

By: Alex King, Deputy Leader  
Samantha Buckland, Acting Head of Internal Audit  
To: Governance and Audit Committee – 29 November 2011  
Subject: **Effectiveness of Internal and External Audit Liaison**  
Classification: Unrestricted

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**Summary:** This paper summarises the effectiveness of the liaison arrangements between External and Internal Audit

## **FOR ASSURANCE**

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### **Introduction**

1. The requirement for Internal Audit and External audit to liaise in an effective way is recognised by the professional guidance within both disciplines. The potential efficiencies that can be realised when this liaison is effective can be high, both in terms of avoided external audit fees, but also in relation to the a reduced audit burden for finance and other front line staff. For this reason the Committee's Terms of Reference include the responsibility for the Committee to annually assess the co-operation between External and Internal Audit.

### **Professional requirements**

2. 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 for securing economy efficiency and effectiveness in its use of resources.
3. Although their overall remits differ, it should be possible for internal and external auditors to rely on each other's work, subject to the limits determined by their responsibilities. The CIPFA code of practice for Internal Audit places requires that:
  - It is possible for Internal Audit and External Audit to rely on each other's work.
  - There are regular meetings between the Head of Internal Audit and the External Audit Manager.
  - Internal and external audit plans are co-ordinated.
4. 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.
5. 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. However it also states 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.

### **Current practice**

6. External Audit's evaluation of Internal Audit has been positive over recent years and no concerns across the four criterion set out in ISA 610 have been raised. There are regular meetings between the two sections to co-ordinate plans. In 2011/2012 Internal Audit is undertaking a number of core financial reviews where we have liaised with External Audit to minimise any potential duplication and to work together as much as possible, this includes the following audits where documentation of the systems and testing will be undertaken jointly:
  - Treasury Management
  - Pensions contributions
  - Pensions investment income
7. In addition the work that the Internal Audit section completes to provide assurance to the Section 151 Officer, and authority wide reviews such as Corporate Governance, Risk Management and Performance Management, can be utilised by the External Auditors to inform their risk assessment of the Council.

### **Conclusion and next steps**

8. Liaison between Internal Audit and External Audit is in place, and there is reliance placed on the work on Internal Audit by the External Audit team where this is relevant.
9. At present Internal Audit spend a significant part of each year's audit plan reviewing the Councils financial systems. Aspects of this work have been tailored to provide the assurance required by External Audit in relation to financial systems and accounts, whilst at the same time providing the required assurance to the Council in relation to Internal Control. It is also possible for the Internal Audit section to deliver specific reviews to address some of the risks identified by External Audit.
10. Both Internal and External Audit are starting to consider their plans for the 2012/2013 year. The Acting Head of Internal Audit has agreed with the Audit Commission to seek synergy between the two audit plans, and it is hoped that this will be reflected in the plans presented for approval by the Committee next year.

### **Recommendations**

11. Members of the committee are asked to
  - Receive the annual update on liaison arrangements between Internal and External Audit for assurance.

**Samantha Buckland**  
**Acting Head of Internal Audit**  
**Ext: 4611**