



Leeds
CITY COUNCIL

**Strategy and Resources Directorate
Audit and Investment
Internal Audit**

**Internal Audit Charter
May 2015**

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Executive Summary – Internal Audit Charter

- This document is the Internal Audit Charter for Leeds City Council (LCC) Internal Audit Service.
- The Public Sector Internal Audit Standards (PSIAS) came into force on 1 April 2013. These are the first internal audit standards to apply across the whole public sector.
- The PSIAS is supported by the Chartered Institute of Public Finance and Accountancy (CIPFA) Local Government Application Note (April 2013.)
- The unified standards intend to ensure sound corporate governance and set out roles and responsibilities with regard to the delivery of internal audit services. The PSIAS require an Internal Audit Charter to be in place which will be reviewed periodically and presented to the Corporate Governance and Audit Committee for approval.
- This Charter sets out the purpose, authority and responsibility of the Council's Internal Audit function, in accordance with the PSIAS.
- The main objective of Internal Audit is to provide, in terms of the PSIAS, a high quality, independent audit service to the Council which provides annual assurance in relation to internal control and overall governance arrangements.
- The PSIAS recognises that Internal Audit's remit extends to the entire control environment of the organisation and not just financial controls.

1. Background

- 1.1 Prior to 1 April 2013, Internal Audit operated in accordance with the Code of Practice for Internal Audit in Local Government in the UK which was issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) in 2006. A requirement of the Code of Practice was the preparation of a “terms of reference” document by each Internal Audit Section; this set out the purpose, authority and responsibility of Internal Audit.
- 1.2 The Public Sector Internal Audit Standards (PSIAS) came into force on 1 April 2013. These are the first Internal Audit standards to apply across the whole public sector. The Standards are issued by the Relevant Internal Audit Standard Setters (RIASS) including CIPFA in respect of local government across the UK.
- 1.3 The PSIAS requires that an Internal Audit Charter is in place for each local authority. The Charter must be consistent with the Definition of Internal Auditing, the Code of Ethics and the Standards contained in the PSIAS.
- 1.4 This Internal Audit Charter has been drawn up in line with the PSIAS requirements and is further informed by the CIPFA Local Government Application Note (April 2013) published to assist in the implementation of the PSIAS.
- 1.5 This Internal Audit Charter replaces all previous Internal Audit Terms of Reference.
- 1.6 This Internal Audit Charter is subject to approval by the Corporate Governance and Audit Committee of Leeds City Council on an annual basis, in line with PSIAS requirements.

2. PSIAS Requirements

- 2.1 The PSIAS requires the Internal Audit Charter to reflect the following points (if further clarification is required, reference to the details is shown below):
 - a. Recognise the mandatory nature of the PSIAS (specifically the Definition of Internal Auditing, Code of Ethics and the Standards) [paragraphs 6.1/Appendix 1.]
 - b. Define the terms ‘Chief Audit Executive’, ‘Board’ and ‘Senior Management’ for the purposes of internal audit activity. Definitions for Leeds City Council are noted below in respect of key duties outlined in the PSIAS. As in CIPFA Application Note guidance, the authority will decide for each occurrence which committee/group/individual best fits the role in that situation, considering the need to preserve Internal Audit’s independence and objectivity [sections 3 – 5.]
 - c. Set out the responsibility of the ‘Board’ and also of the statutory officers with regard to Internal Audit as defined in the Council’s Financial Regulations.

- d. Establish responsibilities and objectives of Internal Audit [section 7.]
- e. Define the scope of Internal Audit activities [section 8.]
- f. Defines the nature of consulting services [section 9.]
- g. Cover the arrangements for appropriate resourcing [section 10.]
- h. Establish the organisational independence of Internal Audit [section 11.]
- i. Establish the accountability, reporting lines and relationships between the Chief Audit Executive (CAE) and:
 - The Board
 - Those to whom the CAE must report functionally
 - Those to whom the CAE may report administratively [paragraph 11.3.]
- j. Include arrangements for avoiding conflicts of interest if internal audit undertakes non-audit activities [paragraph 11.4.]
- k. Set out the arrangements that exist within the organisation's anti-fraud and anti-corruption policies, requiring the CAE to be notified of all suspected or detected fraud, corruption or impropriety, to inform his or her annual internal audit opinion and the risk-based plan [section 14.]
- l. Define the role of internal audit in any fraud-related work [section 14.]
- m. Recognise that internal audit's remit extends to the entire control environment of the organisation and not just financial controls [section 8.]
- n. Establish internal audit's right of access to all records, assets, personnel and premises, including those of partner organisations where appropriate, and its authority to obtain such information and explanations as it considers necessary to fulfil its responsibilities [section 15.]

3. Definition of the Chief Audit Executive (CAE)

- 3.1 Chief Audit Executive describes a person in a senior position responsible for effectively managing the internal audit activity in accordance with the internal audit charter and the *PSIAS Definition of Internal Auditing*, the *Code of Ethics* and the *Standards*. Within Leeds City Council the Head of Internal Audit is the designated 'Chief Audit Executive'

4. Definition of the Board

- 4.1 The PSIAS lays out the role of a Board in relation to specific standards. In a local authority the role of the Board may be satisfied by an Audit Committee. In Leeds City Council the Corporate Governance and Audit Committee fulfils the role of an audit committee and, for the purposes of the key duties laid out in the PSIAS, is the Board.
- 4.2 The key duties of the Board as laid out in the PSIAS are as follows:
- Approve the Internal Audit charter (Standard 1000);
 - Approve the risk based Internal Audit plan including the approval of the Internal Audit budget and resource plan (Standard 1110);
 - Receive communications from the Head of Internal Audit on internal audit's performance relative to its plan and other matters (Standard 2020);
 - Receive an annual confirmation from the Head of Internal Audit with regard to the organisational independence of the internal audit activity (Standard 1110);
 - Receive the results of the Quality Assurance and Improvement Programme from the Head of Internal Audit (Standard 1320);
 - Make appropriate enquiries of the management and the Head of Internal Audit to determine whether there are inappropriate scope or resource limitations.

5. Definition of Senior Management

- 5.1 The PSIAS anticipates the role of Senior Management includes the following:
- Input to the risk based Internal Audit plan (Standard 2010);
 - Receive periodic reports from the Head of Internal Audit on internal audit activity (Standard 2060); that includes follow up reports (Standard 2500);
 - Receive the results of the Quality Assurance and Improvement Programme from the Head of Internal Audit (Standard 1320.)
- 5.2 Within Leeds City Council 'Senior Management' is defined as the Section 151 Officer (Deputy Chief Executive.)

6. Definition of Internal Audit

- 6.1 Leeds City Council has adopted the PSIAS definition of internal auditing as follows:

"Internal Auditing is 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."

7. Purpose, Responsibilities and Objectives of Internal Audit

7.1 Internal Audit is an independent appraisal function established within the authority – as part of the Strategy and Resources Directorate - with the following objectives¹:

- To provide an effective Internal Audit Service, on behalf of the Deputy Chief Executive, in line with legislation and the appropriate audit standards;
- To provide an independent, objective assurance and consulting activity designed to add value and improve the organisation’s operations;
- To help the organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.

7.2 It is the responsibility of the Head of Internal Audit to provide an independent and objective opinion on the overall adequacy and effectiveness of the Council’s framework of governance, risk management and control.

7.3 The Head of Internal Audit reports to the Corporate Governance and Audit Committee on a regular basis in line with the agreed work programme for the Committee. There are a number of standard items reported including the annual Internal Audit plan, an annual opinion on the control environment and regular updates on reports issued. The Head of Internal Audit’s annual report is presented to those charged with governance and should be used to support the Council’s Annual Governance Statement.

7.4 Internal Audit employees will ensure that they conduct work with due professional care and in line with the requirements of the PSIAS and any other relevant professional standards.

7.5 Internal auditors will treat as confidential the information they receive in carrying out their duties. There must not be any authorised disclosure of information unless there is a legal or professional requirement to do so. Confidential information gained in the course of an audit will not be used to effect personal gain.

8. Scope of Internal Audit Activities

8.1 The scope for Internal Audit is the control environment comprising risk management, control and governance. This effectively includes all of the council’s operations, resources, services and responsibilities in relation to other bodies. This description shows the wide potential scope of Internal Audit. In order to translate this description into individual audit reviews, a risk assessment methodology is applied that allows high-risk review areas to be prioritised (also see Section 10.)

¹ Financial Regulations – Section 19 ‘Internal Audit’

8.2 To enable Internal Audit to meet its objectives, it will undertake work within a scope of activities including:

- review of controls within existing systems and systems under development
- compliance with policies and procedures including Financial Regulations
- transactions testing to ensure accuracy of processing
- contract audit
- establishment reviews
- computer audit including data analytics
- anti-fraud work
- investigation of suspected fraud and irregularities
- value for money reviews and transactions testing
- provision of advice to Directorates and establishments including consulting services
- provision of audit services to external clients.

8.3 All Internal Audit work is undertaken in accordance with internal quality procedures incorporated in its quality management system, which has now been ISO accredited for over fifteen years, having first been awarded in 1998. Independent reviews are undertaken on Internal Audit twice yearly by an external organisation to ensure compliance with the ISO standard.

9. Definition of Consulting Services

9.1 The PSIAS defines consulting services as follows: *“Advisory and client related 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.”*

9.2 The PSIAS requires that approval must be sought from the Board for any significant additional consulting services not already included in the audit plan, prior to accepting the engagement (Standard 1130.) Within Leeds City Council significant is defined as any single assignment equivalent to 5% of annual planned days; these will be brought to the Corporate Governance and Audit Committee for approval.

10. Arrangements for Appropriate Resourcing

10.1 As stated in the CIPFA Application Note, “No formula exists that can be applied to determine internal audit coverage needs. However, as a guide, the minimum level of coverage is that required to give an annual evidence-based opinion. Local factors within each organisation will determine this minimum level of coverage.”

10.2 The annual audit plan lays out the planned audit resources for the year with the objective of giving an evidence-based opinion.

- 10.3 Internal Audit must be appropriately staffed in terms of numbers, grades, qualification levels and experience, having regard to its objectives and to the standards. Internal Auditors need to be properly trained to fulfil their responsibilities and should maintain their professional competence through an appropriate on-going development programme.
- 10.4 In the event that the risk assessment, carried out to prepare the annual plan, identifies a need for more audit work than there are resources available, the Head of Internal Audit will identify the shortfall and advise the Chief Officer (Financial Services) and the Deputy Chief Executive followed by the Corporate Governance and Audit Committee as required to assess the associated risks or to recommend additional resources are identified.
- 10.5 The audit plan will include a contingency allocation to address unplanned work including responding to specific control issues highlighted by senior management during the year.
- 10.6 Internal audit work is prioritised according to risk, through the judgement of the Head of Internal Audit, informed by the Council's risk registers and in consultation with senior management and External Audit.
- 10.7 Internal audit activity is subject to annual review by External Audit.
- 10.8 Achievement of the annual plan is reported to Corporate Governance and Audit Committee on a regular basis throughout the year. Should circumstances arise, during the year, that resources fall or appear to be falling below the minimum level required to provide an annual evidence based opinion the Head of Internal Audit will advise the Chief Officer (Financial Services), the Deputy Chief Executive and the Corporate Governance and Audit Committee.

11. Organisational Independence of Internal Audit

- 11.1 The PSIAS requires that reporting and management arrangements must be put in place that preserve the Head of Internal Audit's independence and objectivity, in particular with regard to the principle that the Head of Internal Audit must be independent of the audited activities.
- 11.2 PSIAS Standard 1110 requires that the Head of Internal Audit to report to a level within the organisation that allows the internal audit activity to fulfil its responsibilities and reporting to the Board is the generally accepted method of helping to ensure that organisation independence is attained. The Head of Internal Audit reports directly to the Corporate Governance and Audit Committee within Leeds City Council.
- 11.3 CIPFA and the Chartered Institute of Internal Auditors expect that the Head of Internal Audit should report to at least corporate management team level. Within Leeds City Council, the Head of Internal Audit reports to the Chief Officer (Financial

Services) who in turn reports to the Deputy Chief Executive. In addition, the Head of Audit is able to report without fear or favour in their own name to the Chief Executive, the Executive Board, the Corporate Governance and Audit Committee, and the Scrutiny Function². Reports can also be made to the Corporate Leadership Team.

- 11.4 The Internal Audit team will ensure that independence and objectivity are maintained in line with the PSIAS including where non-audit work is undertaken. To manage potential conflicts of interest, internal auditors have no operational responsibilities and any independence issues are highlighted at the planning stage for individual audit assignments.
- 11.5 If independence or objectivity is impaired in fact or appearance, the details of the impairment must be disclosed in the first instance to Head of Internal Audit and reported to Corporate Governance and Audit Committee and/or Section 151 officer as appropriate.
- 11.6 Internal Audit will have no executive responsibilities. It is not an extension of, or a substitute for, the function of management. Responsibility for internal control rests fully with managers, who should ensure that arrangements are appropriate and adequate. It is for management to accept and implement audit recommendations or to accept the risk resulting from not taking any action.
- 11.7 The Head of Internal Audit will confirm to the Corporate Governance and Audit Committee on an annual basis, within the Annual Report, the organisational independence of the Internal Audit Service.

12. Planning

- 12.1 The annual audit plan will be submitted to the Corporate Governance and Audit Committee at the beginning of the financial year for approval. The plan will be compiled following consultation with the Deputy Chief Executive, the Chief Officer (Financial Services) and individual Directors and Heads of Finance as appropriate and is documented in the audit plan methodology.
- 12.2 The risk-based plan will outline the audit assignments to be carried out.
- 12.3 The audit plan is dynamic in nature and will be reviewed and realigned on a regular basis to take account of new, emerging and changing risks and priorities. It will be based on a risk assessment that covers financial materiality and business risks as well as any suspected or detected fraud, corruption or impropriety that has come to the attention of the Head of Internal Audit under their remit as laid out in the Council's Policy Statement on Fraud and Corruption, Whistleblowing Policy, Anti-Bribery Policy and Anti-Money Laundering Policy. It will be responsive, containing an element of

² Financial Regulations – Section 19 'Internal Audit'

contingency to accommodate assignments which could not have been reasonably foreseen.

- 12.4 Internal Audit will consult with the Council's external auditor and with other relevant inspection and review bodies, as required, in order to co-ordinate effort and avoid duplication.
- 12.5 As part of the planning process, the Head of Internal Audit will identify other potential sources of assurance and will include in the risk based plan the approach to using other sources of assurance and any work required to place reliance upon those other sources.
- 12.6 The plan is prepared based on assurance blocks that each give an opinion on the key control environment elements, targeted towards in year risks.
- 12.7 For each audit assignment, Internal Auditors will develop and document a plan including the objectives of the review, the scope, timing and resource allocations. In planning the assignment, auditors will consider, in conjunction with the auditees, the objectives of the activity being reviewed, significant risks to the activity and the adequacy and effectiveness of the activity's governance, risk management and control processes.

13. Reporting and Follow Up

- 13.1 A written report will be prepared by the appropriate auditor for every audit review and distributed in line with established and agreed reporting protocols. This will include an opinion on the adequacy of controls in the area that has been audited.
- 13.2 The draft report will be discussed with the auditees and a response obtained for each recommendation stating their response to each recommendation along with a timescale for implementation. The final report will include the management responses and will be issued to the relevant Director and other officers in line with directorate protocols.
- 13.3 Any reports where limited or no assurance has been provided for the control environment and/or compliance with the control environment will be subject to a follow up review to determine whether the recommendations made have been implemented.
- 13.4 Regular update reports to Corporate Governance and Audit Committee will show the activity of the Internal Audit Section, progress achieved against plan and a summary of significant audit findings.

- 13.5 The annual report will incorporate the annual opinion, a summary of the audit work that supports the opinion and a statement on conformance with the PSIAS and the results of the Quality Assessment and Improvement Programme (QAIP.)
- 13.6 The PSIAS also requires the Head of Internal Audit to establish a follow up process to monitor and ensure actions have been effectively implemented. This is an established process within Leeds City Council with a follow up review being undertaken on any assignments with limited assurance/no assurance to ensure recommendations have been adopted and suggested controls are working well in practice.

14. Assurances to external organisations

- 14.1 The format and scope of any assurances provided to external organisations will be agreed in advance with the recipient organisation and will be documented in contract terms/service level agreement or equivalent. The work carried out to provide such assurances will be conducted in accordance with Internal Audit's quality procedures and service standards. These will be included in the annual audit plan.

15. Fraud and Corruption

- 15.1 Managing the risk of fraud and corruption is the responsibility of management; Internal Audit will assist management in the effective discharge of this responsibility.
- 15.2 Audit procedures alone, even when performed with due professional care, cannot guarantee that fraud or corruption will be detected. Internal Audit does not have the responsibility for the prevention or detection of fraud and corruption. Internal Audit will, however, be alert in all their work to risks and exposures that could allow fraud and corruption.
- 15.3 In line with Financial Regulations (Section 18 - Fraud and Corruption), whenever any matter arises that involves, or is thought to involve irregularities concerning cash, stores or other property of the council or any suspected irregularity in the exercise of the functions of the council, including bequests, trust and client monies, it must be immediately brought to the attention of the respective Director. Where the irregularity is thought to involve fraud, corruption or impropriety the Director must ensure that the matter is reported to the Head of Internal Audit. If the irregularity or suspected irregularity involves theft or suspected theft of assets, it must also be referred to the Police. In addition where a break-in is suspected, the Police must be informed immediately.

16. Authority of Internal Audit

16.1 Internal Audit is a statutory requirement in local government. The Accounts and Audit (England) Regulations 2015 which came into force on the 1st April 2015 state that:

5.—(1) A relevant authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance.

(2) Any officer or member of a relevant authority must, if required to do so for the purposes of the internal audit—

(a) make available such documents and records; and

(b) supply such information and explanations;

as are considered necessary by those conducting the internal audit.

(3) In this regulation “documents and records” includes information recorded in an electronic form.

16.2 The statutory role is recognised and endorsed within the Council’s Financial Regulations (Section 19 - Internal Audit), which provides the authority for access as follows:

Directors must ensure that Internal Audit is allowed to:

(a) Enter any council premises or land at all reasonable times:

(b) Access all records, documents, data held on computer media, and correspondence relating to all transactions of the council, or unofficial funds operated by an employee as part of their duties:

(c) Receive such explanations as are necessary concerning any matter under examination.

(d) Require any employee of the council to produce cash, stores or any other property under their control, belonging to the council or held as part of the employee’s duties.

17. Code of Ethics

17.1 All our Internal Auditors must conform to the Code of Ethics (see Appendix 1.) The code promotes an ethical culture in a profession founded on the trust placed in its objective assurance about risk management, control and governance.

17.2 The Code of Ethics includes 2 essential components – the Principles and Rules of Conduct (which are an aid to interpreting the Principles into practical applications.)

17.3 Internal Auditors will adhere to LCC relevant policies and procedures (including the Employee Code of Conduct) and the LCC Internal Audit Quality Procedures Manual.

- 17.4 All Internal Auditors will hold a professional qualification or be training towards a professional qualification.
- 17.5 In addition, all internal auditors have a personal responsibility to undertake a programme of continuing professional development (CPD) to maintain and develop their competence. This is fulfilled through the requirements set by professional bodies and through the Council's appraisal and development programme.

18. Review of the Effectiveness of Internal Audit

- 18.1 The Accounts and Audit (England) Regulations 2011 required councils to conduct, at least once a year, a review of the effectiveness of its internal audit. Within Leeds City Council, the internal audit annual report and opinion provides an overview of the work and performance of Internal Audit throughout each year. The annual report, along with independent reviews by the external auditors, provides an assurance of the effectiveness of the Internal Audit service during the year.
- 18.2 These 2011 regulations have now been superseded by the Accounts and Audit Regulations 2015 which maintain the requirement for an effective internal audit function and state that:

*A relevant authority must, each financial year—
(a) conduct a review of the effectiveness of the system of internal control*

- 18.3 Internal Audit will continue to provide assurance on the effectiveness of the function through the annual reporting process.

19. Quality Assurance and Improvement Programme (QAIP)

- 19.1 The PSIAS requires that a quality assurance framework be established, which will include both internal and external assessment of the work of Internal Audit.
- 19.2 The Head of Internal Audit is responsible for providing periodically an internal quality assessment (IQA) on the internal audit activity as regards its consistency with the requirements of the PSIAS. This will be carried out through annual self-assessment using the checklist in the CIPFA Application Note. Results of these IQAs will be communicated to the Chief Officer (Financial Services), the Deputy Chief Executive and the Corporate Governance and Audit Committee.
- 19.3 Internal Audit issues a customer satisfaction questionnaire following each audit assignment. The results are used to determine areas for improvement and inform the continuing personal development training programme for Internal Audit staff. The results are also benchmarked with other core cities who have adopted the same questionnaire.

- 19.4 External quality assessments (EQAs) will be conducted at least once every five years and may be a full external assessment or a self-assessment within independent validation in line with the PSIAS. These reviews will be commissioned in line with the PSIAS and will be agreed by the Corporate Governance and Audit Committee with outputs reported to the Committee by the Head of Internal Audit.
- 19.5 The Head of Internal Audit will continue to report the results of External Audit reviews to the Corporate Governance and Audit Committee.

Appendix 1 – Code of Ethics

- 1.1 A Code of Ethics is necessary for the profession of internal auditing as trust is placed on its objective assurance about risk management, control and governance.
- 1.2 The PSIAS sets out a Code of Ethics around 4 principles which Internal Audit will adhere to. The 4 principles are: **Integrity, Objectivity, Confidentiality** and **Competency**.

2. Integrity

The principle - The integrity of internal auditors establishes trust and this provides the basis for reliance on their judgement.

Rules of Conduct - Internal auditors:

- Shall perform their work with honesty, diligence and responsibility;
- Shall observe the law and make disclosures expected by the law and the profession;
- Shall not knowingly be a party to an illegal activity, or engage in acts that are discreditable to the profession of internal auditing or to the organisation;
- Shall respect and contribute to the legitimate and ethical objectives of the organisation.

3. Objectivity

The principle – Internal auditors exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the activity or process being examined. Internal auditors make a balanced assessment of all the relevant circumstances and are not unduly influenced by their own interests or by others in forming judgements.

Rules of Conduct - Internal auditors:

- Shall not participate in any activity or relationship that may impair or be presumed to impair their unbiased assessment. This participation includes those activities or relationships that may be in conflict with the interests of the organisation;
- Shall not accept anything that may impair or be presumed to impair their professional judgement;
- Shall disclose all material facts known to them that, if not disclosed, may distort the reporting of activities under review.

4. Confidentiality

The principle – Internal auditors respect the value and ownership of information they receive and do not disclose information without appropriate authority unless there is a legal or professional obligation to do so.

Rules of Conduct - Internal auditors:

- Shall be prudent in the use and protection of information acquired in the course of their duties;
- Shall not use information for any personal gain or in any manner that would be contrary to the law or detrimental to the legitimate and ethical objectives of the organisation.

5. Competency

The principle – Internal auditors apply the knowledge, skills and experience needed in the performance of internal auditing services.

Rules of Conduct - Internal auditors:

- Shall engage only in those services for which they have the necessary knowledge, skills and experience;
- Shall perform internal auditing services in accordance with the International Standards for the Professional Practice of Internal Auditing;
- Shall continually improve their proficiency and effectiveness and quality of their services.