



Internal Audit Policy

GOVERNMENT OF KHYBER PAKHTUNKHWA
FINANCE DEPARTMENT



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Preface

It is with great pleasure that we are presenting the first ever Internal Audit Policy of Government of Khyber Pakhtunkhwa – an important milestone in the pursuit of transparency and accountability. The concept of internal audit in government departments was introduced in Khyber Pakhtunkhwa in 2012 to improve internal controls, operational efficiency and effectiveness, and reduce chances of errors, irregularities, pilferages and corruption. With increasing functional and resource portfolios, and evolving systems and processes, public financial management is exposed to higher risks of misuse. Hence, internal audit provides the means for strengthening oversight and empowers the Principal Accounting Officer to detect errors, prevent irregularities and make better and timely decisions to mitigate fiduciary risks and improve organizational effectiveness.

The KP Internal Audit Policy lays down the foundation for building an effective internal audit function. It defines and establishes the purpose, authority and responsibility for internal audit function along with personnel management and reporting relationship in the light of international best practices. This policy sets up a standardized mechanism for conducting internal audit in provincial and local government entities to ensure a harmonized approach towards achieving the overall goal for transparent and accountable governance leading to improved service delivery and greater trust between the state and the citizens.

The guidelines provided herewith will be subject to improvements and expansion over time to keep up to date with the demands of stakeholders and advancing practices and technologies in the global arena. Field Auditors and stakeholders using these guidelines are, therefore, encouraged to make suggestions for further improvements and give regular feedback.

This policy is a result of concerted efforts and dialogue within the Government and with other stakeholders. I am truly appreciative of the efforts of my team in Finance Department for their hard work and valuable contribution in preparation of this Policy. I am also thankful for the support provided by DFID through the Sub National Governance (SNG) Programme, which proved to be paramount in formulation of the document.

The implementation of the Policy will remain a collective responsibility of all the stakeholders. It will be the prerogative and obligation of the Principal Accounting Officers to utilize their internal audit cells to the best of their ability in ensuring efficient use of precious resources for the betterment of the people. This will be the key to success or failure of this initiative. I look forward to working together to achieve the objectives envisioned in the Internal Audit Policy.

Shakeel Qadir Khan
Secretary Finance

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1. Policy Statement

The provincial government intends to establish and put in place effective internal controls in every department and office for the purposes of efficiency, transparency, judicious use of resources and assets, better management to avoid wastage and misappropriation, prevention and timely detection of errors and irregularities in the financial proceedings and other processes of the government. The Provincial Government considers Internal Audit a very important management tool. This policy tasks the Finance Department to establish Internal Audit Cells and provide sustainable support and assistance for running the activity effectively.

2. Purpose

The purpose of this policy document is to provide a legal basis for the functioning of Internal Audit in all the departments of the Government of Khyber Pakhtunkhwa. It defines the broad principles related to the purpose, authority and responsibility of the Internal Audit Cells (IACs) and the role of the Provincial Internal Audit Cell (PIAC) with regard to coordination, support and functioning of IACs and PIAC.

3. Purview

The jurisdiction of the Internal Audit shall include all payments made out of the provincial consolidated fund, contract award and management- its processes and record, recruitments, risk and asset management. This policy shall be applicable to all departments, directorates, attached departments, attached offices and autonomous/semi-autonomous bodies, authorities and boards working under the administrative departments.

4. Objectives

The Internal Audit Cell shall determine whether the Department's governance, processes, internal controls and risk management systems are adequate and functioning in a manner to ensure that:

- i. The application of risk management procedures and methodologies (including risk identification and management) and the functioning of internal control system are effective;
- ii. Significant financial, managerial, and operating information is accurate, reliable, and timely;
- iii. Employees' actions are in compliance with the internal control policies, standards, procedures and applicable laws and regulations;
- iv. Department's resources and assets are economically acquired, efficiently used, properly accounted for and adequately safeguarded;
- v. Department's Key Performance Indicators (KPI), programs, plans and objectives are achieved;
- vi. Quality and continuous improvements are fostered in Department's control processes;
- vii. Significant legislative or regulatory issues impacting the Departments are recognised and appropriately addressed; and

The Internal Audit Cell shall also aim to identify opportunities for improving management controls, cost savings, and Department's image during audits and shall communicate its recommendations to the appropriate level of management in a timely manner.

5. Scope of Work

The scope of work of the Internal Audit Cell includes the following:

- i) Examination and evaluation of the adequacy and effectiveness of the internal control systems;
- ii) Review of the application and effectiveness of risk management procedures and risk assessment methodologies;
- iii) Review of the accuracy and reliability of accounting records and financial reports;
- iv) Review of the measures for safeguarding assets;
- v) Review of the systems established to ensure compliance with the legal and regulatory requirements, code of conduct and implementation of policies and procedures;
- vi) Carrying out special investigations and reviews;
- vii) Examine and audit any activity of the Department and Attached Departments.

6. Organization of Internal Audit

6.1 Provincial Internal Audit Cell (PIAC)

The Provincial Internal Audit Cell (PIAC) shall be a wing of the Finance Department. Its function is to provide support, assistance, technical backstopping and coordination for the functioning of the Internal Audit Cells across the Provincial Government. The PIAC shall be headed by the Provincial Coordinator Internal Audit (PCIA), who shall report to the Secretary Finance.

Functions of PIAC

- i) Formulation of policies and procedures related to the functioning of the IACs;
- ii) Receiving, compiling, consolidating and presenting annual audit plan to the Chief Secretary;
- iii) Collecting progress reports from the IACs and their submission to the Chief Secretary;
- iv) Prepare, review and update Internal Audit Manual and Toolkits, where required;
- v) The PIAC shall assess and determine training needs of the IACs and arrange necessary training resources and assistance to enable personnel to develop and maintain required competence and capabilities.

There shall be no material interference by PIAC in the operations of the IACs.

6.2 Departmental/District Internal Audit Cells (IACs)

Each department, attached department, autonomous body, authority, board, university, district government and major development projects of the Government of Khyber Pakhtunkhwa shall establish a separate and independent Internal Audit Cell with the approval of the Principal Accounting Officer (PAO).

There shall be an Audit Officer along with Auditors and supporting staff who shall be appointed keeping in view the volume of budget and scope of activities. The Audit Officer shall be the Head of the IAC.

6.3 Independence

The Head of the IAC shall report functionally and administratively to the PAO of the Department to ensure independence from Department's operations. Furthermore, the Head of the IAC shall be declared as a Drawing and Disbursing Officer for the operations of the IAC.

All employees within the IAC shall maintain independence from the operational management and shall have no direct authority over any of the operational activities of the Department. In addition, they shall not have any conflict of interest with the Department.

The Head of the IAC may be nominated on various committees of the Department to ensure that the IAC keeps abreast of all the significant developments and issues within the Departments and for providing valuable advice to such committees e.g. Departmental Accounts Committee, Public Accounts Committee and Procurement Committees etc.

The PAO shall provide adequate office space, equipment and other facilities to the officers and officials of the IAC for effective discharge of their duties.

6.4 Objectivity and Impartiality

All employees within the IAC shall maintain objectivity while performing their responsibilities. Objectivity requires that the employees do not subordinate judgement on audit matters to that of others and to perform audits in such a manner that no quality compromises are made.

Where possible, staff assignments within the IAC shall be rotated periodically. In addition, internally-recruited auditors shall not audit activities or functions they performed within the last year. Such audit staff shall work under the supervision of the Head of the IAC concerned. Furthermore, the IAC shall ensure that its objectivity is not adversely affected when it recommends standards of control for systems, or review procedures or capital projects while they are being implemented.

All employees of the IAC shall be impartial and shall be in a position to perform their assignments free from bias and interference. They shall not have any vested interest in the area being audited or the auditee. Thus, they shall not be involved in operations of the auditee and in selection or implementation of internal control measures.

6.5 Professional Standards and Competence

The Head of the IAC shall ensure that internal audit activities are performed according to the Institute of Internal Auditors' mandatory guidance, including the Definition of Internal Auditing, the Code of Ethics, and the International Standards for the Professional Practice of Internal Auditing in addition to applicable Government of Khyber Pakhtunkhwa's rules and such policies and procedures as may be prescribed by the PIAC.

The internal audit activity needs to collectively possess or obtain the knowledge, skills, and other competencies needed to perform its responsibilities. Professional competence should be maintained and enhanced through systematic continuing training (including IT). The PCIA shall ensure necessary training for the auditors.

7. Responsibilities of Internal Audit Cells

The IACs shall have the following responsibilities:

- i) Carrying out strategic long-term planning (for at least three years) for the IAC in order to cover all formations of the Department; submitting the approved plan to the PCIA within one month of its approval;
- ii) Preparing and implementing an Annual Audit Plan as approved by the PAO; submitting the approved plan to the PCIA latest by 1st July of the year planned for. The Head of the IAC shall convey the plan to the entities to be audited;
- iii) Assessing the quality of the Department's risk management, governance and internal control systems and providing an overview of the effectiveness of the internal control system;
- iv) Assessing compliance of the management's activities with the relevant laws and regulations;
- v) Ascertaining the adequacy of and compliance with the governance policies and procedures;
- vi) Appraising the effectiveness and application of the administrative, financial, operational and IT controls and the data security procedures;
- vii) Reviewing the adequacy, application and effectiveness of risk management policies and procedures and risk management methodologies to ensure that all material risks, inherent in the Department's activities are identified, assessed and adequately controlled by the management;
- viii) Considering development and maintenance of a mechanism for assessment of fraud risk within the Department;
- ix) Assisting the Department's management in the investigation of significant suspected fraudulent activities within the Department and notifying the PAO of the results;
- x) Testing of the reliability and timeliness of the regulatory reporting (if any);

- xi) Review of the management and financial information systems, including the electronic information system;
- xii) Appraising the economy and efficiency with which resources are employed;
- xiii) Assessing the adequacy of and compliance with the internal controls for safeguarding the Department's assets and wherever appropriate, verifying the existence of assets;
- xiv) Reviewing specific matters and carrying out special tasks, projects or investigations requested by the PAO. Opinion may be sought on important reorganizations, initiation of important or new activities, creation of new establishments, and the setting up or reorganization of risk control systems, management information systems or information technology systems. However, the responsibility for establishment and introduction of these measures will remain with the respective management;
- xv) Reviewing existing operations or programs to determine whether results are consistent with those expected;
- xvi) Presenting, at the end of each audit/ special assignment, a report containing the summary and detailed description of issues, making recommendations thereon and assigning audit ratings, wherever necessary;
- xvii) Submitting a periodic (preferably quarterly) Internal Audit progress report to the PAO along with summarised results of audit activities; sharing the progress report with the PCIA within one month of the close of the concerned quarter;
- xviii) Monitoring, taking follow-up action and evaluating the corrective actions taken by the management and reporting any significant delays in clearance of audit observations of any auditable entity;
- xix) Assessing, at least on an annual basis, adequacy and effectiveness of the Department's internal control processes and presenting these ratings to the PAO;
- xx) Suggest changes for updating Internal Audit Toolkits to the PIAC, where required;
- xxi) Close coordination with external auditors and facilitate the department in forums like Departmental Accounts Committee and Public Accounts Committee;
- xxii) Determining the need for outsourcing/co-sourcing of any internal audit activity(ies) or other assignment(s) within the IAC and submitting a formal proposal to the PAO.

8. Authority of Internal Audit Cells

The IACs shall be authorised to:

- i) Have unrestricted access to the Department's books and records (including confidential records and information), functions, property, facilities and personnel;
- ii) Consult with and seek any information it requires from any employee and all employees shall be required to cooperate with any request made by the IAC in the course of its duties;
- iii) Conduct any examination within the scope of this policy or as assigned by the PAO;
- iv) Examine and audit any activity of the Department within all the controlling offices including autonomous bodies, public sector entities, projects etc;

- v) Access minutes of relevant consultative and decision-making bodies/ committees of the Department;
- vi) Set frequencies, select subjects and apply techniques required to accomplish audit objectives;
- vii) Seek to obtain necessary assistance from outside sources while carrying out responsibilities under this policy; and
- viii) Monitoring, taking follow-up action and evaluating corrective actions taken by auditee.

The IAC shall not have the authority to:

- i) Perform any operational duties for the Department or its affiliates;
- ii) Initiate or approve accounting transactions external to the IAC;
- iii) Direct the activities of any employee of the Department, not employed by the IAC; and
- iv) Assume a role other than in an advisory capacity in the design, installation or operation of control procedures.

9. Audit Execution and Reporting Cycle

General audit planning: The Head of the IAC shall develop a strategic risk-based plan to determine the priorities of internal audit activity, consistent with the organisation's goals. The Head shall submit the periodic audit plan to the Secretary/PAO.

Approval: The Head of the IAC shall communicate the Internal Audit Plan and resource requirements, including significant interim changes to the Secretary/PAO for review and approval. The Secretary/PAO may approve the plan with or without amendments.

Intimation Letter: Upon approval of the Audit Plan, the Head of the IAC shall intimate the auditee/DDO vide a letter that Internal Audit of the entity has been scheduled.

Initial/Opening meeting: In order to proceed further with audit fieldwork phase and to understand the entity's business, the Head of the IAC shall hold an opening meeting with the auditee to formally discuss the scope of the audit, its objectives and procedures.

Fieldwork: The Internal Audit team shall perform fieldwork in order to obtain and record relevant, reliable, sufficient and convincing audit evidence to support their audit findings, conclusions and recommendations. The Internal Audit team shall be responsible for reporting to the Head of the IAC.

Closing Meeting/Draft Report to the Auditee: Within seven (07) days of the completion of the fieldwork, the Head of the IAC shall write a draft Internal Audit report and provide the auditee with an opportunity for review and discussion.

The auditee shall provide their reply /comments within 14 days of receipt of the formal draft. In case of failure in timely reply of the auditee, the Head of the IAC shall inform the Secretary/PAO. If the reply of the auditee is not received within 30 days thereof, the Head of the IAC, without further waiting, shall submit the report to the Secretary/PAO for appropriate action.

Final Internal Audit Report: After compilation of internal audit findings and management responses thereof, the Head of the IAC shall, within fourteen (14) days thereof, submit the final report to the respective Secretary/ PAO. The Secretary may issue directions directly to the auditee or may require the Head of the IAC to take necessary action(s).

The Secretary/PAO may himself/ herself follow up or assign to any other officer(s) for follow-up action on the recommendations involving other Government entities external to his/ her Department. Follow-up of Internal Audit Report: The Head of the IAC shall be responsible for the verification of compliance/actions taken in the light of directions issued by the Secretary/ PAO and reporting back. The Head the IAC shall prepare quarterly internal audit progress reports and submit to the Secretary/PAO with a copy endorsed to the PCIA at Finance Department.

Follow-up of Internal Audit Report: The Head of the IAC shall be responsible for the verification of compliance/actions taken in the light of directions issued by the Secretary/ PAO and reporting back.

The Head the IAC shall prepare quarterly internal audit progress reports and submit to the Secretary/PAO with a copy endorsed to the PCIA at Finance Department.

10. Accountability

The Head of an IAC and his/ her staff, in the discharge of their duties and functions shall be accountable to the Secretary/ PAO.

They shall submit an assessment of the adequacy and effectiveness of the Department/ organisation's processes for controlling its activities and managing its risks in all the core and non-core areas of operations on periodic basis.

In addition, they shall report significant issues related to the processes for controlling the activities of the Department and its affiliates, together with recommendations for improvements to those processes. Furthermore, they shall provide information on the status and results of annual audit plan on quarterly basis under intimation to the PCIA.

11. Quality Control Review

On an annual basis or as and when required, for appropriate audit assignments, the PIAC shall conduct quality control review (QCR) in order to ensure that internal audit activities are being performed in accordance with the professional standards, regulatory and legal requirements.

12. Formulation and Review of Policies and Procedures

The PIAC shall prescribe and review policies and procedures, including Internal Audit Manual framed under this policy, and ethical requirements (integrity, objectivity, confidentiality, professional behaviour, competence and due care) subject to consultation with all stakeholder departments/ organisations across the Province.

13. Human Resource Management

The Finance Department shall, in consultation with the Establishment Department, lay down the qualifications and recruitment procedure for providing human resource to the PIAC and IACs. All appointments shall be made on open merit/contract basis and for a specified period on market-based salary. The market-based salary package shall be approved by the Chief Minister. Civil Servants may apply for the posts advertised in the IACs with prior permission from their parent department. The vacant posts can be filled through transfer of Civil Servants till the hiring of regular staff. The number of personnel shall be determined by the Finance Department provided that one Cell may be assigned additional audit staff, if so warranted by the workload. Positions of interns in the Cells shall be created and offered to fresh graduates.

14. Commencement Date of the Policy

The Policy will come into force from the date of its notification.

