
INTERNAL AUDIT CHARTER

(December 2020)

1. General

- 1.1 The Internal Audit Charter is a formal document that defines the Internal Audit role, authority and responsibility. The Charter establishes Internal Audit's position within the Scottish Water Group and defines the scope of Internal Audit activities. Approval of the Internal Audit Charter rests with the Audit Committee and will be sought on an annual basis.
- 1.2 The purpose of Scottish Water's Internal Audit function is to provide an independent, objective assurance function designed to add value and improve the organisation's operations, processes and controls. The mission of Internal Audit is to enhance and protect organisational value by providing risk based and objective assurance, advice and insight. Internal Audit helps the Scottish Water Group accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of control, risk management and governance processes. Internal Audit activities will be carried out in compliance with the Public Sector Internal Audit Standards, and general auditing standards, and this Charter recognises the mandatory nature of the 'Definition of Internal Auditing', the 'Code of Ethics' and the 'Standards' defined in the standards.
- 1.3 Internal Audit, as part of the 3rd line of defence, is responsible, to the Audit Committee, for providing assurance that significant strategic, financial, operational, and compliance risks are effectively controlled by management. It is a review activity which does not in any way relieve management of their responsibility for establishing and maintaining effective control.

2. Authority

- 2.1 There are no restrictions placed on the scope of Internal Audit's work. For the purpose of its work, Internal Audit has unrestricted access at all reasonable times to all the records, personnel, property, operations and activities of the Scottish Water Group, including those maintained on its behalf by Third-Party Service Providers (where relevant).
- 2.2 All employees (including Directors, contingent workers and contractors) working for or on behalf of Scottish Water Group are required to assist Internal Audit in fulfilling its roles and responsibilities.
- 2.3 Internal Audit reports to the Scottish Water Audit Committee, with functional line management provided by the Scottish Water Finance Director. To ensure that Internal Audit activities are free from interference in determining the scope of internal audits, performing work and communicating results, the Head of Internal Audit has a right of direct access to the Audit Committee Chairman, the Board Chairman and the Chief Executive. The Head of Internal Audit will exercise these rights of access in an appropriate manner.
- 2.4 To establish, maintain, and assure that Internal Audit has sufficient authority to fulfil its duties, the Audit Committee will :
 - Approve the Internal Audit Charter.
 - Approve the risk based Internal Audit Strategic and Annual Audit Plans.
 - Receive communications from the Head of Internal Audit on the department's performance relative to its plan and other matters.
 - Approve decisions regarding the appointment and removal of the Head of Internal Audit.
 - Make appropriate enquiries of management and the Head of Internal Audit to determine whether there is inappropriate scope or resource limitations.
 - Hold an annual private meeting with the Head of Internal Audit.

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- 2.5 The Audit Committee reviews the scope and nature of the work of Internal Audit. It receives reports at each meeting setting out Internal Audit progress in delivery of the Internal Audit plan approved by the Audit Committee and the executive summary of individual audit reports, including an independent assessment of controls in each area reviewed and details of the issues identified together with the actions agreed with management.

3. Independence

- 3.1 Internal Audit does not perform operational tasks as this would impair its objectivity and neither has it any direct responsibility for, nor authority over, the business activities it reviews. The independence of Internal Audit is assured by its reporting lines.
- 3.2 The Head of Internal Audit and Internal Audit staff are required to comply with Scottish Water's Code of Ethical Conduct, all other corporate policies and regulations of their respective professional bodies.
- 3.3 For the purposes of this Charter, the role of the Board is delegated to the Audit Committee which is the Board sub-committee charged with responsibility for approving the Internal Audit Plan and receiving the findings of Internal Audit work. Where necessary, the Audit Committee will escalate the findings from Internal Audit reports to the Board.

4. Planning and Reporting

- 4.1 The Head of Internal Audit is responsible for developing the Internal Audit Strategic and Annual Audit Plans by reference to the business process audit universe and on the basis of risks identified by the business risk assessment process (including stress testing completed to support the viability statement and highest scored risks in Corporate Risk Register), previous audit findings, experience and changes in the underlying systems of internal control.
- 4.2 The Audit Plans, and the resources to deliver these, are subject to annual approval by the Audit Committee. Any significant changes to the Annual Audit Plan required during the year are reported to the Audit Committee, at the earliest opportunity, for their consideration and approval. Also, progress in delivery of the Audit Plan will be regularly reported to the Audit Committee during the year.
- 4.3 The Strategic Internal Audit Plan will be prepared with input from management. It will be risk based and will have regard to the business plans, strategic direction and vision of the Scottish Water Group as a whole. The Annual Internal Audit Plan will then be developed with reference to the Strategic Internal Audit plan.
- 4.4 Internal Audit will report the findings of its work, including opportunities for improving the efficiency of control, risk management and governance processes, by means of reports to the appropriate operational management, the Chief Executive, the Finance Director, members of the ELT and the Audit Committee. All reports will be copied to the External Auditors.

5. Resources

- 5.1 Internal Audit work is delivered by an in-house team. When required, this is supplemented by additional resources from the business, secondments and external specialist firms. Any external resources engaged will be required to comply with the principles of this Charter.
- 5.2 The Head of Internal Audit is required to have a professional accountancy and/or internal audit qualification and appropriate experience. Internal Audit Team members are also required to have appropriate qualifications and/or experience.

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- 5.3 All professionally qualified staff are required, as per the relevant professional body, to comply with Continued Professional Development (CPD) requirements to ensure they maintain and enhance their knowledge, skills and audit competencies.
- 5.4 The Head of Internal Audit also coordinates activities, where possible, and considers relying upon the work of other internal and external assurance and consulting service providers, as needed.
- 5.5 Internal Audit may perform advisory activities, the nature and scope of which will be agreed with management, provided Internal Audit does not assume management responsibility and there is no potential conflict of interest.

6. Responsibilities

- 6.1 In all contacts, Internal Audit staff and employees will treat each other with respect, courtesy, politeness and professionalism. Any confidential or sensitive issues raised with or reported to Internal Audit will be dealt with in an appropriate manner.
- 6.2 It is management's responsibility to determine and maintain the system of internal controls. The internal control system comprises the whole network of systems established in Scottish Water to provide reasonable assurance that business objectives will be achieved. Also, management has primary responsibility for resolving all issues reported by Internal Audit, in the manner and within the timescales agreed in Internal Audit reports.
- 6.3 Internal Audit will, in the undertaking of individual audits, provide assurance to the Audit Committee and management that :
- Internal control systems (including computer systems), risk management and governance processes are adequate and functioning efficiently and effectively.
 - Corporate assets are being safeguarded.
 - Policies and procedures established by management are complied with, are appropriate in current circumstances and are not wasteful.
 - Information furnished to management in connection with the decision making process is reliable.
- 6.4 Internal Audit will, in the undertaking of individual audits, draw the attention of the Audit Committee and management to :
- Deficiencies in the systems of control, risk management and governance.
 - Instances of duplicated functions, excessive checking, wastage and other inefficiencies.
 - Potential reputational risks.
- 6.5 Internal Audit will, through effective followup procedures, monitor and report progress in implementation of all actions agreed during audits to the Audit Committee and management.
- 6.6 In addition, Internal Audit will :
- Provide an annual opinion and report, including an opinion on the overall adequacy and effectiveness of control, risk management and governance processes.
 - Complete fraud related investigations, as required, in compliance with its responsibilities defined in the Fraud Management and Response Policy.
 - Be primary recipient of all reports from the external whistleblowing line.
 - Provide advice, guidance and assistance, relating to controls, risk management and governance, sometimes through specific reviews or involvement in projects, as requested by the Audit Committee or management.
 - Have membership of and provide support in the activities of the Business Ethics Committee.

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- Support Scottish Water participation in the National Fraud Initiative run by Audit Scotland, including investigation of reported matches.
 - Ensure trends, emerging issues and common audit themes that could impact Scottish Water are considered and communicated to management and the Audit Committee, as appropriate.

6.7 Internal Audit staff will treat as confidential and appropriately label and store all information obtained in carrying out their duties. Internal Audit will not disclose any information held unless there is a business need, it is appropriately authorised or there is a legal or professional requirement to do so.

7. Quality Assurance and Improvement Programme

7.1 Internal Audit will maintain a quality assurance and improvement programme that covers all aspects of the Internal Audit department. The programme will include an evaluation of Internal Audit's conformance with the Public Sector Internal Audit Standards and an evaluation of whether Internal Auditors apply the Code of Ethics. The programme will also assess the efficiency and effectiveness of Internal Audit and identify opportunities for improvement.

7.2 The Head of Internal Audit will communicate to senior management and the Audit Committee on Internal Audit's quality assurance and improvement programme, including results of internal assessments and external assessments, conducted at least once every five years by an external qualified, independent assessor or assessment team.

8. Operating Framework

8.1 All Internal Audit reviews are completed in accordance with the approach and standards defined within the Scottish Water Group Internal Audit Manual. The Manual incorporates details of the Internal Audit professional ethics and standards, strategic planning process, approach to process risk based audits, followup of agreed actions and sundry administration matters. Further details are included in appendix 1.

8.2 Internal Audit will maintain close working relationships with the External Auditors, including sharing of the Annual Audit Plan, in order to compliment the work of each other and to avoid any unnecessary duplication of work.

9. Key Performance Indicators

9.1 To assist the Audit Committee in assessing the performance of Internal Audit, a set of Key Performance Indicators have been defined and were previously approved by the Audit Committee. Performance against these KPI is included in the Quarterly Internal Audit reports and/or the Annual Internal Audit report tabled at the Audit Committee. Details of the KPI and targets are included in appendix 2.

Appendix 1 – Internal Audit Manual

The Internal Audit Manual contents are as follows :

Overview

Introduction
Scottish Water Group
Scottish Water Vision
Internal Audit Role and Objectives
Internal Audit Approach and Scope
Conduct of Internal Audit Work
References
Maintenance of the Manual
Resource

Charter, Ethics and Standards

Internal Audit Charter
Internal Audit Code of Ethics
Internal Audit Standards
Audit Committee Terms of Reference
Fraud Management & Whistleblowing
Bribery Act
Competition Act – Retail Market Requirements

Strategic Audit Planning

Introduction
Integrated Assurance Capability
Audit Planning Methodology
Audit Issue Rating & Overall Control Assessment

Risk Based Process Auditing

Audit Process
Audit File Structure and Documentation
Audit Sampling
Review and Quality Control
Agreed Action Tracking – Evidence Documentation and Re-testing Requirements

Internal Audit Administration

Agreed Action Tracking
Standard Templates
Safety, Health & Wellbeing
Training and Development
Document Version Control
Document Retention and Archiving

Appendix 2 – Internal Audit KPI

KPI Area	Measure	Target
Delivery	(i) Delivery of approved Annual Audit Plan.	100%
	(ii) Overall staff productive time.	90% or higher.
	(iii) Production of draft and final reports by target dates within Terms of Reference.	90% or higher.
	(iv) Issues included in draft reports are included in final reports.	Measure (not target) - 90% or higher.
	(v) Initial followup of management agreed actions within 2 weeks of due date.	100%
Service	(i) Audit Committee approval of Annual Internal Audit Plan.	No major changes to draft Internal Audit Plan.
	(ii) Annual review of Internal Audit by Audit Committee.	No major issues raised.
	(iii) Internal customer service survey.	A new corporate process for internal customer surveys is being sourced. Once implemented, a target will be agreed with the Audit Committee.
Staff	(i) Your Voice surveys.	Match or exceed Scottish Water average scores.
	(ii) Sickness absence levels.	Below Scottish Water average.
	(iii) Completion of professional CPD requirements.	100%
	(iv) Staffing levels maintained at agreed level.	100%
Financial	Full year costs within annual agreed budget.	Total costs (after recharges) equal or below agreed budget.
Safety, Health & Wellbeing	Lost time accidents and near misses.	Zero per year
	Completion of office based staff S,H&W training.	100%
Engagement	Quarterly meetings with Chair of Audit Committee.	4 per year
	Attendance at Audit Committee meetings.	100%
	Private meeting with Audit Committee.	At least once a year.
	Quarterly meeting with Chief Executive.	4 per year