

By: Neeta Major, Head of Internal Audit
To: Governance and Audit Committee – 18 December 2013
Subject: **Effectiveness of Internal and External Audit Liaison**
Classification: Unrestricted

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

FOR ASSURANCE

Introduction

1. The requirement for Internal Audit and External audit to liaise in an effective way is recognised by professional guidance within both disciplines. Effective liaison can reduce the audit burden for finance and other front line staff. For this reason the Committee's Terms of Reference includes the responsibility for the Committee to annually assess the co-operation between Internal and External 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.
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. This was reflected in Grant Thornton's 2012-2013 financial resilience report presented to the July Committee. There are regular meetings between the two

teams to share, discuss and co-ordinate plans. The liaison arrangements are documented within a protocol shown at Appendix 1 to this report.

7. In 2013/2014 Internal Audit is undertaking a number of core financial reviews and is liaising with Grant Thornton to ensure that they can use any work to inform their audit, co-ordinate timing and reduce duplication wherever possible.
8. The key financial systems audits that Internal Audit are undertaking in quarter four of 2013/14 where there may be the possibility of sharing systems documentation or controls testing are as follows;
 - Payroll follow up
 - Accounts payable
 - Treasury management
 - Pensions contributions
 - Pensions investment income
9. In addition the work that the Internal Audit section completes to provide core assurance e.g. Corporate Governance, Risk Management, and performance management is utilised by the External Auditors to inform their risk assessment of the Council. For 2012/2013 the corporate governance review was performed in conjunction with the External Auditors.

Conclusion and next steps

10. Liaison between Internal Audit and External Audit is in place and working effectively. Reliance is placed on the work of Internal Audit by the External Audit team where this is relevant.
11. Both Internal and External Audit are starting to consider their plans for the 2014/2015 year (for external audit this is in relation to the 2013/2014 financial statements). The Head of Internal Audit has agreed with Grant Thornton to coordinate the timing and approach to work wherever possible. This will be reflected in the plans presented for approval by the Committee in April next year.

Recommendations

12. Members of the committee are asked to note this annual update on liaison arrangements between Internal and External Audit for assurance and the protocol at Appendix 1.

Appendices

Appendix 1 KCC Internal Audit – External Audit Protocol

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