

By: Jonathan Idle – Head of Internal Audit
To: Governance and Audit Committee – 21st January 2021
Subject: **EFFECTIVENESS OF EXTERNAL AUDIT AND
INTERNAL AUDIT LIAISON**
Classification: Unrestricted

Summary:

This paper highlights the liaison arrangements between External Audit and Internal Audit.

Recommendation:

The Governance and Audit Committee note this annual update on liaison arrangements between Internal Audit and External Audit for assurance.

FOR ASSURANCE

1. Introduction

1.1 The requirement for Internal and External Audit to liaise in an effective way is recognised by professional guidance within both disciplines. The Chartered Institute of Internal Auditors (IIA) states that:

“Although internal and external audit need to maintain clear boundaries and independence from each other, both functions complement one another. Therefore, it is beneficial for external and internal audit to maintain an appropriate, constructive, and fluid two-way dialogue. This relationship will ensure they coordinate efforts and share valuable information, such as the internal audit programme of work, the external audit management plan, the risks each function has identified, or changes in legislation/regulation.”

1.2 This is reflected in the Public Sector Internal Audit Standards, which include the following in respect of liaison between External and Internal Audit:

“The chief audit executive should share information and coordinate activities with other internal and external providers of assurance and consulting services to ensure proper coverage and minimise duplication of efforts (Standard 2050).

1.3 External Audit’s work is governed by the International Standards on Auditing (ISAs). In particular ISA 610 requires External Audit to:

- Determine whether, and to what extent, to use specific work of the internal auditors; and
- If using the specific work of the internal auditors, to determine whether that work is adequate for the purposes of the audit.

- 1.4 ISA 610 is clear that effective internal auditing will often allow a modification in the nature and timing, and a reduction in the extent of audit procedures performed by the external auditor. It also states, however, that the external auditor may decide that internal auditing will have no effect on external audit procedures. In coming to a conclusion whether to rely on the work of internal audit, the external auditor usually makes an assessment of internal audit's organisational status, objectivity and scope of the function, technical competence of the team and the due professional care in place.
- 1.5 One of the issues raised within the publication of the "Independent Review into the Oversight of Local Audit and the Transparency of Local Authority Financial Reporting" (Redmond Review) was to emphasise the need and benefit of close working between External And Internal Audit. This included commentary that as internal auditors are much closer to the business than external audit and focus upon governance and service delivery matters then "...this could make internal audit a rich source of knowledge, should the external audit team wish to use it."
- 1.6 Furthermore, the NAO's new value for money Code comes into place for 2020/21 external audits. There is a specific requirement for external auditors to reach a view on financial sustainability, governance and economy, efficiency and effectiveness. This will almost certainly involve drawing on the work of Internal Audit, particularly around governance.
- 1.7 It is important to understand that both functions have very different remits. Internal Audit is an independent assurance function within the Council, whereas External Audit is responsible for giving an independent opinion on the Council's financial statements and a conclusion on its arrangements to secure value for money through economic, efficient and effective use of its resources.
- 1.8 It has been noted in previous reports to the Committee and more widely across the public sector that the interaction between the two functions seems to have diminished over recent years.

2. Current practice

- 2.1 Over the last 18 months, External Audit and Internal Audit have ensured that there is regular liaison and communication on a range of issues, principally but not restricted to, regarding financially based reviews.
- 2.2 A key example of this has been the communicating of Internal Audit findings in respect of the Pension Fund Investment Governance Lessons Learned Review, which was a significant factor in consideration of External Audit's Value for Money conclusion for 2019-20 and review of the Council's Annual Governance Statement.
- 2.3 Additionally, Internal Audit regularly appraise External Audit of other key reviews and also liaise and consult in respect of audit coverage and planning on an ongoing basis.

3. Conclusion

- 3.1 There is a positive and constructive working relationship between Internal and External Audit, which reflects good practice endorsed by professional bodies.

4. Recommendation

- 4.1 The Governance and Audit Committee note this annual update on liaison arrangements between Internal Audit and External Audit for assurance.

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