CORPORATE & BUSINESS SYSTEMS

ATTACHMENT B

ESTABLISHMENT OF AUDIT RISK AND IMPROVEMENT COMMITTEE

ORDINARY MEETING

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Internal Audit Guidelines

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Chief Executive's Foreword

Internal audit is an essential component of a good governance framework for all councils. At both a management and councillor level, councils must strive to ensure there is a risk management culture. Internal audit can assist in this regard.

Internal audit is widely used in corporate Australia as a key mechanism to assist councils to manage risk and improve efficiency and effectiveness. At Federal and State Government levels there are clear requirements for internal audit and risk management.

There is also growing acceptance of the importance of internal audit and risk management in local government. It is pleasing to see that a number of councils in New South Wales are showing leadership in fully embracing this concept. However, a survey of councils conducted in 2009 by the Division of Local Government designed to assess the progress of councils in implementation of the internal audit function highlighted that while progress is being made, there is still opportunity for improvement. Effective internal audit and risk management processes should become part of the 'business as usual' operations of councils.

With the implementation of Integrated Planning and Reporting, internal audit will play a vital role at ensuring that the strategies adopted by council are being followed.

These guidelines propose oversight of council systems and processes through an audit committee. The combination of an effective audit committee and internal audit function provide a formal means by which councillors can obtain assurance that risk management is working effectively. Similarly the internal audit process is an on-going mechanism to ensure that the recommendations of the Promoting Better Practice reviews undertaken by the Division of Local Government have been fully implemented.

This guide has been designed to help councils and county councils develop and implement internal audit and risk management frameworks that will in turn build community confidence in their managerial performance. I encourage all councils to use this guide to assist them in building their own internal audit capability within their organisations.

Ross Woodward
Chief Executive, Local Government
A Division of the Department of Premier and Cabinet

1. Introduction

The NSW Division of Local Government (DLG) believes that a professional Internal Audit function is one of the key components of the effective governance of any council. In 2001, the Independent Commission Against Corruption (ICAC) found that while 80% of local council General Managers agreed that internal audit is important, only 20% of councils had an internal audit function or audit committee.

These Internal Audit Guidelines, first released in 2008, are aimed at assisting councils put into place effective internal audit practices.

In 2009 the DLG conducted a survey of councils to assess how they were progressing with the implementation of the recommendations of the Guidelines. While the results of the survey revealed that considerable progress has been made toward the implementation of the Guidelines, with more than 50% of councils reporting that they had an internal audit function, it also identified that there were some areas where some councils appeared to be having difficulties and some areas where the Guidelines needed to be clarified.

These revised Guidelines have been developed to address the issues arising from the survey.

The Guidelines are designed to provide councils with assistance to implement internal audit and risk management. There are already a large number of internal audit standards, guidelines and publications in existence, such as the Institute of Internal Auditors' Internal Audit Framework, Better Practice Guidelines – Local Government Entity Audit Committees and Internal Audit (Victoria) and A Guide to Leading Edge Internal Auditing in the Public Sector (Manitoba).

These Guidelines are Director General's Guidelines for the purposes of section 23A of the *Local Government Act 1993,* issued by the Chief Executive, Local Government under delegated authority. They describe internal audit and risk management systems for Local Government in NSW. The Guidelines also include appropriate structures, functions, charter, and membership of audit and risk management committees.

The Division acknowledges the lead role of the Local Government Internal Audit Network (LGIAN*)* and the Institute of Internal Auditors in the development of these Guidelines*.*

Terminology

The following terms are used throughout this guidance paper:

- Council is used in two contexts. Council can refer to the elected body of councillors, the local government administration and staff and/or the entity as a whole. The term also includes county councils.
- The General Manager is the most senior member of management as per section 335 of the Local Government Act. Chief Financial Officer (CFO) refers to the most senior member of staff within the finance and accounts area of the council.
- Internal Audit Activity is used interchangeably with 'internal audit function' in recognition that there are several methods of resourcing an internal audit function, including outsourcing this to a third party provider or sharing resources with other councils.
- Audit Committee is the name used for the committee which provides independent oversight of both the internal audit function and the external audit function. It provides the council with independent oversight and monitoring of the council's audit processes,

including the council's internal controls activities. This oversight includes internal and external reporting, risk management activities, internal and external audit, and compliance. It is not uncommon for the committee charged with these responsibilities to be referred to by other names such as governance and risk management committee; audit and risk management committee; internal audit committee.

- External Audit refers to the review and certification of the financial reports as per section 415 of the *Local Government Act 1993*.
- Enterprise Risk Management is the holistic management of all risks within council, not just insurable risks or Occupational Health and Safety.

1.1. What is Internal Audit?

Internal audit is described as *'an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations.*

It helps an organisation accomplish its objectives by bringing a systematic disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.' [1]

Internal audit's role is primarily one of providing independent assurance over the internal controls and risk management framework of the council.

Management has primary day-to-day responsibility for the design, implementation, and operation of internal controls.

Internal audit has no direct involvement in day-to-day operations, but it has a direct functional relationship with the General Manager and the council. An effective internal audit function should evaluate and monitor the adequacy and effectiveness of the internal control framework as a minimum.

Risk management is also an essential part of a council's management and internal control framework. It looks at what risks the council may face and the best way to address these risks. Assessment and management of risk is central to determining internal audit activities.

Internal audit's core competencies are in the area of internal control, risk and governance. Typically, internal audit's scope will include some or all of the following areas:

- Reliability and integrity of financial and operational information
- Effectiveness and efficiency of operations and resource usage
- Safeguarding of assets
- Compliance with laws, regulations, policies, procedures and contracts
- Adequacy and effectiveness of the risk management framework.

1.2. Why my council should have an internal audit function.

All councils should have an internal audit function for the following reasons:

- it supports good internal governance
- to ensure consistency with other levels of government
- to improve the effectiveness of risk management, control and governance processes
- helps to instil public confidence in an organisation's ability to operate effectively.

When considering an internal audit function, councils should consider the following issues:

- The need to extend council's understanding of risk management beyond traditional areas of public liability and occupational health and safety, into areas such as internal governance, fraud risk and broader regulatory risk.
- Whether council should have a uniform approach to assessing and managing risk, regardless of size or location.
- Whether it is feasible for council to pool resources with like councils or arrange through regional organisations of councils for internal audit services.

[1] *International Professional Practice Framework (IPPF) 2009, The Institute of Internal Auditors, www.iia.org.au*

- Whether small management teams can feasibly conduct audits or internal reviews in the absence of an audit function, with an appropriate degree of independence and objectivity.
- How council can properly resource internal audit and internal control programs.

1.3. How does internal audit fit in with other governance functions and activities?

Good governance requires an organisation to have a proper framework in place to ensure excellence in decision making, and that decisions are implemented efficiently and effectively. Key components of good governance include the use of:

- Audit Committees
- Internal and External Audit
- Enterprise Risk Management

1.3.1. The Audit Committee

An audit committee plays a pivotal role in the governance framework. It provides councils with independent oversight and monitoring of the council's audit processes, including the council's internal controls activities. This oversight includes internal and external reporting, risk management activities, internal and external audit, and compliance[2]. Given the key role of the Audit Committee, for it to be most effective it is important that it is properly constituted of appropriately qualified independent members.

A strong relationship between the audit committee and internal audit enables the committee to meet its responsibilities and carry out its functions. An audit committee establishes the role and direction for internal audit, and maximises the benefits from the internal audit function.

More information on the Division's expectations of audit committees in Local Government is set out in section 4 of this document.

1.3.2. External Audit

External audit is a statutory function that provides an opinion on the council's annual financial reports, as required under Divisions 2 and 3 of the *Local Government Act 1993*. The primary focus and responsibility is on providing an opinion on the financial report to council and its external stakeholders.

Councils should be aware that the external auditor should not be expected to conduct a deep or thorough review of the adequacy or effectiveness of a council's risk management framework or internal controls. To obtain a deeper understanding of the scope of the external auditor's report it is recommended that you read the disclaimer contained in the external audit report in your council's statutory financial reports. The external auditor may place some reliance on internal audit reviews, monitoring of internal control, including fraud control and risk management as per the Australian Auditing Standards.

An effective internal audit function may contribute to the performance of external audit, as the external auditor may be able to rely on some of the internal audit work performed, and the stronger internal control environment that a strong internal audit function can create. This may have an indirect benefit in reducing audit fees.

[2] *Auditing and Assurance Standards Board, Australian Institute of Company Directors, Institute of Internal Auditors, Audit Committees A guide to good practice 2008*

1.3.3. Management

Management has primary responsibility for the design and operation of the risk management and internal control frameworks of the council. It is separate from the responsibilities of external audit, internal audit and the audit committee. While these functions provide advice and oversight in relation to the risk management and internal controls, they are not responsible for its design or implementation. This responsibility lies solely with management. Good governance in local government relies on a robust independent review of management, finances, risks and operations.

1.3.4. Risk Management

Risk management is an important component of corporate governance. Risk management is the responsibility of management with oversight by council and the audit committee. Internal audit can assist management to identify and evaluate the effectiveness of council's risk management system and contribute to the improvement of risk management and control systems. The annual Internal Audit plan should be developed after consideration of the council's risk registers and those areas that are high risk to the organisation.

Internal audit will usually provide advice and assurance over the risk management and internal control frameworks, but in order to maintain independence, internal audit will not be responsible for its implementation of risk management or making decisions on how risks should be treated. Risk management is an important area that is touched upon in more detail in section 5 of this document.

2. Establishing an Internal Audit Function

Key strategies aimed at ensuring that internal audit services conform with good practice:[3]

- Establish an audit committee, with a majority of members who are external (independent) to council
- Set up an independent reporting structure for internal audit (i.e report functionally to the audit committee and administratively to the General Manager) and define its functions and responsibilities with an internal audit charter
- Adopt and comply with professional internal auditing standards
- Recruit and retain capable staff
- Establish and communicate a clear internal audit vision and strategy
- Demonstrate the value of internal audit
- Understand council, management and community stakeholder needs
- Focus on risk
- Review internal controls
- Educate management on risks and controls
- Continuously improve the quality of internal audit services.

Key Attributes of a good practice internal audit function in local government:[4]

- Maintain independence and objectivity
- Have clear roles and responsibilities
- Comply with the internal auditors International Standards for professional practice of internal auditing in planning and executing work
- Have sufficient and appropriate resources to carry out audit work, as well as the necessary skills, experience and personal attributes to achieve what is expected of internal audit
- Have regular and timely communication of findings and recommendations
- Systematically conduct regular follow-ups on audit recommendations
- Continuously monitor internal audit effectiveness
- Adding value by proactive auditing and advice
- Develop audit plans that are comprehensive and balanced, and are linked to council's management of risks.

[3] Jeffrey Ridley and Andrew Chambers. Leading Edge Internal Auditing. ICSA Publishing, 1998, pgs. xxxiii, and 10 to 17.

[4] Ridley and Chambers: as above

2.1. Internal Audit Charter

An internal audit charter provides a comprehensive statement of the purpose, authority, responsibilities and reporting relationships of the internal audit function. The audit committee or council should approve the internal audit charter.

The content of an internal audit charter should:

- Identify the purpose, authority and responsibility of the internal audit function
- Establish internal audit's position within the organisational structure
- Define reporting relationships of the internal auditor with the General Manager and the audit committee
- Define internal audit's relationship with the council's external auditor
- Have provisions that authorise access to records, personnel, physical property, and attendance at relevant meetings
- Define the scope of internal audit activities, including any restrictions.

The internal auditor should periodically assess whether the purpose, authority and responsibility, as defined in the charter, are still adequate. Results of the assessment should be communicated to the audit committee.

A sample internal audit charter is contained at Appendix 3. Councils should tailor their charters as considered appropriate for their circumstances.

The audit committee should also have a charter that sets out its roles and responsibilities and its oversight of the internal and external audit functions, including any statutory duties. The elected council should approve the audit committee charter (Appendix 2). An external quality assessment every 5 years would assist this process.

2.2. Professional Standards

Internal auditors in NSW local government should comply with appropriate professional standards, such as the Institute of Internal Auditors (IIA) Standards and Code of Ethics. A summary of the standards is shown at Appendix 1. The standards should be the basis of policies, procedures, and plans. Internal audit should be performed with integrity, objectivity, confidentiality and competency.

IIA Standards include the expectation that an internal audit function will establish policies and procedures to guide internal staff in carrying out their work. Policies and procedures should be periodically reviewed to ensure they are up to date with changes in professional practice.

The IIA is thanked for their kind permission to reproduce these standards in this document.

2.3. Reporting lines

Generally, the internal audit function is led by a chief audit executive who is the most senior member of staff in the organisation responsible for the internal audit function. The IIA's Standards for the professional practice of internal auditing state that *"The Chief Audit Executive must report to a level within the organisation that allows the internal audit activity to fulfil its responsibilities. The chief audit executive must confirm to the board, at least annually, the organisational independence of the internal audit activity. The internal audit activity must be free from interference in determining the scope of internal auditing, performing work, and communicating results".*

For local government, the Internal Auditor should report functionally to the audit committee and administratively to the General Manager. If matters involve the conduct of the General Manager, an alternate reporting chain to the Mayor or a protected disclosure to the ICAC, Ombudsman or the Division of Local Government (about serious and substantial waste in local government) should be in place.

It should be remembered that pursuant to section 335 of the Local Government Act the General Manager is responsible for the day-to-day management of council activities including the direction of staff and implicitly the internal audit function. The General Manager may choose to delegate this responsibility provided always that the delegation does not directly or indirectly interfere with the ability of the Internal Auditor to conduct an internal audit function free from interference as required by the IIA's Standards, referred to above (see section 3.4 below).

A clear and properly defined reporting relationship ensures that the Internal Auditor is empowered to perform their role working with management. The direct reporting line to the Audit Committee also acts as an adequate safeguard in the event of a serious breakdown in internal controls or internal control culture at senior levels in the organisation.

Due to the reporting relationships of this key role, it is important that councils appoint an internal auditor who has credibility, and can build relationships and influence decisions at the most senior levels of council, including the audit committee and the General Manager.

2.4. Options for Resourcing Internal Audit

Regardless of size, councils are encouraged to have an appropriately resourced internal audit function. An internal audit function should have sufficient and appropriate resources to carry out its work, including skilled auditors, appropriate technology tools, budgets and professional development opportunities. Budget allocations should align to the approved audit plans.

While size and complexity of a council's operations will drive the size and overall budget of its internal audit function, a small size of operation does not justify forgoing internal audit altogether. The most efficient and effective means of resourcing the internal audit function depends upon the individual circumstances of the council. It is recognised that smaller councils may not be able to justify a full-time internal auditor. Guidance is provided below on alternative resourcing models that may achieve the required outcomes on a cost effective basis.

2.4.1. Appointment of Full-Time or Part-Time Internal Auditor

Ideally the internal auditor should be an independent position reporting directly to the Audit Committee and administratively to the General Manager, with no other operational or management responsibilities. The role and duties and a sample position description are described in more detail in the appendices.

Depending upon the size and complexity of the organisation, councils may consider appointing an internal auditor or internal audit team. The appointment could be full-time or part-time personnel and may be staffed by more than one auditor if the size of the council demands.

Position descriptions should be set for internal audit staff and should identify required qualifications and competencies, including:

- Proficiency in applying internal audit standards, procedures and techniques
- Proficiency in accounting principles and techniques if working extensively with financial records and reports

- An understanding of management principles required recognising and evaluating the significance of deviations from good business practices
- An appreciation of fundamental concepts in areas such as accounting, economics, commercial law, taxation, finance, quantitative methods and IT
- Effective interpersonal skills
- Skills in oral and written communication
- Ability to identify key issues in any area under review
- Ability to influence senior management as and when required
- Knowledge of key information systems technology risks and controls and available technology-based audit techniques.

2.4.2 Outsourced or co-sourced function

Providing that independence requirements are adhered to, councils can contract their internal audit function to private sector accounting firms or internal audit service providers. If this is the preferred option, then councils need to ensure that the service provided is for a professional internal audit service and not an extension of the financial assurance based external audit.

Councils should note that outsourcing or co-sourcing the internal audit function does not abrogate the council's responsibility to oversee and manage the internal audit function.

In monitoring the performance of the internal audit services provided by accounting firms, councils need to ensure that an appropriately qualified auditor is conducting the internal audit. To ensure an effective and comprehensive internal audit program, contracted internal auditors should have authority to independently set an ongoing audit program, which is not constrained by a narrow scope of audit coverage pre-determined by management.

A co-sourced function is one where a staff internal auditor supplements audit services with an outsourced internal audit service provider. An outsourced internal audit function is one where the service provider assumes all the responsibilities of the internal audit function.

Several options are set out below:

- Private sector accounting firms – most large accounting firms have specialist internal audit divisions, which provide a good service. Internal audit is a specialised skill and hence councils are advised to only use firms who have a specialised internal audit division.
- Boutique firms – a number of boutique firms exist that specialise in internal audit services.
- Internal audit contractors – there a range of experienced internal audit contractors available for this sort of work.
- NSW GTE - IAB Services is a State Government agency that provides internal audit services to the public sector.

Each of these options will have their advantages and can be appropriate for different circumstances. The advantages of using external providers include: flexibility; access to a wide range of expertise; ability to access the service as and when required. Disadvantages include loss of corporate knowledge and possible increased costs.

The NSW State Contracts Control Board has compiled a panel of qualified internal audit service providers at competitive rates through a competitive tender process. Councils are able to access this panel to save them time and effort in the procurement process and are encouraged to do so.

2.4.3 Regional or Inter-Council Sharing of Internal Audit Resources

Councils are also encouraged to consider resourcing their internal audit function via collaborative arrangements with other councils or through a regional organisation of councils (ROC).

A ROC or some other body (such as a strategic council alliance) could agree to jointly employ or contract an appropriately qualified internal auditor. This may have benefits in terms of cross-council benchmarking, reduction in travel costs and access to a bigger resource pool than would be available to a single council.

Each council should nevertheless establish its own independent audit committee and the internal auditor would need to report separately to each council, maintaining confidentiality. A funding model could be established that shares the costs on a user-pays basis between participating councils, with internal audit costs based on an agreed cost sharing basis.

Under this model, the appointed internal auditor would prepare an audit plan for each council, based on individual council requirements. There will be some common systems and shared knowledge and tools, such as audit planning, risk assessment, audit programs and procedures.

A small team of internal auditors directed by a suitably qualified and experienced auditor could be appropriate for serving several smaller councils in adjacent local government areas. This model should result in lower audit costs compared to councils employing separate internal auditors or consultants at various management levels.

Risk assessments and annual audit plans need to be designed with input from senior management of each of the participating councils. The internal audit team will need to retain a high degree of independence from management in the planning and conduct of audits. The reporting framework will need to ensure the independence of the audits and confidentiality of findings. The internal auditor should report directly to the General Manager and the Audit Committee of each council.

2.4.4 Other Resources

The Local Government Internal Audit Network (LGIAN) represents internal auditors in NSW local government and adds value to local government by promoting better practice internal audit and sharing of information and resources. This group provides sharing of technical expertise by internal audit professionals who are experienced in local government operations, legislation and governance. Member councils host quarterly meetings. Contact details are available from the Division of Local Government.

3. Internal Audit Operations

3.1. Adding Value

One of the primary objectives of the internal audit function is to add value to the council operations. Adding value involves taking a proactive approach with a focus on risk, organisational concerns and effective controls at a reasonable cost. By focusing audit work on high risk areas, the organisation will benefit from assessments of their systems and gain independent assurance on whether those systems that are critical to program delivery are operating efficiently and effectively.

This risk approach contributes to preventative auditing, rather than relying on detecting issues and exceptions after they have already eventuated.

3.2. Roles and Responsibilities

An internal audit function should have clear roles and responsibilities. This includes complete and unrestricted access to employees, property and records. Roles and responsibilities should be communicated in the internal audit charter and position descriptions.

Policies and Procedures Checklist

Councils should establish a manual of policies / procedures that guide internal auditors in their work. The content of these policies / procedures should be consistent with relevant standards, such as the IIA Standards, and cover the following topics:

Attribute Standards

- Purpose, Authority and Responsibility
- Independence
- Proficiency and Due Care
- Quality Assurance

Performance Standards

- Managing the Internal Audit Activity
- Nature of the Work
- Engagement Planning
- Performing the Engagement
- Communication of Results
- Monitoring Progress
- Resolution of Management's Acceptance of Risk.

3.3. Independence and Objectivity

An internal audit function should maintain an appropriate level of independence and objectiveness through sound reporting relationships, and by those involved in internal audit activities avoiding bias and conflicts of interest.

3.3.1 Avoidance of Bias and Conflict of Interest

Policies and procedures should be in place to help an internal audit ensure against the risk of bias, particularly arising from perceived familiarity by virtue of long association with persons the subject of internal audit activity.

The Avoidance of Bias and Conflict of Interest Checklist

An internal auditor or person responsible for internal audit should have a process in place to ensure that:

- An internal auditor does not undertake audit work regarding operations / services for which he / she has held responsibility within the last two (2) years.
- An internal auditor who provides consulting services regarding a particular operation / service is not the same auditor who provides assurance on that same operation / service.
- Internal auditors are rotated periodically whenever it is practical to do so; alternatively, some other method is put in place to address the risks associated with having the same auditors responsible for auditing the same unit / functional area over a prolonged period.

Position Description Checklist

The internal audit function should have written position descriptions for each level of audit staff. The position descriptions for audit staff should identify required qualifications and competencies, including:

- Proficiency in applying internal audit standards, procedures and techniques
- Proficiency in accounting principles and techniques
- An understanding of management principles required recognising and evaluating the materiality and significance of deviations from good business practices
- An appreciation of fundamental concepts in areas such as accounting, economics, commercial law, taxation, finance, quantitative methods and IT
- Effective interpersonal skills
- Skills in oral and written communication.

3.4. Reporting Relationships

Councils establishing an internal audit function must provide appropriate independence for the internal audit function by establishing some degree of separation of the function from management.

In private companies, the internal auditor is accountable to the Board of Directors through the Chairman of the Audit Committee. This approach cannot be directly reproduced under the provisions of the *Local Government Act 1993*. Internal audit is an operational matter that falls within the responsibility of the General Manager. Under section 335(1) of the Local Government Act, the General Manager is responsible for the efficient and effective operation of the council's organisation.

The separation of powers between the General Manager and the elected council is a key element to the Act and accordingly both need to ensure that they do not interfere with or control the exercise of each of these functions. It is therefore not appropriate for an internal auditor to report directly to the mayor and/or councillors.

Internal auditors should be mindful of their obligation under section 11 of the ICAC Act to report suspected areas of corrupt activity. Further, they may wish to report their findings under the provisions of the *Protected Disclosures Act 1994*. This may be necessary if concerns are raised in regard to the General Manager or other senior staff.

Councils have the power to appoint an external audit firm to be the internal auditor. Where possible this firm should not be the same one that provides council's external audit services. This does not change the fact that internal audit remains an operational role. It should be remembered that pursuant to section 335 of the Local Government Act the General Manager is responsible for the day-to-day management of council activities including the direction of staff and implicitly the internal audit function.

While management employs the internal auditor, the internal auditor is also expected to review the conduct of management. Therefore, the internal auditor should be able to report to a person or body with sufficient authority to implement internal audit recommendations.

It is important for the internal auditor to have direct access to the audit committee to monitor the scope of the work of internal audit and to review the reports issued. This is achieved by having the internal auditor attend meetings of the audit committee.

The appointment of an internal auditor does not give council the ability to direct the performance of the internal audit function. However, councils can use the General Manager's employment contract to ensure that relevant internal audit work is being undertaken as a requirement of the General Manager's performance obligations.

The Internal Auditor should maintain independent reporting relationships with the audit committee, General Manager and management. This requires:

- Reporting functionally to the audit committee and administratively to the General Manager
- Reporting to an audit committee with external members
- Internal audit charter to be approved by the audit committee and the audit committee charter to be approved by council
- Audit committee to approve of internal audit plans, and provide a forum for discussion of areas worthy of internal audit attention
- Audit committee to ensure coordination and cooperation of internal and external auditors
- Audit committee to make enquiries of management to determine if the scope or budgetary limitations impede the internal audit's ability to function properly, and ensure that the internal audit function is properly resourced
- Reporting to the General Manager for budgeting and accounting, human resource administration, internal communications, administration of policies and procedures.

Reporting to an audit committee with a majority of members, who are external and independent to the council, ensures that internal audit operates independently from management and can effectively review risk, control, governance processes and management assertions.

Reporting Relationships Checklist

The audit committee should include persons external to the organisation. In the absence of an audit committee, the internal auditor should report to a level within the organisation that ensures that the internal audit is able to have broad audit coverage and to fulfil its responsibilities independently and objectively.

Reporting functionality to an audit committee means the committee:

- Approves the internal audit charter

- Approves short and long term audit plans
- Comments on the performance of the internal auditor
- Makes enquiries of management to determine if there are scope or budgetary limitations that impede internal audit's ability to function properly
- Ensures that the internal audit function is adequately resourced
- Approves the scope of external assessments of the internal audit
- Provides a forum for discussion to identify areas worthy of examination by internal audit
- Recommends to Council who should be the internal audit provider and/or has input into the selection of the Chief Audit Executive.

Reporting administratively to the General Manager relates to day to day operations of internal audit including:

- Budgeting and accounting
- Human resource administration
- Internal communication / information flow
- Administration of internal policies and procedures.

3.5. Internal Audit Plans

Internal audit should prepare an audit plan that identifies internal audit's objectives and strategies, and the audit work they will undertake.

Good practice internal audit plans will be based on a risk assessment of the council's key strategic and operational areas to determine an appropriate timing and frequency of coverage of each of these areas. Best practice will also include audit judgment of areas that should also be reviewed despite not appearing as a high priority in the council's risk profile.

The annual plan will generally be developed with input from the General Manager and senior management and approved by the audit committee. Generally, such a plan will identify:

- The audit projects that will be carried out during the year and rationale for selecting each
- When each audit project is expected to commence and the time allocated for each
- The performance measures that will be used to evaluate the performance in relation to established goals / objectives and strategies
- Any areas that cannot be covered within existing budgets and additional areas, which in the opinion of the internal auditor, should be reviewed
- Whether the audit projects identified require the use of external expertise.

A rolling three year plan of coverage can be proposed so that it can be readily determined what areas will be covered in any given year, and if their area is not covered in a given year, when it is scheduled for review. The ability of the internal auditor to execute this plan over a three year cycle is a useful method to assess whether internal audit is adequately resourced. However the plan should be reviewed at least annually to ensure that it still aligns with the council's risk profile.

Audit Plans Checklist

The internal auditor should have a long term strategic plan and annual work program to guide their work.

Long term strategic plans that are prepared with input from and approval by the internal audit committee should be risk based. They would generally include:

- A description of the goals / objectives of internal audit
- Key organisational issues and risks of the organisation prepared in consultation with senior management, the audit committee, the external auditor and other relevant parties
- The strategies / priorities in order to address issues and risks.

Mid term operational plans may also be prepared to assist an organisation in the implementation of the key strategies / priorities identified in the strategic plan. Typically these plans would include aspects such as:

- Staffing, competency needs
- Professional development
- Information technology requirements
- Budgeting requirements
- How performance monitoring, measurement, and internal / external assessments will be operationalised.

The annual audit plan is prepared with input from and approval by the audit committee. It should be developed based on the long term strategic plan and the mid term plan. Generally, such a program will identify:

- The audits and other types of projects that will be carried out during the year and the rationale for selecting each
- Staffing for each project, when it is expected to commence and the time allocated for each
- Financial budgets
- The performance measures that will be used to evaluate performance in relation to established goals / objectives and strategies
- As applicable, the plans for internal / external assessments of an internal audit group.

3.6. Performing Internal Audits

Internal Auditors should perform internal audit reviews in accordance with the accepted Institute of Internal Auditors (IIA) Standards and the IIA Code of Ethics for performance standards, practices and guidelines. An outline is shown in the appendices. This includes:

- planning the audit
- defining the audit scope
- identifying sufficient, reliable, relevant, and useful information to achieve the audit's objectives
- identifying and evaluating the risks
- analysis and evaluation of controls
- maintaining proper records of the audit and evidence collected and analysed
- performing tests

- making recommendations
- discussing audit results with relevant staff and management.

Internal Audit may also perform consulting engagements and investigations of allegations, depending on the roles conferred in the Internal Audit Charter. Professional standards should also be applied when conducting these types of reviews.

3.7. Communication of Audit Results

Internal audit should regularly communicate its findings and recommendations to the audit committee, General Manager and management of the areas audited. An internal audit report should communicate accurate, objective, clear, concise, constructive, complete and timely information.

Audit reports should normally include background information, the audit objectives, scope, approach, observations/findings, conclusions, recommendations and agreed management actions. Reports should promote better practice options and explain why the recommended changes are necessary and how they add value.

Reports and memos should share internal audit's observations on significant risk exposures, control issues, corporate governance issues, and other related audit matters. By sharing audit criteria, explaining causes and consequences of audit observations, councils can gain an understanding of the implications and impacts of the audit findings.

Depending on the size of the internal audit reports, summaries may be appropriate for the General Manager and the audit committee with full reports available on request.

Internal Audit Reports Checklist

The following table is based on the IIA Professional Practices Framework.

Background	✓ Identifies the organisational units and activities reviewed and provides explanatory information. ✓ Indicates why the audit project was conducted, including whether the report covers a scheduled engagement or is responding to a request. ✓ Includes the status of observations, conclusions and recommendations from prior audits.
Objectives	✓ Statements that define intended engagement accomplishments.
Scope	✓ Identifies the audited activities. ✓ Identifies the time period reviewed. ✓ Identifies related activities that are not reviewed.
Approach	✓ Establishes the procedures for identifying, analysing, and evaluating sufficient information to achieve the engagement's objectives.
Observations / Findings	✓ Identifies the standards, measures, or expectations used in making an evaluation and / or verification (criteria). ✓ Identifies the factual evidence that the internal auditor found during the examination that supports the conclusions and recommendations (conditions). ✓ Identifies the reason for the difference between the expected and actual conditions (causes).

	✓ Identifies the risk or exposure the organisation and / or others encounter because the condition is not consistent with the criteria (effect).
Conclusions	✓ Should be clearly identified. ✓ Should be based on appropriate analyses and evaluations. ✓ Should encompass the entire scope of an engagement. ✓ Should relate directly to objectives.
Recommendations	✓ Should be based on engagement observations and conclusion. ✓ Should either be general or specific and call for action to correct existing conditions or improve operations. ✓ Should suggest approaches to correct or enhance performance.
Agreed actions	✓ An agreed set of actions proposed by management to address any recommendations. (In some cases the internal audit teams may move straight to agreeing actions and skip recommendations. This is considered good practice.)

3.8. Follow-Up on Audit Reports

The General Manager and audit committee should systematically review progress against audit recommendations and agreed action plans. This ensures that a clear message is sent to management and staff that these matters are important and are being reviewed at the most senior levels in the organisation.

If management accepts a risk that internal audit believes is unacceptable, then this should normally be discussed at an appropriate level in the organisation, including with the General Manager and the audit committee, as considered appropriate.

3.9. Access to Audit Reports

Internal audit reports are intended for internal use only. Where audit reports have findings that are useful to other areas of council, internal audit may share this information on a limited basis. Internal audit reports should be shared with the council's external auditor to assist them in the course of their work. This permission should be documented in the audit committee charter.

Councillors should also have access to the minutes of the Audit Committee. As the minutes may contain confidential information, broader public access should be controlled. However the council should be mindful of its obligations under the *Government Information (Public Access) Act 2009* to provide greater transparency and accountability.

3.10. Annual report from the Audit Committee to Council

The audit committee should report regularly to the council on the management of risk and internal controls. This may be done following each meeting of the audit committee, but as a minimum, the audit committee should report at least annually to the full council on its oversight role of the internal audit function. The General Manager should also provide an annual report to the audit committee on the performance of the internal audit function.

Council may request the Chairperson of the Audit Committee to address the Council to answer any enquiries about the operation of the Audit Committee.

3.11. Performance Measurement

Internal audit should have performance measures that are based on its specific goals / objectives and performance targets that are derived from the internal audit group's plans / strategies. Quality assurance and review of audit work papers in accordance with Australian Auditing Standards is also an essential requirement to ensure the audit findings are adequately evidenced and documented. The work of internal audit can be used by the external auditors where they are satisfied of its quality as per the Australian Auditing Standards AA610.

Performance Measurement System Checklist

Performance measures should provide information that enables the internal audit function to determine whether its activities are achieving its charter and planned results (ie, the aims expressed in its various types of plans).

The performance measurement system should be documented and should be clear on:

- Performance data that is to be collected
- The frequency of data collection
- Who is responsible for data collection
- Data quality control
- Who generates performance data reports
- Who receives such reports.

Performance measures may cover aspects such as:

- Stakeholder satisfaction
- Internal audit processes (eg, risk assessment / audit planning, performing the audits, reporting, and value added)
- Innovation and capabilities (training, technology, knowledge of business)
- Control deficiencies identified and resolved by management
- Cost/benefit analysis of internal audit recommendations.

An internal audit function should regularly report to the General Manager and the audit committee on its progress against the annual internal audit plan.

3.12. Independent Quality Review of Internal Audit

Internal audit should be subject to an external quality assessment of its performance using accepted standards for performance measurement and evaluation at least every five years.

This is to provide assurance to the General Manager and council that internal audit is effective and operating in accordance with the International Standards for the Professional Practice of Internal Auditing.

The Institute of Internal Auditors provides a quality assessment framework for this purpose.

3.13. Internal Audit and Protected Disclosures

Where there is otherwise no designated protected disclosures coordinator for the council, the internal auditor can be appointed to fulfil the requirements of the *Protected Disclosures Act 1994* and the provisions of council's internal reporting policy. Alternatively, the General Manager can appoint the internal auditor to conduct an independent investigation of matters arising from a protected disclosure.

Protected disclosures are an important means by which councils can signal commitment to ethical practice. They also can act as an early warning system for management and to assist staff in making any disclosures of alleged corrupt conduct, maladministration or serious and substantial waste of public money under the *Protected Disclosures Act 1994*.

Every public official has a statutory right to make a disclosure under the Protected Disclosure Act to the following external agencies:

- NSW Ombudsman
- Independent Commission Against Corruption (ICAC)
- Audit Office
- Police Integrity Commission or
- Division of Local Government, Department of Premier and Cabinet (about serious and substantial waste in local government).

Councils should inform their councillors, staff and council delegates of the requirements and protections of the *Protected Disclosures Act 1994* through staff and councillor induction and training programs.

4. Establishing an Audit Committee

4.1. What is an Audit Committee?

An audit committee pays a pivotal role in the governance framework to provide council with independent oversight and monitoring of the council's audit processes, including the council's internal control activities. This oversight includes internal and external reporting, risk management activities, internal and external audit and compliance.[5]. A strong relationship between the audit committee and the internal audit function enables the committee to meet its responsibilities and carry out its functions. An audit committee establishes the importance and executive direction for an internal audit function, and ensures that the council achieves maximum value from the internal audit function. The audit committee sets the appropriate tone at the top. Guidelines for establishment and operations of audit committees in local government are set out below.

No two audit committees will function in exactly the same way, nor should they. A dynamic audit committee process is required for each council to cater for the particular internal and external influences impacting upon them. The size and conduct of council audit committees will also vary depending on a council's size and other circumstances.

Key characteristics of good practice audit committees are:

- A thorough understanding of the audit committee's position in the legal and governance framework
- Clearly defined roles and responsibilities
- Members with relevant personal qualities, skills and experience, including at least one member with a strong financial and/or audit background
- The ability to maintain effective relationships with key stakeholders
- The ability and capacity to conduct its affairs efficiently and effectively
- A robust and considered process of assessment and continuous improvement.

4.2. Independence and Objectivity

The audit committee will achieve its independence by having a majority of independent members external to council and its operations. In addition, it is highly desirable that all members chosen exhibit an independence of mind in their deliberations and do not act as a representative of a particular area of council, or with conflicts of interests. Regular rotation of some or all members is also desirable to keep a fresh approach.

Ideally the audit committee should consist of at least three and preferably no more than five members comprised of independent external members, who should be in the majority, and councillors other than the Mayor (or an Administrator). Staff should not be members of the audit committee.

When selecting committee members it is important to ensure that they have appropriate qualifications and experience to fulfil their role. The following qualities are desirable when appointing members:

Individuals should have:

- Knowledge of local government
- Strong communication skills

[5] Auditing and Assurance Standards Board, Australian Institute of Company Directors, Institute of Internal Auditors, Audit committees, A Guide to Good Practice 2008

- High levels of personal integrity and ethics
- Sufficient time available to devote to their responsibilities as a committee member
- High levels of financial literacy and, if possible accounting; financial; legal compliance and/or risk management experience or qualifications.

The audit committee as a whole should have:

- At least one member with financial qualifications and experience
- Skills and experience relevant to discharging its responsibilities, including experience in business, financial and legal compliance, risk management

Selection and Appointment of Committee Members

Committee members and the audit committee chair should be appointed by the council. This could be done on the recommendation of a committee which has been convened by council with the power to interview and recommend suitable candidates. It is important that the process used is transparent and accountable.

If the council wishes to use this process then the committee should prepare a written report for the council that provides details of the qualifications and experience of all eligible applicants for the position(s) of independent audit committee member(s) or audit committee chair from which the council can select the most suitable appointees.

Sufficient funds need to be allocated to the audit committee for it to operate effectively. Council should resolve to provide a budget and funds for the audit committee, this should include fees payable to the audit committee members.

Independent and councillor members

Independent and councillor members must be free from any management, business or other relationships that could be perceived to interfere with their ability to act in the best interests of the council.

When considering whether an individual has the necessary independence from council it is common to examine the individual's past and current relationships with the council. Some of the following are relationships that might affect the independent status of an independent and/or councillor:

- Is a substantial shareholder; an owner, officer or employee of a company; or a consultant, that is a material provider of professional advice, or goods, or services to the council;
- Is employed by or has previously been employed by a council and there has not been a period of at least two years between ceasing such employment;

To maximise both the real and perceived independence of the committee individuals currently employed by a council cannot be considered as an independent member of a council audit committee.

This list is not exhaustive and if one or more of the above examples is exhibited by an independent or councillor it is possible that their status as an "independent" member of the committee might be compromised.

Members and potential members of an audit committee need to ensure that they disclose to the council any relationships that could be viewed by other parties as creating conflicts of interests that impair either the individual's or the audit committee's actual or perceived independence.

In order to maximise the effectiveness of the audit committee it is important for members to be both independent and to be seen to be independent.

Audit committee chair

The chair of the audit committee is critical to the overall effectiveness of the committee. The chair of the committee should be independent and should not be the mayor or a member of council. The council should select an audit committee chair who:

- Is knowledgeable of the duties and responsibilities of the position as outlined in the audit committee charter; especially about local government, financial reporting and auditing requirements;
- Has the requisite local government, financial and leadership skills;
- Has the ability to build good relationships; and
- Has strong communication skills

The term of appointment of the chair should be specified by the council.

4.3. Structure and Membership

The structure and membership of an audit committee in the NSW local government environment will depend on the size of the council. Membership should have a majority of independent members and councillors (excluding the Mayor), with between 3 and 5 members. Good practice in governance is that council staff should not to be members of the committee. However, this may not be practical for some councils. The chair should be an independent member. A suggested membership is:

- 1 or 2 councillors (excluding the mayor)
- 2 or 3 independent members, at least one with financial expertise and one of whom should be the chair.

The internal auditor and Chief Financial Officer should be invited to attend all meetings. The external auditor should also be invited to attend as an independent advisor.

To preserve the independence of the Audit Committee the General Manager should not be a voting member of the Audit Committee. In accordance with section 376(2) of the Local Government Act the General Manager is entitled to attend meetings of the Audit Committee. Furthermore pursuant to Section 376(3) of the Local Government Act the General Manager may only be excluded from the meeting while the committee deals with a matter relating to the standard of performance of the General Manager or the terms of the employment of the General Manager. However, the General Manager is not automatically entitled to be, nor should the General Manager be, a member of the audit committee.

General Managers are strongly encouraged to enable the audit committee to conduct its activities without undue influence from the General Manager.

It is recommended that, even though, pursuant to the Local Government Act, the General Manager is entitled to attend all meetings, in line with better practice, the General Manager should allow the audit committee to meet separately with each of the internal auditor and the external auditor without the presence of management on at least one occasion per year.

A suggested structure for smaller councils is as follows:

- 1 councillor (excluding the Mayor)
- 2 independents – at least one with financial expertise

A structure for bigger councils could be:

- 1 or 2 councillors (excluding the Mayor)
- 2 or 3 independents – at least one with financial expertise and/or one with financial, legal or business expertise

The audit committee should also have its own charter that sets out the roles and responsibilities of the audit committee and its oversight of the internal and external audit functions, including any statutory duties. The elected council should approve the audit committee charter.

An example charter for audit committees is included in Appendix 2. Councils should not use this example verbatim but should tailor it according to their specific circumstances.

4.4. Audit Committee Operations

4.4.1. Meetings

The audit committee should meet with sufficient frequency to meet its responsibilities.

The number of meetings and their duration will vary depending on the range and complexity of the council and the committee's responsibilities. The audit committee should decide the number of meetings needed for the year after taking into consideration:

- The roles and responsibilities of the committee
- Maturity of the committee and audit arrangements
- The level and/or volume of internal and external audit activity
- Key reporting deadlines
- Significant developments or emerging risks for the entity, for example, restructuring, policy initiatives or new programs
- The potential resource implications versus the benefit to the committee and the entity of more frequent meetings.

Generally, the audit committee should meet at least four times a year. It is also appropriate to have meetings dedicated to considering the annual external audit plan, external management letters and council's audited annual financial reports. Where significant issues arise during the year, committees should consider the need to schedule additional meetings.

Where possible, the dates for audit committee meetings should be established 12 months in advance, particularly where the committee has independent members with other commitments. Each year the committee should agree a forward meeting plan, including meeting dates, location and agenda items. When developing the forward meeting plan, the committee should ensure it covers all the responsibilities outlined in its charter.

The audit committee charter should require the chair of the committee to hold a meeting if asked to do so by another committee member or by the council or the General Manager. There should also be provision for both the internal and external auditors to meet privately with the chair of the audit committee if required, and this should be documented in the audit committee charter.

4.4.2. Functions

Clear roles and responsibilities should be given to an audit committee, and documented in the audit committee charter (see Appendix 2 for a model charter). The broad responsibilities for best practice include the following:

- Risk management
- The control framework
- External accountability (including the council's annual audited financial reports)
- Legislative compliance
- Internal audit

- External audit
- Approving the internal audit charter that will guide the activities of an internal audit group
- Having input into and approving an internal audit's long-term strategic plan and annual audit plan
- Having input into the appointment and remuneration of the internal auditor
- Making enquiries of management and the internal audit to determine if there are scope or budgetary limitations that impede an internal auditor's ability to function properly
- Approving the scope of an external assessment or equivalent internal assessment of internal audit to be undertaken every 5 years; and internal assessments which can be undertaken in intervening years if desired.

An audit committee, as a crucial component of corporate governance, is fundamental to assisting the General Manager and council with their oversight function to:

- Ensure all key controls are operating effectively
- Ensure all key controls are appropriate for achieving corporate goals and objectives
- Meet their statutory and fiduciary duties
- Provide a forum for discussing problems and issues that may affect the operations of the internal audit group and acting as a forum for discussion
- Provide a forum for discussion to identify areas worthy of examination by an internal audit group
- Review the implementation of the annual audit plan and implementation of audit recommendations.

4.4.3. Conflict of Interests

Councillors, council staff and members of council committees must comply with the applicable provisions of council's code of conduct in carrying out their functions as council officials. It is the personal responsibility of council officials to comply with the standards in the council's code of conduct and regularly review their personal circumstances with this in mind.

There will in all likelihood be times where matters to be considered by the Committee raise a conflict of interests for a member of the committee. To preserve the integrity and independence of the Audit Committee it is of utmost important that any conflict of interests is appropriately managed.

This can be done by Committee members declaring any conflict of interests at the start of each meeting or before discussion of a relevant agenda item or topic. Details of any conflict of interests should be appropriately minuted.

Where members or invitees at Committee meetings are deemed to have a real or perceived conflict of interests, it may be appropriate they be excused from Committee deliberations on the issue where the conflict of interests may exist. The final arbiter of such a decision is the Chair of the Committee.

5. Enterprise Risk Management

5.1. What is Risk Management

Internal audit is not responsible for designing or implementing risk management in councils, but is required to consider the risk management framework in planning and conducting audits.

Risk management is an essential part of effective corporate governance. It is defined as "the culture, processes and structures that are directed towards realising potential opportunities whilst managing adverse effects."[6] Enterprise Risk Management is the holistic management of all risks within council, not just insurable risks or occupational health and safety.

The concept of risk has two elements, the likelihood of something happening and the consequences if it happens. It is recommended that councils refer to the International Standard "*Risk Management – Principles and Guidelines*" ISO 31000:2009(E) for detailed guidance on risk management.

Risk can arise from internal or external sources, and might include exposure to such things as economic or financial loss or gain, physical damage, failure of a project to reach its objectives, ratepayer dissatisfaction, unfavourable publicity, a threat to physical safety or breach of security, mismanagement, failure of equipment, corruption and fraud. Risks should not necessarily be avoided. If managed effectively, they allow us to seize opportunities for improving services and business practices.

Risks can be categorised according to the goals, objectives or outcomes in the council's strategic, management or business plans. At the highest level, these represent risks to the council's ability to implement policy and deliver outcomes to the community. Risks also can be categorised into:

- Strategic risks (risks to the council's direction, external environment and to the achievement of its plans)
- Commercial risks (risks of commercial relationships, such as failed contractual relationships)
- Operational risks (risks to core business activities, such as inadequate human resources, disasters or threats to physical safety)
- Technical risks (risks of managing assets, such as equipment failure or structure collapse)
- Financial and systems risks (risks with financial controls and systems, such as fraud)
- Compliance risks (risks to meeting regulatory obligations).

Risk management is a logical and systematic process that can be used when making decisions and in managing performance. It is a means to an end and should be integrated into everyday work. Good risk management is forward-looking and helps to improve business decisions. It is not just about avoiding or minimising losses, but also about dealing positively with opportunities. It is a powerful tool for local government managers.

Good risk management is based on a well-planned, logical, comprehensive and documented strategy. This strategy provides general policy guidance, and plans and procedures that can be used as part of the organisation's everyday work to manage risk.

Good risk management must be based on a strategy, but a strategy itself doesn't manage risks. Leadership, effort by all levels of management and staff, and careful monitoring by councillors and risk committees, are needed to make the strategy a success.

[6] "*Risk Management – Principles and Guidelines*" ISO 31000:2009(E)

Focus should be on embedding a risk management philosophy into organisational decision making and providing tools to enable this process. Where major risks are identified then managerial effort should be directed to managing those risks. Overly complex approaches to risk management will divert resources from the main objective of better management performance, and hence a common sense approach is encouraged.

5.2. Why Implement Risk Management?

Increasingly, risk management is a mainstream activity embedded into good management in both the private and public sectors. Through better understanding of risks, and their likelihood and consequences, councils and their staff will be better prepared to anticipate these risks and take appropriate action.

By utilising risk management principles, councils are able to maximise the likelihood of successfully achieving their goals through proactive treatment of risks resulting in the following outcomes:

- Higher level of service delivery
- Efficient and effective allocation of resources
- Improved responsiveness and flexibility
- Increased accountability and transparency
- Reduced stress to council staff and management.

It is also hoped that effective risk management will result in fewer surprises and unanticipated negative events.

5.3. Risk Management in New South Wales Local Government

The *Local Government Act 1993* was enacted in an era before enterprise risk management was a widely accepted element of good governance. The Act nevertheless requires councils, among other things, to:

> *"provide directly or on behalf of other levels of government, after due consultation, adequate, equitable and appropriate services and facilities for the community* ***and to ensure that those services and facilities are managed efficiently and effectively".***[7]

The Act also requires Councillors:

> **"to review the performance of the council and its delivery of services**, and the management plans and revenue policies of the council"[8]

and that the General Manager:

> *"is generally responsible for the* ***efficient and effective operation*** *of the council's organisation and for ensuring the implementation, without undue delay, of decisions of the council".*[9]

While there is currently no specific reference to risk management in the Act, it is implicit in each of the above broader requirements for efficiency, effectiveness and oversight.

The Division of Local Government's Promoting Better Practice Program reviews have frequently made recommendations to actively encourage councils to undertake a comprehensive risk management plan across all functions of council to proactively identify and manage risk exposures.

[7] Local Government Act 1993 – Section 8
[8] Local government Act 1903 Section 232(1)
[9] Local government Act 1903 Section 335(1)

One of the key roles of the internal auditor is to provide advice and assurance over the risk management and internal control frameworks. To maintain independence, internal audit will not normally be responsible for the implementation of risk management or making decisions on how risks should be treated.

5.4. Risks Inherent Within Local Government

While each council will have different sizes and complexities in its structure and operations, and these in turn will generate different risks, there are a number of risks that will be common to the sector and be applicable in some form to most councils.

As a first step, councils may wish to identify material risks to the achievement of the council's goals, objectives and desired outcomes of the council's strategic, management and/or business plans. At the highest level, these represent risks to the council's ability to implement policy and deliver outcomes to the community.

A number of common risks for local government are set out in Appendix 5, which may assist in this process.

5.5. Whole-Of-Government Risk Management

Councils often face risks that significantly influence other risks (such as inadequate staff skills or low morale that influence productivity). These links between risks are important - a risk may not look significant in isolation, but is significant when its flow-on effect is considered.

As whole-of-government approaches become more common, state-sector risks – risks that affect the state as a whole – are becoming better understood and therefore can be better managed.

Councils will increasingly need to understand state-sector risks, and to pay greater attention to identifying and working with other layers of government to manage them. There are 3 types of state-sector risk, each of which calls for a different response:

- Council-level risks (such as the risks above). These can become risks to the State because of their size and significance, because of the wider impact of measures to manage them, or because of poor management by councils.
- Inter-agency risks, which if unmitigated by one agency, become risks for other agencies (such as the link between meeting the educational and social needs of teenagers and anti-social behaviour).
- State-wide risks, which are beyond the boundaries of any one council and call for a response across councils coordinated by a central council (such as bushfires, floods and other emergencies).

There is no such thing as a risk-free environment, but many risks can be avoided, modified or shared through good risk management. Similarly it is not desirable to attempt to create a risk-free environment and not all risks should be reduced. It may be appropriate in some circumstances to retain the risk, or even look at increasing the level of risk taken.

Risk management is an effective tool to identify, evaluate and manage both risks and opportunities at all levels of the organisation. Good risk management also takes advantage of opportunities while analysing and dealing with risks.

Risks should not necessarily be avoided. If managed effectively, they allow councils to seize opportunities for improving services and business practices and avoiding unexpected negative impacts.

5.6. Other Guidance

Risk management is a common sense, yet highly evolved discipline. This guide aims to provide grounding on some of the key principles and practices councils should embrace. For those seeking a deeper understanding of risk management principles and practice, the Division recommends:

- International Standard ISO 31000:2009(E) risk management – Principles and guidelines
- ISO Guide 73:2009 Risk Management – Vocabulary
- IS/IEC 31010 Risk Management – Risk Assessment Techniques

These important publications provide detailed and authoritative guidance about risk management practices. They constitute a step-by-step guide for councils wanting to develop and implement risk management frameworks.

Although not all organisations use this approach, public sector risk management continues to expand beyond a financial focus to encompass all parts of an organisation's business and services. The Commonwealth Government based its *Guidelines for Managing Risk in the Australian Public Service* on this standard. See www.apsc.gov.au/mac/index.htm.

The Australian National Audit Office describes the key components of effective risk management, as well as the importance of developing a risk management culture, in its better practice guide, *Public Sector Governance Volume 1*6. See www.anao.gov.au.

CPA Australia has a number of publications relating to public sector risk management. They include *Case Studies in Public Sector Risk Management: Better Practice Guide; Enterprise-wide Risk Management: Better Practice Guide; Public Sector Risk Management: A State of Play;* and *Research Report on Public Sector Risk Management.* See www.cpaaustralia.com.au/20_cpastore.

Appendix 1 - Summary of Internal Audit Standards and Professional Practices Framework

The Institute of Internal Auditors

International Standards for the Professional Practice of Internal Auditing

Reprinted with permission of the Institute of Internal Auditors, Australia. Note that these standards are under continuous development and hence while correct at the time of publication, readers should obtain the latest version of the standards from IIA Australia.

The purpose of the *Standards* is to:

1. Delineate basic principles that represent the practice of internal auditing, as it should be.
2. Provide a framework for performing and promoting a broad range of value-added internal audit activities.
3. Establish the basis for the evaluation of internal audit performance.
4. Foster improved organisational processes and operations.

The structure of the Standards is divided between Attribute and Performance Standards. Attribute Standards address the attributes of organisations and individuals performing internal auditing. The Performance Standards describe the nature of internal auditing and provide quality criteria against which the performance of these services can be measured. The Attribute and Performance Standards are also provided to apply to all internal audit services.

Implementation Standards are also provided to expand upon the Attribute and Performance standards, by providing the requirements applicable to assurance (A) or consulting (C) activities.

The Standards are part of the International Professional Practices Framework (IPPF). The IPPF includes the Definition of Internal Auditing, the Code of Ethics, the Standards, and other guidance. Guidance regarding how the Standards might be applied is included in Practice Advisories that are issued by the Professional Issues Committee.

Attribute Standards

Attribute Standards

1000 – Purpose, Authority, and Responsibility
The purpose, authority, and responsibility of the internal audit activity must be formally defined in an internal audit charter, consistent with the Definition of Internal Auditing, the Code of Ethics, and the *Standards*. The chief audit executive must periodically review the internal audit charter and present it to senior management and the board for approval.

Interpretation:
The internal audit charter is a formal document that defines the internal audit activity's purpose, authority, and responsibility. The internal audit charter establishes the internal audit activity's position within the organisation; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities. Final approval of the internal audit charter resides with the board.

> **1000.A1 –** The nature of assurance services provided to the organisation must be defined in the internal audit charter. If assurances are to be provided to parties outside the organisation, the nature of these assurances must also be defined in the internal audit charter.
>
> **1000.C1 –** The nature of consulting services must be defined in the internal audit charter.

1010 – Recognition of the Definition of Internal Auditing, the Code of Ethics, and the Standards in the Internal Audit Charter
The mandatory nature of the Definition of Internal Auditing, the Code of Ethics, and the *Standards* must be recognized in the internal audit charter. The chief audit executive should discuss the Definition of Internal Auditing, the Code of Ethics, and the *Standards* with senior management and the board.

1100 – Independence and Objectivity
The internal audit activity must be independent, and internal auditors must be objective in performing their work.

Interpretation:
Independence is the freedom from conditions that threaten the ability of the internal audit activity or the chief audit executive to carry out internal audit responsibilities in an unbiased manner. To achieve the degree of independence necessary to effectively carry out the responsibilities of the internal audit activity, the chief audit executive has direct and unrestricted access to senior management and the board. This can be achieved through a dual-reporting relationship. Threats to independence must be managed at the individual auditor, engagement, functional, and organisational levels.

Objectivity is an unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others. Threats to objectivity must be managed at the individual auditor, engagement, functional, and organisational levels.

1110 – Organisational Independence
The chief audit executive must report to a level within the organisation that allows the internal audit activity to fulfil its responsibilities. The chief audit executive must confirm to the board, at least annually, the organisational independence of the internal audit activity.

> **1110.A1 –** The internal audit activity must be free from interference in determining the scope of internal auditing, performing work, and communicating results.

1111 – Direct Interaction with the Board
The chief audit executive must communicate and interact directly with the board.

1120 – Individual Objectivity
Internal auditors must have an impartial, unbiased attitude and avoid any conflict of interest.

Interpretation:
Conflict of interest is a situation in which an internal auditor, who is in a position of trust, has a competing professional or personal interest. Such competing interests can make it difficult to fulfil his or her duties impartially. A conflict of interest exists even if no unethical or improper act results. A conflict of interest can create an appearance of impropriety that can undermine confidence in the internal auditor, the internal audit activity, and the profession. A conflict of interest could impair an individual's ability to perform his or her duties and responsibilities objectively.

1130 – Impairment to Independence or Objectivity
If independence or objectivity is impaired in fact or appearance, the details of the impairment must be disclosed to appropriate parties. The nature of the disclosure will depend upon the impairment.

Interpretation:
Impairment to organisational independence and individual objectivity may include, but is not limited to, personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations, such as funding.

The determination of appropriate parties to which the details of an impairment to independence or objectivity must be disclosed is dependent upon the expectations of the internal audit activity's and the chief audit executive's responsibilities to senior management and the board as described in the internal audit charter, as well as the nature of the impairment.

> **1130.A1 –** Internal auditors must refrain from assessing specific operations for which they were previously responsible. Objectivity is presumed to be impaired if an internal auditor provides assurance services for an activity for which the internal auditor had responsibility within the previous year.
>
> **1130.A2 –** Assurance engagements for functions over which the chief audit executive has responsibility must be overseen by a party outside the internal audit activity.
>
> **1130.C1 –** Internal auditors may provide consulting services relating to operations for which they had previous responsibilities.
>
> **1130.C2 –** If internal auditors have potential impairments to independence or objectivity relating to proposed consulting services, disclosure must be made to the engagement client prior to accepting the engagement.

1200 – Proficiency and Due Professional Care
Engagements must be performed with proficiency and due professional care.

1210 – Proficiency
Internal auditors must possess the knowledge, skills, and other competencies needed to perform their individual responsibilities. The internal audit activity collectively must possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities.

Interpretation:
Knowledge, skills, and other competencies is a collective term that refers to the professional proficiency required of internal auditors to effectively carry out their professional responsibilities. Internal auditors are encouraged to demonstrate their proficiency by obtaining appropriate professional certifications and qualifications, such as the Certified Internal Auditor designation and other designations offered by The Institute of Internal Auditors and other appropriate professional organisations.

1210.A1 – The chief audit executive must obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

1210.A2 – Internal auditors must have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organisation, but are not expected to have the expertise of a person whose primary responsibility is detecting and investigating fraud.

1210.A3 – Internal auditors must have sufficient knowledge of key information technology risks and controls and available technology-based audit techniques to perform their assigned work. However, not all internal auditors are expected to have the expertise of an internal auditor whose primary responsibility is information technology auditing.

1210.C1 – The chief audit executive must decline the consulting engagement or obtain competent advice and assistance if the internal auditors lack the knowledge, skills, or other competencies needed to perform all or part of the engagement.

1220 – Due Professional Care
Internal auditors must apply the care and skill expected of a reasonably prudent and competent internal auditor. Due professional care does not imply infallibility.

1220.A1 – Internal auditors must exercise due professional care by considering the:

- Extent of work needed to achieve the engagement's objectives;
- Relative complexity, materiality, or significance of matters to which assurance procedures are applied;
- Adequacy and effectiveness of governance, risk management, and control processes;
- Probability of significant errors, fraud, or noncompliance; and
- Cost of assurance in relation to potential benefits.

1220.A2 – In exercising due professional care internal auditors must consider the use of technology-based audit and other data analysis techniques**.**

1220.A3 – Internal auditors must be alert to the significant risks that might affect objectives, operations, or resources. However, assurance procedures alone, even when performed with due professional care, do not guarantee that all significant risks will be identified.

1220.C1 – Internal auditors must exercise due professional care during a consulting engagement by considering the:

- Needs and expectations of clients, including the nature, timing, and communication of engagement results;
- Relative complexity and extent of work needed to achieve the engagement's objectives; and
- Cost of the consulting engagement in relation to potential benefits.

1230 – Continuing Professional Development
Internal auditors must enhance their knowledge, skills, and other competencies through continuing professional development.

1300 – Quality Assurance and Improvement Program
The chief audit executive must develop and maintain a quality assurance and improvement program that covers all aspects of the internal audit activity.

Interpretation:
A quality assurance and improvement program is designed to enable an evaluation of the internal audit activity's conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.

1310 – Requirements of the Quality Assurance and Improvement Program
The quality assurance and improvement program must include both internal and external assessments.

1311 – Internal Assessments
Internal assessments must include:

- Ongoing monitoring of the performance of the internal audit activity; and
- Periodic reviews performed through self-assessment or by other persons within the organisation with sufficient knowledge of internal audit practices.

Interpretation:
Ongoing monitoring is an integral part of the day-to-day supervision, review, and measurement of the internal audit activity. Ongoing monitoring is incorporated into the routine policies and practices used to manage the internal audit activity and uses processes, tools, and information considered necessary to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards.

Periodic reviews are assessments conducted to evaluate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards.

Sufficient knowledge of internal audit practices requires at least an understanding of all elements of the International Professional Practices Framework.

1312 – External Assessments
External assessments must be conducted at least once every five years by a qualified, independent reviewer or review team from outside the organisation. The chief audit executive must discuss with the board:

- The need for more frequent external assessments; and
- The qualifications and independence of the external reviewer or review team, including any potential conflict of interest.

Interpretation:
A qualified reviewer or review team consists of individuals who are competent in the professional practice of internal auditing and the external assessment process. The evaluation of the competency of the reviewer and review team is a judgment that considers the professional internal audit experience and professional credentials of the individuals selected to perform the review. The evaluation of qualifications also considers the size and complexity of the organisations that the reviewers have been associated with in relation to the organisation for which the internal audit activity is being assessed, as well as the need for particular sector, industry, or technical knowledge.

An independent reviewer or review team means not having either a real or an apparent conflict of interest and not being a part of, or under the control of, the organisation to which the internal audit activity belongs.

1320 – Reporting on the Quality Assurance and Improvement Program
The chief audit executive must communicate the results of the quality assurance and improvement program to senior management and the board.

Interpretation:
The form, content, and frequency of communicating the results of the quality assurance and improvement program is established through discussions with senior management and the board and considers the responsibilities of the internal audit activity and chief audit executive as contained in the internal audit charter. To demonstrate conformance with the Definition of Internal Auditing, the Code of Ethics, and the Standards, *the results of external and periodic internal assessments are communicated upon completion of such assessments and the results of ongoing monitoring are communicated at least annually. The results include the reviewer's or review team's assessment with respect to the degree of conformance.*

1321 – Use of "Conforms with the *International Standards for the Professional Practice of Internal Auditing*"
The chief audit executive may state that the internal audit activity conforms with the *International Standards for the Professional Practice of Internal Auditing* only if the results of the quality assurance and improvement program support this statement.

1322 – Disclosure of Nonconformance
When nonconformance with the Definition of Internal Auditing, the Code of Ethics, or the *Standards* impacts the overall scope or operation of the internal audit activity, the chief audit executive must disclose the nonconformance and the impact to senior management and the board.

Performance Standards

2000 – Managing the Internal Audit Activity
The chief audit executive must effectively manage the internal audit activity to ensure it adds value to the organisation.

Interpretation:
The internal audit activity is effectively managed when:

- *The results of the internal audit activity's work achieve the purpose and responsibility included in the internal audit charter;*
- *The internal audit activity conforms with the Definition of Internal Auditing and the Standards; and*
- *The individuals who are part of the internal audit activity demonstrate conformance with the Code of Ethics and the Standards.*

2010 – Planning
The chief audit executive must establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organisation's goals.

Interpretation:
The chief audit executive is responsible for developing a risk-based plan. The chief audit executive takes into account the organisation's risk management framework, including using risk appetite levels set by management for the different activities or parts of the organisation. If a framework does not exist, the chief audit executive uses his/her own judgment of risks after consultation with senior management and the board.

> **2010.A1 –** The internal audit activity's plan of engagements must be based on a documented risk assessment, undertaken at least annually. The input of senior management and the board must be considered in this process.
>
> **2010.C1 –** The chief audit executive should consider accepting proposed consulting engagements based on the engagement's potential to improve management of risks, add value, and improve the organisation's operations. Accepted engagements must be included in the plan.

2020 – Communication and Approval
The chief audit executive must communicate the internal audit activity's plans and resource requirements, including significant interim changes, to senior management and the board for review and approval. The chief audit executive must also communicate the impact of resource limitations.

2030 – Resource Management
The chief audit executive must ensure that internal audit resources are appropriate, sufficient, and effectively deployed to achieve the approved plan.

Interpretation:
Appropriate refers to the mix of knowledge, skills, and other competencies needed to perform the plan. Sufficient refers to the quantity of resources needed to accomplish the plan. Resources are effectively deployed when they are used in a way that optimizes the achievement of the approved plan.

2040 – Policies and Procedures
The chief audit executive must establish policies and procedures to guide the internal audit activity.

Interpretation:
The form and content of policies and procedures are dependent upon the size and structure of the internal audit activity and the complexity of its work.

2050 – Coordination
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 minimize duplication of efforts.

2060 – Reporting to Senior Management and the Board
The chief audit executive must report periodically to senior management and the board on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the board.

Interpretation:
The frequency and content of reporting are determined in discussion with senior management and the board and depend on the importance of the information to be communicated and the urgency of the related actions to be taken by senior management or the board.

2100 – Nature of Work
The internal audit activity must evaluate and contribute to the improvement of governance, risk management, and control processes using a systematic and disciplined approach.

2110 – Governance
The internal audit activity must assess and make appropriate recommendations for improving the governance process in its accomplishment of the following objectives:

- Promoting appropriate ethics and values within the organisation;
- Ensuring effective organisational performance management and accountability;
- Communicating risk and control information to appropriate areas of the organisation; and
- Coordinating the activities of and communicating information among the board, external and internal auditors, and management.

2110.A1 – The internal audit activity must evaluate the design, implementation, and effectiveness of the organisation's ethics-related objectives, programs, and activities.

2110.A2 – The internal audit activity must assess whether the information technology governance of the organisation sustains and supports the organisation's strategies and objectives.

2110.C1 – Consulting engagement objectives must be consistent with the overall values and goals of the organisation.

2120 – Risk Management
The internal audit activity must evaluate the effectiveness and contribute to the improvement of risk management processes.

Interpretation:
Determining whether risk management processes are effective is a judgment resulting from the internal auditor's assessment that:

- *Organisational objectives support and align with the organisation's mission;*
- *Significant risks are identified and assessed;*
- *Appropriate risk responses are selected that align risks with the organisation's risk appetite; and*
- *Relevant risk information is captured and communicated in a timely manner across the organisation, enabling staff, management, and the board to carry out their responsibilities.*

Risk management processes are monitored through ongoing management activities, separate evaluations, or both.

2120.A1 – The internal audit activity must evaluate risk exposures relating to the organisation's governance, operations, and information systems regarding the:

- Reliability and integrity of financial and operational information.
- Effectiveness and efficiency of operations.
- Safeguarding of assets; and
- Compliance with laws, regulations, and contracts.

2120.A2 – The internal audit activity must evaluate the potential for the occurrence of fraud and how the organisation manages fraud risk.

2120.C1 – During consulting engagements, internal auditors must address risk consistent with the engagement's objectives and be alert to the existence of other significant risks.

2120.C2 – Internal auditors must incorporate knowledge of risks gained from consulting engagements into their evaluation of the organisation's risk management processes.

2120.C3 – When assisting management in establishing or improving risk management processes, internal auditors must refrain from assuming any management responsibility by actually managing risks.

2130 – Control
The internal audit activity must assist the organisation in maintaining effective controls by evaluating their effectiveness and efficiency and by promoting continuous improvement.

2130.A1 – The internal audit activity must evaluate the adequacy and effectiveness of controls in responding to risks within the organisation's governance, operations, and information systems regarding the:

- Reliability and integrity of financial and operational information;
- Effectiveness and efficiency of operations;
- Safeguarding of assets; and
- Compliance with laws, regulations, and contracts.

2130.A2 – Internal auditors should ascertain the extent to which operating and program goals and objectives have been established and conform to those of the organisation.

2130.A3 – Internal auditors should review operations and programs to ascertain the extent to which results are consistent with established goals and objectives to determine whether operations and programs are being implemented or performed as intended.

2130.C1 – During consulting engagements, internal auditors must address controls consistent with the engagement's objectives and be alert to significant control issues.

2130.C2 – Internal auditors must incorporate knowledge of controls gained from consulting engagements into evaluation of the organisation's control processes.

2200 – Engagement Planning
Internal auditors must develop and document a plan for each engagement, including the engagement's objectives, scope, timing, and resource allocations.

2201 – Planning Considerations
In planning the engagement, internal auditors must consider:

- The objectives of the activity being reviewed and the means by which the activity controls its performance;
- The significant risks to the activity, its objectives, resources, and operations and the means by which the potential impact of risk is kept to an acceptable level;
- The adequacy and effectiveness of the activity's risk management and control processes compared to a relevant control framework or model; and
- The opportunities for making significant improvements to the activity's risk management and control processes.

2201.A1 – When planning an engagement for parties outside the organisation, internal auditors must establish a written understanding with them about objectives, scope, respective responsibilities, and other expectations, including restrictions on distribution of the results of the engagement and access to engagement records.

2201.C1 – Internal auditors must establish an understanding with consulting engagement clients about objectives, scope, respective responsibilities, and other client expectations. For significant engagements, this understanding must be documented.

2210 – Engagement Objectives
Objectives must be established for each engagement.

2210.A1 – Internal auditors must conduct a preliminary assessment of the risks relevant to the activity under review. Engagement objectives must reflect the results of this assessment.

2210.A2 – Internal auditors must consider the probability of significant errors, fraud, noncompliance, and other exposures when developing the engagement objectives.

2210.A3 – Adequate criteria are needed to evaluate controls. Internal auditors must ascertain the extent to which management has established adequate criteria to determine whether objectives and goals have been accomplished. If adequate, internal auditors must use such criteria in their evaluation. If inadequate, internal auditors must work with management to develop appropriate evaluation criteria.

2210.C1 – Consulting engagement objectives must address governance, risk management, and control processes to the extent agreed upon with the client.

2220 – Engagement Scope
The established scope must be sufficient to satisfy the objectives of the engagement.

> **2220.A1 –** The scope of the engagement must include consideration of relevant systems, records, personnel, and physical properties, including those under the control of third parties.
>
> **2220.A2 –** If significant consulting opportunities arise during an assurance engagement, a specific written understanding as to the objectives, scope, respective responsibilities, and other expectations should be reached and the results of the consulting engagement communicated in accordance with consulting standards.
>
> **2220.C1 –** In performing consulting engagements, internal auditors must ensure that the scope of the engagement is sufficient to address the agreed-upon objectives. If internal auditors develop reservations about the scope during the engagement, these reservations must be discussed with the client to determine whether to continue with the engagement.

2230 – Engagement Resource Allocation
Internal auditors must determine appropriate and sufficient resources to achieve engagement objectives based on an evaluation of the nature and complexity of each engagement, time constraints, and available resources.

2240 – Engagement Work Program
Internal auditors must develop and document work programs that achieve the engagement objectives.

> **2240.A1 –** Work programs must include the procedures for identifying, analysing, evaluating, and documenting information during the engagement. The work program must be approved prior to its implementation, and any adjustments approved promptly.
>
> **2240.C1 –** Work programs for consulting engagements may vary in form and content depending upon the nature of the engagement.

2300 – Performing the Engagement
Internal auditors must identify, analyse, evaluate, and document sufficient information to achieve the engagement's objectives.

2310 – Identifying Information
Internal auditors must identify sufficient, reliable, relevant, and useful information to achieve the engagement's objectives.

Interpretation:
Sufficient information is factual, adequate, and convincing so that a prudent, informed person would reach the same conclusions as the auditor. Reliable information is the best attainable information through the use of appropriate engagement techniques. Relevant information supports engagement observations and recommendations and is consistent with the objectives for the engagement. Useful information helps the organisation meet its goals.

2320 – Analysis and Evaluation
Internal auditors must base conclusions and engagement results on appropriate analyses and evaluations.

2330 – Documenting Information
Internal auditors must document relevant information to support the conclusions and engagement results.

> **2330.A1 –** The chief audit executive must control access to engagement records. The chief audit executive must obtain the approval of senior management and/or legal counsel prior to releasing such records to external parties, as appropriate.
>
> **2330.A2 –** The chief audit executive must develop retention requirements for engagement records, regardless of the medium in which each record is stored. These retention requirements must be consistent with the organisation's guidelines and any pertinent regulatory or other requirements.
>
> **2330.C1 –** The chief audit executive must develop policies governing the custody and retention of consulting engagement records, as well as their release to internal and external parties. These policies must be consistent with the organisation's guidelines and any pertinent regulatory or other requirements.

2340 – Engagement Supervision
Engagements must be properly supervised to ensure objectives are achieved, quality is assured, and staff is developed.

Interpretation:
The extent of supervision required will depend on the proficiency and experience of internal auditors and the complexity of the engagement. The chief audit executive has overall responsibility for supervising the engagement, whether performed by or for the internal audit activity, but may designate appropriately experienced members of the internal audit activity to perform the review. Appropriate evidence of supervision is documented and retained.

2400 – Communicating Results
Internal auditors must communicate the engagement results.

2410 – Criteria for Communicating
Communications must include the engagement's objectives and scope as well as applicable conclusions, recommendations, and action plans.

> **2410.A1 –** Final communication of engagement results must, where appropriate, contain internal auditors' overall opinion and/or conclusions.
>
> **2410.A2 –** Internal auditors are encouraged to acknowledge satisfactory performance in engagement communications.
>
> **2410.A3 –** When releasing engagement results to parties outside the organisation, the communication must include limitations on distribution and use of the results.
>
> **2410.C1 –** Communication of the progress and results of consulting engagements will vary in form and content depending upon the nature of the engagement and the needs of the client.

2420 – Quality of Communications
Communications must be accurate, objective, clear, concise, constructive, complete, and timely.

Interpretation:
Accurate communications are free from errors and distortions and are faithful to the underlying facts. Objective communications are fair, impartial, and unbiased and are the result of a fair-minded and balanced assessment of all relevant facts and circumstances. Clear communications are easily understood and logical, avoiding unnecessary technical language and providing all significant and relevant information. Concise communications are to the point and avoid unnecessary elaboration, superfluous detail, redundancy, and wordiness. Constructive communications are helpful to the engagement client and the organisation and lead to improvements where needed. Complete communications lack nothing that is essential to the target audience and include all significant and relevant information and observations to support recommendations and conclusions. Timely communications are opportune and expedient, depending on the significance of the issue, allowing management to take appropriate corrective action.

2421 – Errors and Omissions
If a final communication contains a significant error or omission, the chief audit executive must communicate corrected information to all parties who received the original communication.

2430 – Use of "Conducted in Conformance with the *International Standards for the Professional Practice of Internal Auditing*"
Internal auditors may report that their engagements are "conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*", only if the results of the quality assurance and improvement program support the statement.

2431 – Engagement Disclosure of Nonconformance
When nonconformance with the Definition of Internal Auditing, the Code of Ethics or the *Standards* impacts a specific engagement, communication of the results must disclose the:

- Principle or rule of conduct of the Code of Ethics or *Standard(s)* with which full conformance was not achieved;
- Reason(s) for nonconformance; and
- Impact of nonconformance on the engagement and the communicated engagement results.

2440 – Disseminating Results
The chief audit executive must communicate results to the appropriate parties.

Interpretation:
The chief audit executive or designee reviews and approves the final engagement communication before issuance and decides to whom and how it will be disseminated.

2440.A1 – The chief audit executive is responsible for communicating the final results to parties who can ensure that the results are given due consideration.

2440.A2 – If not otherwise mandated by legal, statutory, or regulatory requirements, prior to releasing results to parties outside the organisation the chief audit executive must:

- Assess the potential risk to the organisation;
- Consult with senior management and/or legal counsel as appropriate; and
- Control dissemination by restricting the use of the results.

2440.C1 – The chief audit executive is responsible for communicating the final results of consulting engagements to clients.

2440.C2 – During consulting engagements, governance, risk management, and control issues may be identified. Whenever these issues are significant to the organisation, they must be communicated to senior management and the board.

2500 – Monitoring Progress

The chief audit executive must establish and maintain a system to monitor the disposition of results communicated to management.

2500.A1 – The chief audit executive must establish a follow-up process to monitor and ensure that management actions have been effectively implemented or that senior management has accepted the risk of not taking action.

2500.C1 – The internal audit activity must monitor the disposition of results of consulting engagements to the extent agreed upon with the client.

2600 – Resolution of Senior Management's Acceptance of Risks

When the chief audit executive believes that senior management has accepted a level of residual risk that may be unacceptable to the organisation, the chief audit executive must discuss the matter with senior management. If the decision regarding residual risk is not resolved, the chief audit executive must report the matter to the board for resolution.

Glossary

Add Value
Value is provided by improving opportunities to achieve organisational objectives, identifying operational improvement, and/or reducing risk exposure through both assurance and consulting services.

Adequate Control
Present if management has planned and organised (designed) in a manner that provides reasonable assurance that the organisation's risks have been managed effectively and that the organisation's goals and objectives will be achieved efficiently and economically.

Assurance Services
An objective examination of evidence for the purpose of providing an independent assessment on governance, risk management, and control processes for the organisation. Examples may include financial, performance, compliance, system security, and due diligence engagements.

Board
A board is an organisation's governing body, such as a board of directors, supervisory board, head of an agency or legislative body, board of governors or trustees of a non-profit organisation, or any other designated body of the organisation, including the audit committee to whom the chief audit executive may functionally report.

Charter
The internal audit charter is a formal document that defines the internal audit activity's purpose, authority, and responsibility. The internal audit charter establishes the internal audit activity's position within the organisation; authorizes access to records, personnel, and physical properties relevant to the performance of engagements; and defines the scope of internal audit activities.

Chief Audit Executive
Chief audit executive is a senior position within the organisation responsible for internal audit activities. Normally, this would be the internal audit director. In the case where internal audit activities are obtained from external service providers, the chief audit executive is the person responsible for overseeing the service contract and the overall quality assurance of these activities, reporting to senior management and the board regarding internal audit activities, and follow-up of engagement results. The term also includes titles such as general auditor, head of internal audit, chief internal auditor, and inspector general.

Code of Ethics
The Code of Ethics of The Institute of Internal Auditors (IIA) are Principles relevant to the profession and practice of internal auditing, and Rules of Conduct that describe behaviour expected of internal auditors. The Code of Ethics applies to both parties and entities that provide internal audit services. The purpose of the Code of Ethics is to promote an ethical culture in the global profession of internal auditing.

Compliance
Adherence to policies, plans, procedures, laws, regulations, contracts, or other requirements.

Conflict of Interest
Any relationship that is, or appears to be, not in the best interest of the organisation. A conflict of interest would prejudice an individual's ability to perform his or her duties and responsibilities objectively.

Consulting Services
Advisory and related client service activities, the nature and scope of which are agreed with the client, are intended to add value and improve an organisation's governance, risk management, and control processes without the internal auditor assuming management responsibility. Examples include counsel, advice, facilitation, and training.

Control
Any action taken by management, the board, and other parties to manage risk and increase the likelihood that established objectives and goals will be achieved. Management plans, organises, and directs the performance of sufficient actions to provide reasonable assurance that objectives and goals will be achieved.

Control Environment
The attitude and actions of the board and management regarding the significance of control within the organisation. The control environment provides the discipline and structure for the achievement of the primary objectives of the system of internal control. The control environment includes the following elements:

- Integrity and ethical values
- Management's philosophy and operating style
- Organisational structure
- Assignment of authority and responsibility
- Human resource policies and practices
- Competence of personnel.

Control Processes
The policies, procedures, and activities that are part of a control framework, designed to ensure that risks are contained within the risk tolerances established by the risk management process.

Engagement
A specific internal audit assignment, task, or review activity, such as an internal audit, control self-assessment review, fraud examination, or consultancy. An engagement may include multiple tasks or activities designed to accomplish a specific set of related objectives.

Engagement Objectives
Broad statements developed by internal auditors that define intended engagement accomplishments.

Engagement Work Program
A document that lists the procedures to be followed during an engagement, designed to achieve the engagement plan.

External Service Provider
A person or firm outside of the organisation that has special knowledge, skill, and experience in a particular discipline.

Fraud
Any illegal act characterized by deceit, concealment, or violation of trust. These acts are not dependent upon the threat of violence or physical force. Frauds are perpetrated by parties and organisations to obtain money, property, or services; to avoid payment or loss of services; or to secure personal or business advantage.

Governance
The combination of processes and structures implemented by the board to inform, direct, manage, and monitor the activities of the organisation toward the achievement of its objectives.

Impairment
Impairment to organisational independence and individual objectivity may include personal conflict of interest, scope limitations, restrictions on access to records, personnel, and properties, and resource limitations (funding).

Independence
The freedom from conditions that threaten objectivity or the appearance of objectivity. Such threats to objectivity must be managed at the individual auditor, engagement, functional, and organisational levels.

Information Technology Controls
Controls that support business management and governance as well as provide general and technical controls over information technology infrastructures such as applications, information, infrastructure, and people.

Information Technology Governance
Consists of the leadership, organisational structures, and processes that ensure that the enterprise's information technology sustains and supports the organisation's strategies and objectives.

Internal Audit Activity
A department, division, team of consultants, or other practitioner(s) that provides independent, objective assurance and consulting services designed to add value and improve an organisation's operations. The internal audit activity helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of governance, risk management and control processes.

International Professional Practices Framework
The conceptual framework that organises the authoritative guidance promulgated by The IIA. Authoritative Guidance is comprised of two categories – (1) mandatory and (2) strongly recommended.

Must
The *Standards* use the word "must" to specify an unconditional requirement.

Objectivity
An unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they have an honest belief in their work product and that no significant quality compromises are made. Objectivity requires internal auditors not to subordinate their judgment on audit matters to others.

Residual Risk
The risk remaining after management takes action to reduce the impact and likelihood of an adverse event, including control activities in responding to a risk.

Risk
The possibility of an event occurring that will have an impact on the achievement of objectives. Risk is measured in terms of impact and likelihood.

Risk Appetite
The level of risk that an organisation is willing to accept.

Risk Management
A process to identify, assess, manage, and control potential events or situations to provide reasonable assurance regarding the achievement of the organisation's objectives.

Should
The *Standards* use the word "should" where conformance is expected unless, when applying professional judgment, circumstances justify deviation.

Significance
The relative importance of a matter within the context in which it is being considered, including quantitative and qualitative factors, such as magnitude, nature, effect, relevance, and impact. Professional judgment assists internal auditors when evaluating the significance of matters within the context of the relevant objectives.

Standard
A professional pronouncement promulgated by the Internal Audit Standards Board that delineates the requirements for performing a broad range of internal audit activities, and for evaluating internal audit performance.

Technology-based Audit Techniques
Any automated audit tool, such as generalized audit software, test data generators, computerized audit programs, specialized audit utilities, and computer-assisted audit techniques (CAATs).

Appendix 2 - Sample Audit Committee Charter

AUDIT COMMITTEE CHARTER

1. Objective

The objective of the Audit Committee (Committee) is to provide independent assurance and assistance to the NAME OF COUNCIL on risk management, control, governance, and external accountability responsibilities.

2. Authority

The Council authorises the Committee, within the scope of its role and responsibilities, to:

- Obtain any information it needs from any employee or external party (subject to their legal obligations to protect information).
- Discuss any matters with the external auditor or other external parties (subject to confidentiality considerations).
- Request the attendance of any employee or councillor at Committee meetings.
- Obtain external legal or other professional advice considered necessary to meet its responsibilities.

3. Composition and Tenure

The Committee will consist of:

3.1 Members (voting)

- Councillor
- Independent external member (not a member of the Council).
- Independent external member (not a member of the Council to be the chairperson).

3.2 Attendee (non-voting)

- General Manager
- Head of Internal Audit
- Chief Financial Officer

3.3 Invitees (non-voting) for specific Agenda items

- Representatives of the external auditor.
- Other officers may attend by invitation as requested by the Committee.

The independent external member will be appointed for the term of council, after which they will be eligible for extension or re-appointment following a formal review of their performance.

The members of the Committee, taken collectively, will have a broad range of skills and experience relevant to the operations of NAME OF COUNCIL. At least one member of the Committee shall have accounting or related financial management experience, with understanding of accounting and auditing standards in a public sector environment.

4. Role and Responsibilities

The Committee has no executive powers, except those expressly provided by the Council.

In carrying out its responsibilities, the Committee must at all times recognise that primary responsibility for management of Council rests with the Council and the General Manager as defined by the Local Government Act.

The responsibilities of the Committee may be revised or expanded by the Council from time to time. The Committee's responsibilities are:

4.1 Risk Management

- Review whether management has in place a current and comprehensive risk management framework, and associated procedures for effective identification and management of business and financial risks, including fraud.
- Review whether a sound and effective approach has been followed in developing strategic risk management plans for major projects or undertakings;
- Review the impact of the risk management framework on its control environment and insurance arrangements; and
- Review whether a sound and effective approach has been followed in establishing business continuity planning arrangements, including whether plans have been tested periodically.

4.2 Control Framework

- Review whether management has adequate internal controls in place, including over external parties such as contractors and advisors;
- Review whether management has in place relevant policies and procedures, and these are periodically reviewed and updated;
- Progressively review whether appropriate processes are in place to assess whether policies and procedures are complied with;
- Review whether appropriate policies and procedures are in place for the management and exercise of delegations; and
- Review whether management has taken steps to embed a culture which is committed to ethical and lawful behaviour.

4.3 External Accountability

- Satisfy itself the annual financial reports comply with applicable Australian Accounting Standards and supported by appropriate management sign-off on the statements and the adequacy of internal controls.
- Review the external audit opinion, including whether appropriate action has been taken in response to audit recommendations and adjustments.
- To consider contentious financial reporting matters in conjunction with council's management and external auditors.
- Review the processes in place designed to ensure financial information included in the annual report is consistent with the signed financial statements.
- Satisfy itself there are appropriate mechanisms in place to review and implement, where appropriate, relevant State Government reports and recommendations.
- Satisfy itself there is a performance management framework linked to organisational objectives and outcomes.

4.4 Legislative Compliance

- Determine whether management has appropriately considered legal and compliance risks as part of risk assessment and management arrangements.
- Review the effectiveness of the system for monitoring compliance with relevant laws, regulations and associated government policies.

4.5 Internal Audit

- Act as a forum for communication between the Council, General Manager, senior management, internal audit and external audit.
- Review the internal audit coverage and Internal Audit Plan, ensure the plan has considered the Risk Management Plan, and approve the plan.
- Consider the adequacy of internal audit resources to carry out its responsibilities, including completion of the approved Internal Audit Plan.
- Review all audit reports and consider significant issues identified in audit reports and action taken on issues raised, including identification and dissemination of better practices.
- Monitor the implementation of internal audit recommendations by management.
- Periodically review the Internal Audit Charter to ensure appropriate organisational structures, authority, access and reporting arrangements are in place.
- Periodically review the performance of Internal Audit.

4.6 External Audit

- Act as a forum for communication between the Council, General Manager, senior management, internal audit and external audit.
- Provide input and feedback on the financial statement and performance audit coverage proposed by external audit, and provide feedback on the external audit services provided.
- Review all external plans and reports in respect of planned or completed external audits, and monitor the implementation of audit recommendations by management.
- Consider significant issues raised in relevant external audit reports and better practice guides, and ensure appropriate action is taken.

4.7 Responsibilities of Members

Members of the Committee are expected to:

- Understand the relevant legislative and regulatory requirements appropriate to NAME OF COUNCIL.
- Contribute the time needed to study and understand the papers provided.
- Apply good analytical skills, objectivity and good judgment.
- Express opinions frankly, ask questions that go to the fundamental core of issues, and pursue independent lines of enquiry.

5. Reporting

At the first Committee meeting after 30 June each year, Internal Audit will provide a performance report of:

- The performance of Internal Audit for the financial year as measured against agreed key performance indicators.
- The approved Internal Audit Plan of work for the previous financial year showing the current status of each audit.

The Committee may, at any time, consider any other matter it deems of sufficient importance to do so. In addition, at any time an individual Committee member may request a meeting with the Chair of the Committee.

The Committee will report regularly, and at least annually, to the governing body of council on the management of risk and internal controls.

6. Administrative arrangements

6.1 Meetings

The Committee will meet at least four times per year, with one of these meetings to include review and endorsement of the annual audited financial reports and external audit opinion.

The need for any additional meetings will be decided by the Chair of the Committee, though other Committee members may make requests to the Chair for additional meetings.

A forward meeting plan, including meeting dates and agenda items, will be agreed by the Committee each year. The forward meeting plan will cover all Committee responsibilities as detailed in this Audit Committee Charter.

6.2 Attendance at Meetings and Quorums

A quorum will consist of a majority of Committee members, including at least one independent member. Meetings can be held in person, by telephone or by video conference.

The Head of Internal Audit will be invited to attend each meeting unless requested not to do so by the Chair of the Committee. The Committee may also request the Chief Finance Officer or any other employees to participate for certain agenda items, as well as the external auditor.

The General Manager may attend each meeting but will permit the Committee to meet separately with each of the Head of Internal Audit and the External Auditor in the absence of management on at least one occasion per year.

6.3 Secretariat

The Committee has appointed the Head of Internal Audit to be responsible for ensuring that the Committee has adequate secretariat support. The Secretariat will ensure the agenda for each meeting and supporting papers are circulated, at least one week before the meeting, and ensure minutes of the meetings are prepared and maintained. Minutes shall be approved by the Chair and circulated to each member within three weeks of the meeting being held.

6.4 Conflict of Interests

Councillors, council staff and members of council committees must comply with the applicable provisions of Council's code of conduct in carrying out the functions as council officials. It is the personal responsibility of council officials to comply with the standards in the code of conduct and regularly review their personal circumstances with this in mind.

Committee members must declare any conflict of interests at the start of each meeting or before discussion of a relevant agenda item or topic. Details of any conflicts of interest should be appropriately minuted.

Where members or invitees at Committee meetings are deemed to have a real or perceived conflict of interest, it may be appropriate they be excused from Committee deliberations on the issue where the conflict of interest may exist. The final arbiter of such a decision is the Chair of the Committee.

6.5 Induction

New members will receive relevant information and briefings on their appointment to assist them to meet their Committee responsibilities.

6.6 Assessment Arrangements

The Chair of the Committee will initiate a review of the performance of the Committee at least once every two years. The review will be conducted on a self-assessment basis (unless otherwise determined by the Chair), with appropriate input from management and any other relevant stakeholders, as determined by the Chair.

6.7 Review of Audit Committee Charter

At least once every two years the Audit Committee will review this Audit Committee Charter.

The Audit Committee will approve any changes to this Audit Committee Charter.

Approved: Audit Committee Meeting Date:

Appendix 3 - Sample Internal Audit Charter

The mission of internal auditing is to provide an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

Internal Audit at NAME OF ORGANISATION is managed by the TITLE OF INTERNAL AUDIT MANAGER who is the designated Head of Internal Audit within the organisation. The Head of Internal Audit is the top position within an organisation for internal audit activities, as defined in The International Standards for the Professional Practice of Internal Auditing (Standards) issued by the Institute of Internal Auditors.

1. Introduction

This Internal Audit Charter is a formal statement of purpose, authority and responsibility for an internal auditing function within NAME OF ORGANISATION.

- It establishes Internal Audit within NAME OF ORGANISATION and recognises the importance of such an independent and objective service to the organisation.
- It outlines the legal and operational framework under which Internal Audit will operate.
- It authorises the Head of Internal Audit to promote and direct a broad range of internal audits across NAME OF ORGANISATION and, where permitted, external bodies.

Mandate for Internal Audit THIS WILL VARY FROM ORGANISATION TO ORGANISATION AND MAY INCLUDE LEGISLATIVE OR REGULATORY REQUIREMENTS).

2. Role and Authority

The Head of Internal Audit is authorised to direct a comprehensive program of internal audit work in the form of reviews, previews, consultancy advice, evaluations, appraisals, assessments and investigations of functions, processes, controls and governance frameworks in the context of the achievement of business objectives.

For this purpose, all members of Internal Audit are authorised to have full, free and unrestricted access to all functions, property, personnel, records, information, accounts, files, monies and other documentation, as necessary for the conduct of their work.

3. Objectivity, Independence and Organisational Status

Objectivity requires an unbiased mental attitude. As such, all Internal Audit staff shall perform internal audit engagements in such a manner that they have an honest belief in their work product and that no significant quality compromises are made. Further, it requires Internal Audit staff not to subordinate their judgment on internal audit matters to that of others.

To facilitate this approach, Internal Audit shall have independent status within NAME OF ORGANISATION, and for this purpose shall be responsible directly through the Head of Internal Audit to the Audit Committee and administratively to the General Manager. Internal Audit shall be independent of the activities reviewed, and therefore shall not undertake any operating responsibilities outside internal audit work. Neither shall Internal Audit staff have any executive or managerial powers, authorities, functions or duties except those relating to the management of Internal Audit. Internal Audit staff and contractors shall report to the Head of Internal Audit any situations where they feel their objectivity may be impaired. Similarly, the Head of Internal Audit should report any such situations to the Audit Committee.

The work of Internal Audit does not relieve the staff of NAME OF ORGANISATION from their accountability to discharge their responsibilities. All NAME OF ORGANISATION staff are responsible for risk management and the operation and enhancement of internal control. This includes responsibility for implementing remedial action endorsed by management following an internal audit.

Internal Audit shall not be responsible for operational activities on a daily basis, or in the detailed development or implementation of new or changed systems, or for internal checking processes.

4. Scope of Work

The scope of services provided by Internal Audit shall encompass:

- The examination and evaluation of the adequacy and effectiveness of systems of internal control, risk management, governance, and the status of ethical behaviour.
- Ascertaining conformity with the goals and objectives of NAME OF ORGANISATION.
- Assessment of the economic and efficient use of resources.
- The examination of compliance with policies, procedures, plans and legislation.
- Assessment of the reliability and integrity of information.
- Assessment of the safeguarding of assets.
- Any special investigations as directed by the Audit Committee.
- All activities of NAME OF ORGANISATION, whether financial or non-financial, manual or computerised.

5. The scope of work may include

- **Assurance services** – objective examination of evidence for the purpose of providing an independent assessment on risk management, control, or governance processes for the organisation. Examples may include financial, performance, operational, compliance, system security, and due diligence engagements.
- **Consulting services** – advisory and related client service activities, the nature and scope of which are agreed with the client and which are intended to add value and improve an organisation's governance, risk management, and control processes without the internal auditor assuming management responsibility. Examples include counsel, advice, facilitation and training.

6. Internal Audit Methodology

Internal Audit shall use the most appropriate methodology for each internal audit engagement, depending on the nature of the activity and the pre-determined parameters for the engagement. Generally, internal audits will include:

- Planning.
- Reviewing and assessing risks in the context of the audit objectives.
- Examination and evaluation of information.
- Communicating results.
- Following up on implementation of audit recommendations.

7. Operating Principles

Internal Audit shall conform with:

- The Standards and Code of Ethics issued by the Institute of Internal Auditors.
- Where relevant, the Statement on Information Systems Auditing Standards issued by the Information Systems and Control Association.
- Relevant auditing standards issued by the Auditing and Assurance Standards Board.

8. Internal Audit shall:

- Possess the knowledge, skills, and technical proficiency essential to the performance of internal audits.

- Be skilled in dealing with people and in communicating audit issues effectively.
- Maintain their technical competence through a program of continuing education.
- Exercise due professional care in performing internal audit engagements.

9. Internal Audit staff shall:

- Conduct themselves in a professional manner.
- Conduct their activities in a manner consistent with the concepts expressed in the Standards and the Code of Ethics.

10. Reporting Arrangements

The Head of Internal Audit shall at all times report to the Audit Committee. At each Audit Committee meeting the Head of Internal Audit shall submit a report summarising all audit activities undertaken during the period, indicating:

- ✓ Internal audit engagements completed or in progress.
- ✓ Outcomes of each internal audit engagement undertaken.
- ✓ Remedial action taken or in progress.

On completion of each internal audit engagement, Internal Audit shall issue a report to its audit customers detailing the objective and scope of the audit, and resulting issues based on the outcome of the audit. Internal Audit shall seek from the responsible senior executive an agreed and endorsed action plan outlining remedial action to be taken, along with an implementation timetable and person responsible. Responsible officers shall have a maximum of ten working days to provide written management responses and action plans in response to issues and recommendations contained in internal audit reports.

The Head of Internal Audit shall make available all internal audit reports to the Audit Committee. However, the work of Internal Audit is solely for the benefit of NAME OF ORGANISATION and is not to be relied on or provided to any other person or organisation, except where this is formally authorised by the Audit Committee or the Head of Internal Audit.

In addition to the normal process of reporting on work undertaken by Internal Audit, the Head of Internal Audit shall draw to the attention of the Audit Committee all matters that, in the Head of Internal Audit's opinion, warrant reporting in this manner.

11. Planning Requirements

Internal Audit uses a risk-based rolling program of internal audits to establish an annual Internal Audit Plan to reflect a program of audits over a 12 month period. This approach is designed to be flexible, dynamic and more timely in order to meet the changing needs and priorities of NAME OF ORGANISATION.

The Head of Internal Audit shall prepare an annual Internal Audit Plan for review and approval by the Audit Committee, showing the proposed areas for audit. The annual Internal Audit Plan shall be based on an assessment of the goals, objectives and business risks of NAME OF ORGANISATION, and shall also take into consideration any special requirements of the Audit Committee and senior executives.

The Head of Internal Audit has discretionary authority to adjust the Internal Audit Plan as a result of receiving special requests from management to conduct reviews that are not on the plan, with these to be approved at the next meeting of the Audit Committee.

12. Quality Assurance & Improvement Program

The Head of Internal Audit shall oversee the development and implementation of a quality assurance and improvement program for Internal Audit, to provide assurance that internal audit work conforms to the Standards and is focused on continuous improvement.

13. Co-ordination with External Audit

The Head of Internal Audit shall periodically consult with the external auditor, to discuss matters of mutual interest, to co-ordinate audit activity, and to reduce duplication of audit effort.

14. Review of the Internal Audit Charter

The Head of Internal Audit shall periodically review the Internal Audit Charter to ensure it remains up-to-date and reflects the current scope of internal audit work.

15. Evaluation of Internal Audit

The Head of Internal Audit shall develop performance measures (key performance indicators) for consideration and endorsement by the Audit Committee, as a means for the performance of Internal Audit to be periodically evaluated.

Internal Audit shall also be subject to an independent quality review at least every five years. Such review shall be in line with the Standards of Professional Practice in Internal Audit and be commissioned by and report to the Audit Committee.

16. Conflict of Interests

Internal auditors are not to provide audit services for work for which they may previously have been responsible. Whilst the Standards provide guidance on this point and allow this to occur after 12 months, each instance should be carefully assessed.

When engaging internal audit contractors, the Head of Internal Audit shall take steps to identify, evaluate the significance, and manage any perceived or actual conflicts of interest that may impinge upon internal audit work.

Instances of perceived or actual conflicts of interest by the Head of Internal Audit or Internal Audit staff and contractors are to be immediately reported to the Audit Committee by the Head of Internal Audit.

Any changes to this Internal Audit Charter will be approved by the Audit Committee.

Approved: Audit Committee Meeting Date:

Appendix 4 - Risk Management Assessment Tool

This tool is designed to assist the Audit Committee's consideration of risk management, through the review of material, and discussion or presentations from senior management.

The Committee's charter will determine the extent to which the Audit Committee needs to consider risk management or whether this is to be overseen by a separate Risk Committee.

The tool consists of a series of questions, or high level prompts, which should be tailored to meet the Council's particular circumstances. The extent and nature of the Committee's consideration of risk will largely be dependent on whether or not the Council has in place a formal and structured risk management framework.

Some elements, for example, questions on risk strategy and structure, could be addressed on an annual basis while others could be considered on a more regular basis, depending on Council's individual risk management activities, and the Committee charter.

A 'no' answer does not necessarily indicate a failure or breakdown in Council's risk management framework but may indicate where more detailed discussion or consideration by the Committee is warranted.

Risk Strategy	**Yes**	**No**
Is Council's risk management framework clearly articulated and communicated to all staff?	❑	❑
Is Council's risk posture clear? (i.e. the amount of risk Council is willing to take)	❑	❑
Has the 'tone at the top' from the General Manager's perspective permeated the risk culture of the Council?	❑	❑
Is there a clear link between risk management, the control environment and business planning?	❑	❑
Risk Structure	**Yes**	**No**
Is responsibility and accountability for risk management clearly assigned to individual managers?	❑	❑
Are risk management activities/responsibilities included in job descriptions, where appropriate?	❑	❑
Are the primary risk management activities (for example, business continuity planning, fraud control plan, annual risk assessment, and so on) across Council, clearly defined?	❑	❑
Is responsibility for co-ordinating and reporting risk management activity to the Audit Committee, or other relevant committee clearly defined?	❑	❑
Does Council have a risk management support capability to assist the development of emerging risk management practices?	❑	❑
Is there a common risk management language/terminology across Council?	❑	❑

Does management have a formal business continuity plan incorporating a disaster recovery plan?	❑	❑
Risk Identification and Assessment	**Yes**	**No**
Are risk assessments undertaken at both strategic and operational levels?	❑	❑
Have the risks associated with cross-agency governance arrangements been identified?	❑	❑
Does a comprehensive risk profile exist?	❑	❑
Is a risk assessment undertaken for all significant organisational changes/projects?	❑	❑
Does management have effective processes for ensuring risk assessments have been performed in each major business area?	❑	❑
Is there a process in place to identify emerging risks and to incorporate these into the Council's risk management plan?	❑	❑
Do the Council's policies appropriately address relevant operational and financial risks?	❑	❑
Have any frauds, material irregularities or possible illegal acts been identified?	❑	❑
Does Council have a current fraud control policy and plan in place which identifies all fraud related risks?	❑	❑
Risk Mitigation and Improvement	**Yes**	**No**
Has management assessed the effectiveness of controls over the highest priority risks?	❑	❑
Does management consider the controls to mitigate risks to within Council's risk tolerance to be adequate?	❑	❑
Have all significant recommendations that impact on risk or the effective operation of controls, made by Council's internal and external auditors, been addressed in a timely manner?	❑	❑
Is there a response plan for prompt and effective action when fraud or an illegal act is discovered?	❑	❑
Monitoring and Assurance	**Yes**	**No**
Are systems in place for measuring and monitoring risk, including consideration of common risk themes across Council?	❑	❑
Are risks, including suspected improprieties, escalated to the appropriate levels of management within Council?	❑	❑
Does Council have a formal process by which senior management periodically assure the General Manager/Council that key control strategies are operating effectively?	❑	❑

Continuous Improvement	**Yes**	**No**
Do Council's management practices reflect the concept of risk management?	❑	❑
Does Council have a culture of continuous improvement? (for example does Council 'learn' from past risk exposures)	❑	❑
Does management periodically review its risk profile?	❑	❑
Is risk a priority consideration whenever business processes are improved?	❑	❑

Name	
Position	*(To be completed by the most senior executive responsible for risk management within council)*

Signed	Date

Appendix 5 - Common risks in the council environment

This appendix lists some of the more significant risk exposures which are likely to be faced in the council environment.

Warning - This list is provide as an aid to check completeness. It should only be used after a thorough risk identification process is conducted and should not be used as a substitute for an effective risk identification process. Not adhering to this advice is likely to result in significant risks which are specific to your council not being identified, which may have significant consequences if that risk were to eventuate.

Governance

- Advocacy processes ineffective at State and Federal Government level leading to unwanted results/lack of funding etc.
- Governance training processes (Code of Conduct, Protected Disclosures, Conflict of Interests, councillor interaction with staff, identifying fraud) not undertaken/ineffective leading to higher risk of fraud and corruption.
- Corruption (development applications/rezonings/election funding) leading to loss of reputation of Council.
- Lack of cohesion of Councillors leading to lack of strategic direction/poor decision making.
- Complaints handling processes ineffective leading to legal disputes/lack of transparency.
- Misuse of personal information leading to penalties under Privacy legislation or loss of confidence in Council.
- Poor processes for the disclosure and management of staff conflicts of interest leading to partial decision making.
- Inappropriate delegations or delegations not properly exercised.
- Failure to implement council resolutions leading to breakdown of council/staff relationships.

Planning and Regulation

- Unanticipated population growth leading to unsustainable natural environment/infrastructure demand.
- Planning strategies not developed in timely manner leading to delayed delayed/inappropriate development/community angst.
- Population decrease leading to community breakdown.
- Planning controls outdated, leading to poor urban design.
- Legislation not complied with leading to legal disputes/penalties
- Poor planning controls leading to poor planning decisions

Assets and Finance

- Adequate asset management processes not being in place, leading to substantial additional long term financial burdens to council.
- Adequate long term financial management processes not being in place leading to poor decision making by council.
- Limited opportunities to increase rates and user charges, leading to increasing reliance on grants/one off funding.
- Cost of infrastructure to be funded under section 94 contributions under-estimated/unaffordable, leading to funding shortfalls/reduced level of infrastructure.
- Limited regional collaboration between councils, leading to on-going inefficiencies and additional costs to regional residents.

- Operational unit business plans not effectively in place, leading to poor decision making/performance monitoring.
- Inadequate disaster/crisis management processes, leading poor response in real situation.
- Community assets under-utilised leading to closure in longer term.
- Quasi commercial operations of Council (child care/tourist parks/airports/cultural centres etc) not operated effectively leading to higher than appropriate council subsidisation.
- Project management practices not effectively in place, leading to cost over run/quality issues.
- Appropriate procurement processes not undertaken, leading to value for money issues/questions of probity.
- Council assets under insured leading to financial exposure to Council
- Plant fleet under utilised leading to additional costs to Council.
- Minor road condition unable to be maintained at satisfactory level leading to community dissatisfaction.
- Mismanagement of Council supported community entities leading additional financial burden to Council/cessation of service.
- Knowledge management processes not effectively in place leading to poor decision making.
- Inadequate information security leading to issues of confidentiality or legal/financial penalties to Council.

Community and Consultation

- Inability to maintain/increase employment base leading to adverse socio/economic consequences.
- Poor issues management, leading to sustained loss of public support for council in media and/or public.
- Unnecessary bureaucratic processes/red tape leading to additional costs to those dealing with Council.

Workforce Relations

- Productivity levels of council below industry/commercial benchmarks or not measured, leading to additional costs/perpetuation of inefficiencies.
- Skill shortages in professional areas, leading to inability to maintain standards/deliver services.
- Loss of trained staff with specific knowledge, leading to loss of knowledge, ability and experience.
- Inadequate/insufficient staff training leading to reduced skills, currency of knowledge, errors and omissions, turnover of staff.
- Information technology systems outdated leading to on-going inefficiencies..
- OHS not appropriately embedded in operational processes leading to major injury/death or penalty against Council or Council staff.