

**Date: 6 March 2013**

**Item 8: Review of Internal Audit Effectiveness – Action Plan**

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**This paper will be considered in public**

**1 Summary**

- 1.1 The purpose of this paper is to update the Audit and Assurance Committee on the proposed actions arising out of KPMG's review of Internal Audit effectiveness.

**2 Recommendation**

- 2.1 **The Committee is asked to note the paper.**

**3 Background**

- 3.1 The findings from KPMG's review of TfL Internal Audit were presented to the December meeting of the Audit and Assurance Committee.
- 3.2 The report found that Internal Audit's methodologies and day to day processes were generally effective and commented positively on TfL's 'direction of travel' with regard to the integrated assurance agenda. However, the report also made a number of recommendations for further development.
- 3.3 All of the recommendations are agreed and are being implemented. The attached Appendix sets out these recommendations and the proposed actions that will be taken to implement them.

**List of appendices to this report:**

Appendix 1 – KPMG Effectiveness Review 2012 – Action Plan

**List of Background Papers:**

KPMG Review of TfL Internal Audit – Report dated 14 November 2012

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## KPMG Effectiveness review 2012 – Action Plan

	Recommendation	Proposed action/ Status
1	<p><b>Assurance Mapping</b></p> <p>The current audit plan is set out in the integrated assurance plan which amalgamates various source of assurance but does not clearly demonstrate the synergies and potential efficiencies to be gained from integrating assurance. Work is currently underway to map controls to risks, starting with HR and IM, with the aim of building an integrated assurance plan around this.</p> <p><i>We recommend that this process continues to be rolled out to all functions to allow an organisational map of risks, controls and assurances to be created, around which an integrated assurance plan can be constructed.</i></p>	<p>Agreed. The ADG has initiated a project to develop assurance maps for all major activities in TfL. The work is being facilitated by Internal Audit in liaison with representatives from the business. Assurance maps for HR and IM have been completed, and a map for key financial process is currently being developed. Further assurance maps will be developed during 2013/14, with project assurance, health and safety and efficiencies identified as the next areas to be covered.</p>
2	<p><b>Integrated assurance reporting</b></p> <p>Reporting of progress against the integrated assurance plan is a work in progress. Currently the Director of IA reports to the Audit and Assurance Committee quarterly summarising internal audit activity and, separately, provides commentary on the activity of other assurance providers. There is currently no mechanism to summarise concisely and in a consistent format the assurances from work performed in the last quarter or to explicitly link those assurances back to risks being mitigated by the processes and controls subject to review.</p> <p><i>As integrated assurance develops further, the internal audit function should determine how it will report against the integrated plan and the extent to which outputs from other assurance functions will be sense checked and summarised by the Director of Internal Audit before inclusion in the report (and use in the annual internal audit opinion).</i></p>	<p>Agreed. A reporting format that links assurance outputs to strategic risks has been developed and piloted with the Surface Transport Board and the Rail and Underground Board. It will also be piloted with the Leadership Team prior to introducing a regular process for reporting progress in 2013/14.</p> <p>Once in place this report will also form part of the Director of Internal Audit's quarterly report to the Audit and Assurance Committee.</p>

3	<p><b>ADG work programme</b>  Post-Project Horizon, the organisation and its assurance arrangements continue to evolve. The forthcoming transition of the LU HSE assurance function to the TfL IA team, the development of the TfL management system and associated in-built self-assurance, and the development of strategic risk management mean that the internal audit and assurance functions will need to continue to adapt to provide the most appropriate assurance offer to the business.</p> <p><i>The Assurance Delivery Group (ADG) has made significant steps in moving forward the integrated assurance agenda, but now needs a formalised work programme to set out clearly its next steps. This should include actions and milestones to achieve these.</i></p>	<p>Completed. A paper setting out the achievements of the ADG to date, together with a forward programme of work, was presented to the Leadership Team in January, and is included elsewhere on this agenda.</p>
4	<p><b>Impact of recommendations</b>  A number of interviewees expressed concern around the ability of IA to add real value by getting to the root of the problem and raising useful recommendations. The perception of several stakeholders is that issues are not always clear in terms of their strategic impact on the organisation.</p> <p><i>Recommendations included in reports should clearly demonstrate the impact of non-implementation on the business and therefore the value that implementation will add.</i></p>	<p>Agreed. Internal Audit reports already seek to demonstrate the impact of non-implementation on the business in the 'risk exposure' sections of the report.</p> <p>In addition, some local issues may result from wider issues arising elsewhere in TfL (eg with IT or HR processes) and this may not always be fully brought out in reports. We will seek to ensure that root causes of issues are identified, and, where appropriate, act as a conduit for raising these in the wider business.</p>

5	<p><b>Frequency of meetings</b> Two stakeholders interviewed commented that meetings with internal audit were too frequent, and that agenda content was therefore not always sufficient.</p> <p><i>Internal audit should aim to build its schedule of stakeholder meetings around the integrated assurance plan and emerging risks to ensure there is a clear need and focus for each meeting held.</i></p>	<p>Agreed. A stakeholder management process has been developed to monitor contacts with managers around the business, with the aim of ensuring that stakeholder meetings are held with an appropriate level of frequency and that multiple meetings with individual stakeholders are avoided.</p> <p>In addition, members of the Internal Audit management team who have stakeholders that they meet on a regular basis will ask the views of those stakeholders on the frequency of their meetings.</p>
6	<p><b>Defining competencies</b> IA have not formally defined the overall mix of competencies required within the department. This creates the risk that there is no clear basis for recruitment decisions or responding to changes in demand from the business.</p> <p><i>A matrix of required competencies should be developed based on the current needs of the business and IA's mission and role. It should define the optimum skill mix and be sufficiently flexible to respond to changes in demand. Such a document is particularly important given the structure of the TfL IA function, as specialisation of staff reduces the flexibility of resources to fill gaps.</i></p>	<p>Agreed. A competencies matrix for the department is being developed. This will set out the qualifications and skillsets that the department requires, and highlight any gaps. This will then be used to inform any future recruitment programmes or secondments (see 7 below).</p> <p>The competency matrix will be in place by 30 June 2013.</p>
7	<p><b>Rotation programme</b> There has been low staff turnover in IA recently, which can reduce opportunities for innovation and challenge to existing staff practices.</p> <p><i>IA could consider expanding the existing secondment programme to increase exposure of staff in the wider organisation to internal audit, and vice versa. There may also be possibilities for secondments within the GLA family.</i></p>	<p>Agreed. The Director of Internal Audit will discuss this with senior managers in relevant areas of TfL, and with HR, with the aim of identifying potential opportunities. We will seek to have achieved at least one inward and one outward secondment during the course of 2013/14.</p>

8	<p><b>Medium term strategy</b></p> <p>Internal audit does not currently prepare a medium term strategy, and has only an activity plan covering the year ahead. Though it would require review and refresh at least annually as part of the planning cycle, such a strategy would enable IA and the Audit and Assurance Committee to understand how assurance is proposed to be gained over the longer term, and allow review and challenge to the coverage and frequency of reviews on a medium term programme. For example, it is extremely difficult to judge the prioritisation and time criticality of reviews in the absence of any information on frequency of review.</p> <p><i>The annual integrated assurance plan should be set in the context of a medium term strategy which incorporates inputs from all assurance functions to prevent duplication of effort. The strategy would make it clear which reviews required completing on a cyclical basis and enable review and challenge to be made to gaps, coverage and prioritisation in the context of a 3 – 5 year programme of activity. The plan should be explicitly linked to risks.</i></p>	<p>Completed. The Integrated Assurance Plan presented to the March 2013 Audit and Assurance Committee meeting includes a section showing plans for cyclical areas of the plan with a three year outlook.</p>
9	<p><b>Risk-based procedures</b></p> <p>In one instance from our file review (review of supplier relationship management), there was no discussion of risk in the audit program, and it was therefore unclear how the set of procedures had been developed to respond to the organisation's risks.</p> <p><i>Risks identified in the scoping document (see recommendation above) should map directly through to the audit programme, with designed procedures in turn being mapped to these risks. This should result in more focused testing and a clearer link between perceived risk, procedures performed and days allocated.</i></p>	<p>Completed. This is already an established part of our process as set out in our Audit Manual. We will re-emphasise this point to staff, and audit managers reviewing working papers will explicitly check that there is a clear trail mapping from the risks within the area under review to the audit procedures performed.</p>

10	<p><b>Key Performance Indicators (KPIs)</b> IA have KPIs in place for timeliness of reporting and customer feedback. No others KPIs are currently reported, although we note that a framework for evaluating IA's performance is currently being developed. This is intended for use internally rather than the wider organisation.</p> <p><i>We recommend that the Audit and Assurance Committee provide input to this evaluation process, and monitor performance against agreed elements of the framework going forward. The evaluation criteria should be based upon IA's mission and objectives, and be specific and measurable.</i></p>	<p>Agreed. An Internal Audit Performance Dashboard, incorporating a range of performance indicators has been developed and is currently being piloted internally.</p> <p>Once the Dashboard is operating effectively, it will be shared with the Audit and Assurance Committee, whose views will be sought on which performance indicators it would be useful to have reported on a regular basis.</p>
11	<p><b>Report ratings</b> It is unclear for the audience how overall assurance ratings for interim reports are arrived at in the absence of RAG rated recommendations. At the time of conducting our review, recommendations were not RAG rated to give the reader a detailed assessment of perceived significance. We note however that IA now intends to grade its recommendations as Priority 1, 2 or 3.</p> <p><i>Once clear priority ratings have been implemented, and acknowledging the importance of auditor judgement, the convention for converting recommendations into an overall assurance rating for a review should be communicated in the annual plan.</i></p>	<p>Completed. Individual audit issues raised in reports are now given a priority rating of 1, 2, or 3, and these priority ratings have been defined and are set out in the audit reports. We have also documented how these individual ratings translate into the overall rating for the audit.</p>

12	<p><b>Positive assurance</b></p> <p>We note that IA reports include areas of good practice, and state the scope of reviews in broad terms and that areas not specifically mentioned in the report have been found to be operating effectively. However, reports do not state which risks have been reviewed and which procedures have been performed. Internal audit has a role in reporting positive assurance as well as exceptions. Because reports are generally written on an exceptions basis, the user is unable to determine which controls have been found to be operating effectively.</p> <p><i>We recommend that IA consider ways in which reports could be enhanced to set out more clearly positive assurances over risks that are found to be controlled effectively.</i></p>	<p>Agreed. Internal Audit reports already set out positive assurances, both by explicitly highlighting areas of good practice that we have found and by stating that scope areas not mentioned were found to be working effectively.</p> <p>However, we will consider whether there are opportunities to bring out the positive assurances more clearly without significantly increasing the length of the reports.</p>
13	<p><b>Anticipated assurance</b></p> <p>Reports or scoping documents do not state what management expected the assurance rating to be prior to the audit work commencing. Obtaining this anticipated assurance may encourage more openness in requesting IA to perform work into areas that are known not be operating effectively and provides a sense check for the Audit and Assurance Committee on management's view of control environments.</p> <p><i>We recommend that an 'anticipated assurance' rating is obtained from relevant directors or senior officers prior to each review.</i></p>	<p>Agreed. Anticipated assurance will be piloted on a sample of audits and we will review the outcomes before deciding whether to make this a standard part of our audit methodology.</p>