

HSS(FAU) 19/2003

Chief Executives of
HSS Boards/Trusts/Agencies

Directors of Finance
HSS Boards/Trusts/Agencies

2nd May 2003

Dear Sir/Madam

STATEMENT OF INTERNAL CONTROL: TRANSITIONAL STATEMENT 2002/03

The purpose of this Circular is to advise HSS bodies of the wording of a model transitional statement for 2002/03.

HSS (F) 24/2001, issued on May 21 2001, advised all HSS bodies of the phased introduction of a Statement on Internal Control with full implementation by 2003/04.

The circular advised that a transitional statement was permitted for 2001/02 and for 2002/03. However a full statement will be required for 2003/04.

HPSS bodies must develop the model wording provided to suit their own circumstances and explain what has been done to date, what remains to be done and the action planned for the coming year and a proposed timetable.

System of Internal Control

The statement on the system on internal control summarises the process that has been applied in reviewing the effectiveness of the system of internal control as appropriate to the circumstances of the reporting body.

Examples of some of the types of processes are:

- procedures for identifying the body's objectives and key risks;
- the development of the control strategy and risk management policy;
- the allocation of risk ownership;
- the role of the Audit Committee or other relevant committee;
- involvement and role of Internal Audit
- procedures for ensuring that aspects of risk management and internal control are regularly reviewed and reported on;
- systems used to ensure compliance with specific regulations or procedures laid down by the Department;
- monitoring of progress with current initiatives.

The review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the executive managers within the organisation who have responsibility for the development and maintenance of the internal control framework, and comments made by the external auditors in their management letter and other reports. The statement should specify the work undertaken during the year. It should also record details of actions taken or proposed to deal with material internal control aspects of any significant problems disclosed in the annual report and accounts.

It must also identify what has been done and what is planned to achieve a risk-based approach to internal control across all the functions of the organisation by the commencement of the 2003-04 accounting period when the Statement on Internal Control will be fully introduced.

Risk Management

HPSS bodies are referred to Circular HSS (PPM) 13/2002, issued on 6 December 2002, which reminds them of the importance of implementing an organisation-wide system of risk management and requires them to have the fundamental structures and processes to support the system in place by 31st March 2003. Circular HSS(PPM) 5/2003, issued on 11 April, requires all HPSS bodies to have a functioning risk register in place by September 2003.

Statement on Internal Control

The Statement on Internal Control should be developed in accordance with the proforma at Appendix 1 to this Circular.

The wording of the proforma in italics is an example of wording, which should be developed by individual organisations to suit their particular circumstances and should provide a brief but comprehensive summary of the actual processes in place including a description of how current initiatives are being taken forward. The statement should provide an honest appraisal of the state of internal controls currently in operation which is capable of substantiation. The narrative description of the processes in place should be used for reporting on progress or compliance with central initiatives.

The wording should reflect that a body is satisfied a sound system of internal control has been in place throughout the year, or that the body is developing its internal control process but considers that further elements are required to be introduced together with a continued period of trial and assessment prior to the preparation of a full statement.

The Statement on Internal Control should be presented along with the annual accounts. It should be signed by the Accountable Officer and passed to the external auditors for review and will form part of the audited annual financial statements.

Any enquiries concerning the content of this circular should be addressed in the first instance to John McCracken telephone 028 9076 5697.

Yours faithfully

PAULA MAGEE
Financial Accounting Unit

Suggested wording for a Transitional Statement on Internal Control for the Financial Year 2002/03

The board of [HPSS body] is accountable for internal control. As Accountable Officer and Chief Executive of the board of [HPSS body] I have responsibility for maintaining a sound system of internal control that supports the achievement of the policies, aims and objectives of the organisation, and for reviewing the effectiveness of the system.

The system of internal control is designed to manage rather than eliminate the risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness.

The system of internal control is based on an ongoing process designed to identify the principal risks to the achievement of the organisation's policies, aims and objectives, to evaluate the nature and extent of those risks and to manage them efficiently, effectively and economically.

Either:

This process has been in place for the year ended 31 March 2003 and up to the date of approval of the annual report and accounts and accords with the Department of Finance and Personnel guidance

OR

I expect to have the procedures in place in March 2003 necessary to implement DFP guidance. This takes account of the time needed to embed fully the processes which the [HPSS body] has agreed should be established and to improve their robustness.

Example wording:

The Board exercises strategic control over the operation of the organisation through a system of corporate governance which includes:-

- *a schedule of matters reserved for Board decisions;*
- *a scheme of delegation, which delegates decision making authority within set parameters to the Chief Executive and other officers;*
- *standing orders and standing financial instructions, the establishment of an audit committee.*

The system of internal financial control is based on a framework of regular financial information, administrative procedures including the segregation of duties and a system of delegation and accountability. In particular it includes:-

- *comprehensive budgeting systems with an annual budget which is reviewed and agreed by the board;*
- *regular reviews by the board of periodic annual financial reports which indicate financial performance against the forecast;*
- *setting targets to measure financial and other performances;*
- *clearly defined capital investment control guidelines;*
- *as appropriate, formal budget management disciplines.*

The [HPSS body] has an internal audit function which operates to defined standards and whose work is informed by an analysis of risk to which the body is exposed and annual audit plans are based on this analysis. In 2002-03 Internal Audit reviewed the following systems [specify the systems]. In his annual report, the Internal Auditor reported that the [HPSS body] system of internal control was adequate and effective [or otherwise as concluded by auditors]. However, [as appropriate] weaknesses in control were identified in a [small] number [be specific] of areas. Recommendations to address these control weaknesses have been or are being implemented.

With regard to the wider control environment the [HPSS body] has in place a range of organisational controls, commensurate with the current assessment of risk, designed to ensure the efficient and effective discharge of its business in accordance with the law and departmental direction. Every effort is made to ensure that the objectives of the [HPSS body] are pursued in accordance with the recognised and accepted standards of public administration.

For example: [bodies should provide specific examples], the [HPSS body's] recruitment and selection policies are based on the principle of equality of opportunity and controls are in place to ensure that all such decisions are taken in accordance with the relevant legislation. [Details of compliance or lack of it with management action to address weaknesses could be given].

With regard to estate management, decisions are taken within the context of an estate control plan, which prioritises management action based on an assessment of risk. [Additional information should be provided on Fire Code and Health and Safety and the extent of compliance].

The [HPSS body] is developing its approaches to risk management. In 2001/02 the Department accepted the internationally risk management standard AS/NZS 4360:1999, and the [HPSS body] has been working throughout 2002-03 to ensure its application throughout the Board/Trust/Agency by 2003-04.

In the interim the [HPSS body] has developed/is developing a risk management strategy, which has identified/will identify the organisation's objectives and risks and set out a control strategy for each of the significant risks. It is the intention to ensure that procedures are in place/procedures have been put in place for verifying that aspects of risk management and internal control are regularly reviewed and reported and that risk management has been incorporated fully into the corporate planning and decision making processes of the organisation.

[Add further detail as necessary, potentially referring to the continuing development of risk management and the introduction of controls assurance standards in accordance with departmental guidance].

In addition to these factors the actions outlined below are planned in the coming year [include a brief description of planned actions in the current year]. Include too the conclusion of any recent independent review, for example by internal audit or consultants, of the current situation.