the core objectives of preventing, protecting and responding effectively as a result of insufficient or ineffective employees.
10	The Fire Authority would be unable to manage its responsibilities under the Regulatory Reform (Fire Safety) Order and associated legislation resulting in a decline in non-domestic fire safety standards or legal action being taken against the Authority.
11	The Fire Authority would be unable to maintain its command and control function, resulting in an inability to receive, process and respond to emergency calls effectively.
13	The Fire Authority suffers a significant health, safety or environmental failure, resulting in legal challenge and/or litigation.

### Identifying the “audit universe”

In order to undertake the assessment, it is first necessary to define the audit universe for the Authority. The audit universe describes all the systems, functions, operations and activities undertaken by the Authority. Given that the key risk to the Authority is that it fails to achieve its objectives, we have identified the audit universe by determining which systems and operations impact upon the achievement of the core objectives of the Authority, as identified above, and the management objectives in section 3 above. These auditable areas include the control processes put in place to address the key risks. The auditable areas identified within the audit universe are set out in Appendix A.



### Assessing the risk of auditable areas

Risk is defined as “The threat that an event or action will adversely affect an organisation's ability to achieve its Business objectives and execute its strategies.” Source: Economist Intelligence Unit - Executive Briefing.

There are a number of key factors for assessing the degree of risk within the auditable area. These have been used in our calculation for each auditable area and are based on the following factors:

- Risk
- Business Impact
- Materiality
- Audit Experience
- Potential for Fraud and Error

### Deriving the level of risk from the risk values

In this model, the assignment of the relative values are translated into an assessment of risk. The risk ratings used are high, medium or low to establish the frequency of coverage of internal audit.

## 6 Developing a strategy for Internal Audit

The Strategy for Internal Audit is based on management's risk priorities, as set out in the Authority's own risk analysis/assessment. The Strategy has been designed so as to, wherever possible, cover the key risks identified by this risk analysis.

In establishing a strategy for Internal Audit, the relationship between risk and frequency of audit remains absolute. The level of risk will always determine the frequency by which auditable areas will be subject to audit. This ensures that key risk areas are looked at on a frequent basis. The aim of this approach is to ensure the maximum level of assurance can be provided with the minimum level of audit coverage.

In the course of the period covered by the internal audit strategy, the priority and frequency of audit work will be subject to amendment in order to recognise alterations in the audit needs assessment/risk analysis, caused by change within the Authority. Auditor's judgement has been applied in assessing the number of days required for each audit identified in the strategic cycle. The Strategy for Internal Audit is not static, but a dynamic plan which may be updated periodically to reflect changes in the risks faced by the Authority.

The assessment of assurance need's purpose is to:

- determine priorities and establish the most cost-effective means of achieving audit objectives;
- assist in the direction and control of all audit work

This approach builds upon the previous Strategy for Internal Audit prepared for 2012/13. Included within the strategy, in addition to audit days for field assignments are:

- a contingency allocation, which will be utilised when the need arises, for example, special projects, investigations, advice and assistance, unplanned and ad-hoc work as and when requested. This element has been calculated on the basis of past experience.
- a follow-up allocation, which will be utilised to assess the degree of implementation achieved in relation to recommendations agreed by management during the prior year.

- an audit management allocation, which is used for management, quality control, client and External Audit liaison and for preparation for, and attendance at various meetings including the Audit and Performance Management Committee.

## 7 Considerations required of the Audit Committee

- Are the objectives and key risks identified consistent with those recognised by the Authority?
- Does the audit universe identified include all those systems which would be expected to be subject to internal audit?
- Are the risk scores applied to the audit universe reasonable and reflect the Service as it is recognised by the Authority?
- Does the Strategy for Internal Audit cover the key risks as they are recognised?
- Is the allocation of audit resource accepted, and agreed as appropriate, given the level of risk identified?

## 8 Information to support the Internal Audit Strategy

### Resources required

Appendices A and B provides details of the resources required for delivery of the strategy over its three year life cycle. It is envisaged that 210 audit days will be required in 2013/14.

### Communication of results

The outcome of internal audit reviews is communicated by way of a written report on each assignment undertaken. However, should a serious matter come to light, this will be reported to the appropriate level of management without delay.

### Staffing

Where appropriate, audit staff are either professionally qualified, or sponsored to undertake relevant professional qualifications. All staff are subject to an appraisal programme, which leads to an identification of training needs. In this way, we ensure that staff are suitably skilled to deliver the internal audit service. This includes the delivery of specialist skills which are provided by staff within the service with the relevant knowledge, skills and experience.

### Quality assurance

Our procedures manual stipulates the quality control mechanisms that will operate on each audit assignment. The manual has been constructed so as to ensure that we meet the requirements of and complies with appropriate professional and technical standards for internal audit work. The quality of work is assured through the review of files of working papers and reports by a Client Lead or the Head of Audit.

## West Midlands Fire Service - Strategy for Internal Audit

For the period: 1 April 2013 to 31 March 2016

## Appendix A

Auditable Areas:	Risk	13/14	14/15	15/16
<b>Director – Technical and Operational Support (TOpS)</b>				
Performance Management	Medium			√
Risk Management	High	√	√	√
Follow up	-	√	√	√
<b>Director - Human Resources</b>				
Sickness/Absence Management	Medium	√		
Workforce Planning	Medium			√
Governance	High	√	√	√
<b>Director – Operations</b>				
Business Continuity Plan	Medium			√
Environmental Protection Targets	Medium		√	
Fire Stations – Management of Fuel	Medium		√	
Partnerships	Medium	√		
<b>Director - Resources</b>				
Payroll /Pensions (KFS)	High	√	√	√
Accounts Receivable (KFS)	High	√	√	√
Accounts Payable (KFS)	High	√	√	√
Fixed Asset Accounting/Asset Planning (KFS)	High	√	√	√
Budgetary Control (KFS)	High	√	√	√
Bank Account	Medium	√		
Data Transparency	Medium	√		
Counter Fraud	-	√	√	√
IT	High	√	√	√
National Fraud Initiative	-	√	√	√
Procurement	Medium			√
<b>Other</b>				
Contingency	-	√	√	√
Management	-	√	√	√
Liaison with External Audit	-	√	√	√
<b>Total</b>		<b>205</b>	<b>190</b>	<b>190</b>

### Key

√	Auditable area will be subject to review in this year.
KFS	All key financial systems reviews are undertaken on behalf of the external auditors, in order to enable them to place reliance upon our work and reduce their workload accordingly.
-	Mandatory or best practice area.

### Audit Universe: Horizon Scanning

We are aware that the Authority is currently reviewing the viability of its wholly owned trading company 'West Midlands Fire Service Business Safety Limited'. Internal Audit may have a role to play in providing assurance to the Audit and Performance Management Committee on various aspects of the operation of the venture. Discussions will be held during the year with senior officers and the external auditors, in order to ensure that a coordinated assurance approach is undertaken.

We will also monitor the potential impact of government mutualisation proposals and any changes suggested by the Knight spending review.

The following areas within the Audit Universe were scored as **low risk** and therefore do not appear in the above Strategy for Internal Audit. However, the scores will be revisited on an annual basis, and should the risk increase they will be incorporated:

- |                                     |
|-------------------------------------|
| • Health and Safety                 |
| • Training                          |
| • Maintenance of Vehicles           |
| • Insurance Claims on vehicles      |
| • Freedom of Information            |
| • Long Term Planning                |
| • Treasury Management               |
| • Purchase/Disposal of Vehicles     |
| • Home Safety Checks                |
| • Asset Protection/Inventory System |

## West Midlands Fire Service - Periodic Audit Plan for the period 1 April 2013 to 31 March 2014

Auditable Area	Purpose	Risk Category	Estimated Days
<b>Director – TOPS</b>			
Risk Management <i>(The Head of Internal Audit is required to give an annual opinion on the adequacy and effectiveness of the Service's risk management arrangements.)</i>	A review to ensure the Service is adequately identifying, assessing and managing the risks it faces in achieving its objectives, including the continued development of a detailed assurance mapping process.	High	10
Follow up <i>(Internal Audit is required to obtain assurances that previously agreed actions have been implemented.)</i>	A follow up of the key audit recommendations made during the previous year.	-	10
<b>Director - Human Resources</b>			
Sickness/Absence Management	A review of recording procedures with a particular focus on sickness "hotspots"	Medium	10
Governance <i>(The Head of Internal Audit is required to give an annual opinion on the adequacy and effectiveness of the Service's governance arrangements.)</i>	An annual review of aspects of the Service's governance arrangements, based upon the CIPFA/SOLACE model.	High	15
<b>Director – Operations</b>			
Partnerships	A review of the strategic management (governance, reporting, risk etc) of key partnerships with particular emphasis on monitoring and measurement of outcomes.	Medium	10

Auditable Area	Purpose	Risk Category	Estimated Days
<b>Director - Resources</b>			
<i>Key Financial System Reviews are undertaken on behalf of the Authority's external auditors. Where appropriate, using guidance supplied by them, in order to enable them to place reliance upon the work of internal audit and reduce their workload according. All such reviews are deemed as high risk by their very nature.</i>			
Payroll /Pensions	A review of the key financial controls relating to the administration of the Payroll System.	High	15
Accounts Receivable	A review of the key financial controls relating to invoicing and collection of debts.	High	15
Accounts Payable	A review of the key financial controls relating to the ordering and payment of goods and services.	High	15
Fixed Asset Accounting	A review of the key financial controls relating to the accurate recording of fixed assets. Consideration will also be given to assessing the impact of potential asset sales and valuation reductions due to the economic climate.	High	15
Budgetary Control	A review of the key financial controls relating to Budgetary Control.	High	10
Bank Accounts	A review of the internal control processes around the operation of the Authority's bank accounts.	Medium	10
Data Transparency	A review of compliance with the Code of Recommended Practice for Local Authorities on Data Transparency issued by DCLG and Local Spending Data Guidance issued by the LGA, and other general transparency issues.	Medium	8
Counter Fraud <i>(Demonstrating a pro-active approach to countering fraud and corruption is a key element of the requirements of the External Auditors.)</i>	A range of pro-active fraud activities will be undertaken including maintenance of a fraud risk register, targeted pro-active testing of areas within the Company open to the potential of fraudulent activity, money laundering, hosting a raising fraud awareness seminar and benchmarking against recognised best practice such as the Audit Commission's Protecting the Public Purse, CIPFA's Managing the Risk of Fraud (red book 2) and the National Fraud Authority's "Fighting Fraud Locally".	N/A	10
IT <i>(IT systems are a key element of the internal control environment, over which The Head of Internal Audit is required to give an annual opinion.)</i>	A continuous programme of IT auditing and providing ongoing advice and assistance on IT related controls. This will include focussing upon areas such as Procurement, Information Security Standards, IT Policies, and use of the Internet.	High	12

Auditable Area	Purpose	Risk Category	Estimated Days
National Fraud Initiative	We will lead on the Authority’s NFI requirements. The abolition of the Audit Commission will see the NFI exercise overseen by a new body. We will work with whatever new organisation is assigned this role, in order to ensure that the Authority continues to meet all its responsibilities.	N/A	10
Other			
Contingency	Special projects, investigations, advice and assistance, unplanned and ad-hoc work as and when requested.	N/A	10
Management	An allocation of time for the management of the internal audit service. To include meeting any training requirements of the Authority or Members and for preparation for, and attendance at, various meetings including the Audit Committee (to include a Committee skills audit and self assessment workshop).	N/A	15
Liaison with External Audit	Liaison with Grant Thornton on a regular basis throughout the year, including working with them during the transition period following the abolition of the Audit Commission.	N/A	5
Total			205