

Report to the Finance and Performance Management Cabinet Committee



**Epping Forest
District Council**

Date of meeting: 25 September 2006

Subject: Business and Internal Control Assurance Framework

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Committee Secretary: Graham Lunnun (Ext: 4244)

Recommendations/Decisions Required:

That the Cabinet be recommended to adopt the Council's draft Business and Internal Control Assurance Framework

Summary

1. The purpose of the report is to recommend the adoption of the Council's draft Business and Internal Control Assurance Framework. The proposal has regard to current best practice in governance arrangements, and the improvement areas identified by the Audit Commission in its 'Use of Resources' Key Lines of Enquiry (KLOE) relating to internal control and the management of significant business risks. Officers consider that the feedback provided by the Commission in this respect is useful in helping the Council to improve in this area.

Background

2. The Use of Resources assessment focuses on financial management, but links to the wider strategic management of the Council. It looks at how financial management is integrated with Council strategy and corporate management, supports council priorities and delivers value for money. For district councils, use of resources assessments will be carried out annually and will inform decisions about possible CPA re-categorisation.
3. The Audit Commissions has updated its Use of Resources assessment model, to assist in their evaluation of how well authorities manage their financial resources. It is a more stringent test than the scored judgements that formed part of the CPA framework up to 2004. The 4-point scale has been modified so that 'adequate performance' (at minimum requirements) will score 2. The Council has been assessed at this level for the Internal Control category, and is targeting the next level. One of the improvements needed to move to level 3 requires the Council "to put in place an assurance framework that maps the Council's strategic objectives to risks, controls and assurances", to support the statutory Statement on Internal Control.
4. The KLOE relating to internal control issues also promotes the establishment of an audit committee, which is the subject of a report elsewhere on this agenda. It is

envisaged that the regular review and updating of a business assurance framework would fall within the remit of such a committee.

Internal Control and Business Assurance Framework

5. The Council already has effective processes dealing with the elements of the control framework, including its Financial Regulations, Contract Standing Orders and Risk Management processes. The main purpose of the assurance framework document is to bring these elements together to enable them to be evidenced in providing assurance that effective controls are in place.
6. The draft framework document is attached to this report, and provides the mechanism for continuous review of the effectiveness of the Council's internal control and risk management systems. It is supported by more detailed guidance produced by CIPFA, which sets out the main sources of evidence to support the Statement on Internal Control. This guidance emphasises reliance on existing processes and documents.
7. The key policies and procedures listed below comprise the core of this process. They are subject to ongoing or periodic review, and updated as appropriate. In the future, the review of the effectiveness of these policies, in the context of the Council's control framework, could be undertaken by the proposed Audit and Governance Committee.

The Council Constitution
The Community Strategy
The Council Plan
Standing Orders and Financial Regulations
Scheme of Officer Delegation
Consultation Strategy
The Local Code of Corporate Governance
Risk Management Strategy
Service Business Planning and Business Continuity Planning
Performance Management Framework
Treasury Management Policy
Human Resources Policies
Members Code of Conduct
Internal and External Audit planning and reporting
Anti-Fraud Policy and Confidential Reporting Policy
Planning Protocol
Health and Safety Policy
Data Protection Policy
Guidance to Members and Officers when representing the Council on Outside Organisations
Guidance to Councillors on the use of Member services (including IT facilities)
Code on Local Authority Publicity
Complaints procedure

A number of other policies are currently being developed or updated, and will be implemented during this financial year:

Staff Code of Conduct
Value for Money Strategy
Data Quality Strategy
Internet and E-Mail Acceptable Usage Policies
Telephone Usage Policy

8. These policies and procedures provide the evidence to demonstrate the robustness of the Council's governance arrangements, and support the production of the Statement on Internal Control. By regularly reviewing the controls and their consistent application across the Council on a day to day basis, it will be possible for the Council to demonstrate the effectiveness of its control environment and identify where further improvement is required.

Conclusion

9. The Council is seeking continuous improvement in the Council's governance arrangements, and to achieve as high a rating as possible under the CPA arrangements. One of the options open to the Council in demonstrating the robustness of its governance arrangements is to adopt the Business and Internal Control Assurance Framework along the lines outlined in this report.

Options

To adopt the Business and Internal Control Assurance Framework on the basis outlined in this report, or to recommend no action on this matter at the present time.

Resource implications: From existing resources

Community Plan/BVPP reference: Not applicable

Relevant Statutory Power: None

Background Papers: Audit Commission's Use of Resources Audit Score Feedback

EPPING FOREST DISTRICT COUNCIL

BUSINESS AND INTERNAL CONTROL ASSURANCE FRAMEWORK**1.1 Introduction**

The Accounts and Audit Regulations (2003) require audited bodies to conduct a review at least once a year of the effectiveness of its system of internal control, and publish a Statement on Internal Control (SIC) each year with the authority's financial statements.

The purpose of the SIC process is to provide a continuous review of the effectiveness of an organisation's internal control and risk management systems, so as to give assurance on their effectiveness and/or to produce a management action plan to address identified weaknesses in either process. It is intended that the process of preparing the SIC adds value to the Council's corporate governance and internal control framework.

1.2 Context

The Audit Commission uses a 'Use of Resources' assessment model, to assist in their evaluation of how well authorities manage and use their financial resources. Epping Forest District Council has been assessed at level 2 (adequate performance) for the Internal Control category, and is targeting the next level. One of the improvements needed, to move to level 3, requires the Council to put in place an assurance framework that maps the Council's strategic objectives to risks, controls and assurances, to support the SIC.

The Council already has effective processes dealing with the elements of the control framework, including its Financial Regulations, Contract Standing Orders and Risk Management processes. The main purpose of this assurance framework document is to bring these elements together to enable them to be evidenced in providing assurance that effective controls are in place.

1.3 Corporate ownership

In accordance with CIPFA's proper practice, the Joint Chief Executives, as the two most senior officers, and the Leader of the Council, as the most senior member will sign the SIC each year. They will satisfy themselves that the document is supported by reliable evidence and accurately reflects the internal control environment. This emphasises that the document is about all corporate controls and is not confined to financial issues.

1.4 Proper practice

The Accounts and Audit Regulations refer to the preparation of a SIC document in accordance with "proper practice". At the suggestion of the Audit Commission, CIPFA published a statement on proper practice in April 2004 giving high-level guidance on the necessary processes and providing a model SIC. The Council will comply with this guidance.

1.5 **Scope of Internal Control**

The scope of internal control spans the whole range of the Council's activities and includes those controls designed to ensure:

- the authority's policies are put into practice
- the Council's values are met
- laws and regulations are complied with
- required processes are adhered to
- financial statements and other published information are accurate and reliable
- human, financial and other resources are managed efficiently and effectively, and high quality services are delivered efficiently and effectively.

Having established the system of internal control, the Council has put in place processes to maintain it and keep it up to date. In practice, this process is closely aligned with the arrangements to review and keep up to date the Council's risk management arrangements, which features strongly in the SIC process and feeds into the process annually for compiling the SIC.

1.6 **Assurance gathering process**

The Council already has effective processes dealing with aspects of the SIC. The feature of the SIC is to bring them together and evidence them.

This framework is supported by more detailed guidance produced by CIPFA, which sets out the main sources of evidence to support the SIC. This emphasises reliance on existing processes and documents.

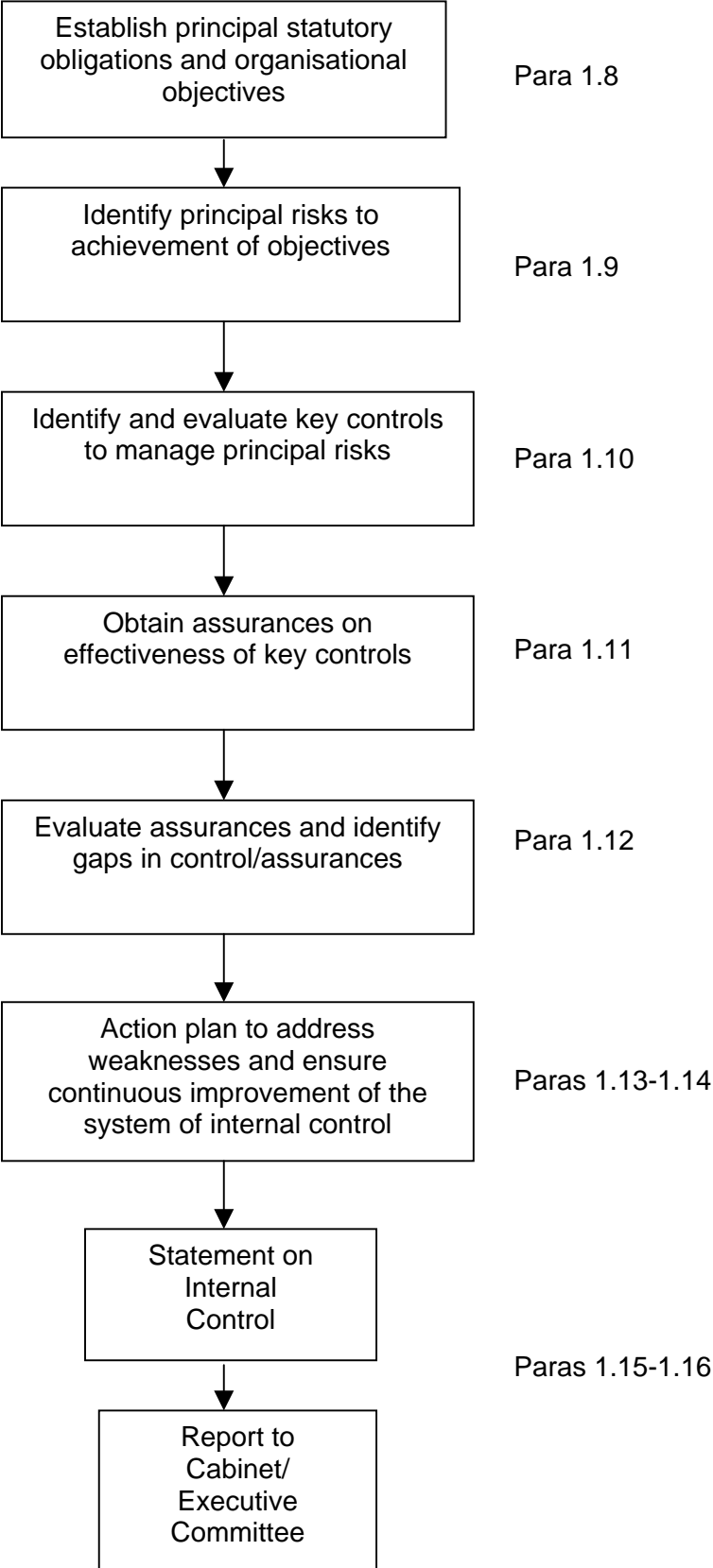
The task of producing the SIC involves the need to research and formally recognise things currently done across the authority and to record them. The co-ordination of existing evidence should ensure consistency of approach across the Council, and promote corporate awareness of good practice.

1.7 **Compiling the SIC - CIPFA's flowchart**

The Council uses the flowchart at the heart of CIPFA's guidance (See Table 1) to relate the SIC back to the Council's statutory obligations and organisational objectives.

Each step on the flowchart is underpinned by "examples of assurance" - in turn supported by suggested sources of evidence that the Council can use to demonstrate delivery. There are many potential sources of evidence, some of which are set out in the Appendix. They are not definitive, but they give a flavour of what the Council will look for in compiling and evidencing the SIC.

Table1: Review of Internal Control and SIC Assurance Gathering Process



Establish Obligations and Objectives

- 1.8 The multifunctional nature of local authorities means that there are a vast number of mandatory and discretionary requirements and powers. The Council will ensure that processes are in place to properly reflect these obligations in its aims and objectives and also to identify changes in these requirements. The Council will therefore ensure that all the main statutory requirements and the Council's key objectives are fully reflected in the Council Plan and Best Value Performance Plan.

Identify Principal Risks to Achievement of Objectives

- 1.9 In order to ensure complete identification of risks, the Council considers risk from both a strategic and an operational perspective. Strategic risk includes those to service provision, reputation and political standing, whilst operational risk includes financial, physical and contractual risks. Risks are prioritised according to their likelihood and potential impact. Those risks that are both highly likely and of high impact are considered to be the principal risks to achievement of the objectives of the authority.

Identify and Evaluate Key Controls to Manage Principal Risks

- 1.10 Having identified the principal risks, through this Framework, the Council will ensure that it has adequate controls to mitigate them. The nature and importance of these controls is formally recorded and communicated to those responsible for operating the control through the Action Plan attached to EFDC's Strategic Risk Register.

Obtain Assurance on Effectiveness of Key Controls

- 1.11 The Accounts and Audit Regulations 2003 state that the "relevant body" is responsible for ensuring that the body (authority) has "*a sound system of internal control*". The Council's Corporate Governance Group is responsible for ensuring that procedures have been established to provide sufficient assurance to the Council's Finance and Performance Management Cabinet Committee (and from 2007/8, the proposed new Audit Committee), that effective controls are in place.

Sources of Assurance

(a) Management

Heads of Service and managers assigned with the ownership of risks are responsible for routinely monitoring and reviewing the related internal controls as an integral part of the risk management process, and for regularly reporting to the Corporate Risk Management Group. Any other general concerns about the operation of internal controls are reported to the Head of Finance, Chief Internal Auditor, or to the Council's Management Board.

The Council recognises the importance of training on finance and internal controls, and during 2005/06 a number of sessions of finance awareness training were provided to groups of managers and other staff with financial responsibilities across the Council. Following the success of these courses the Council has embedded training on finance and internal control issues within its Corporate Training Programme.

(b) **The Role of the Chief Financial Officer and the Monitoring Officer**

The statutory functions undertaken by these two officers provide a key source of assurance that the systems and procedures of internal control that are in operation are effective, efficient and are being complied with on a routine basis. As the SIC will be read alongside financial statements, the Chief Financial Officer will ensure that he reviews it at an early stage.

(c) **Internal Audit**

The statutory responsibility for maintaining and reviewing the system of internal control rests with the "relevant body" (the Council). In practice, however, the Council takes assurance from the work of Internal Audit. *The Code of Practice for Internal Audit in Local Government in the United Kingdom* (the Code) defines Internal Audit as:

"...an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment, comprising risk management, control and governance by evaluating its effectiveness in achieving the organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources."

The Head of Internal Audit is required to include in the annual Internal Audit report to the Council an opinion on the overall adequacy and effectiveness of the authority's internal control environment, providing details of any weaknesses that qualify this opinion and bringing to the attention of the authority any issues particularly relevant to the preparation of the SIC.

(d) **External Audit**

Whilst External Audit is another potential source of assurance on the operation of internal controls, the Council takes into account that External Audit reports/management letters will not cover the full range of activities and risks and that external auditors are not required to form an opinion on the effectiveness of the Council's corporate governance procedures or its risk and control procedures.

(e) **Corporate Governance Group**

The Corporate Governance Group comprises Management Board, the Monitoring Officer, the Chief Financial Officer and the Chief Internal Auditor. The Group reviews the arrangements to provide assurance on the adequacy and effectiveness of the Council's governance framework, including compliance with the Local Code of Corporate Governance.

(f) **Other Review Agencies and Inspectorates**

The system of internal control covers the whole of the Authority's operations. Aspects of these operations, such as housing benefits and health and safety, are subject to independent external review and these reports also provide the Council with relevant assurance. Internal review agencies include the fraud investigation unit. Reports of the Local Government Ombudsman may also contribute to this assurance. However, the Council recognises that it, and not the external body, is responsible for satisfying itself as to the efficiency and effectiveness of internal control.

Evaluate Assurance

- 1.12 Having received assurance from the various sources, the Council reviews this against risk documentation and the list of principal risks to objectives. Any gaps in the assurance over principal risks are recorded for inclusion in the SIC. The Council also reaches a conclusion as to the independence and objectivity of the various sources of assurance before coming to an overall conclusion.

Action Plan for Addressing Internal Control Issues

- 1.13 The Council will prepare an action plan (in the context of areas for improvement) to address significant internal control issues, which it will disclose in the SIC, in order to deliver public assurance that these issues have been, or are being, addressed and that the SIC is a balanced reflection of the actual control position. In order to help the disclosure in relation to a significant internal control issue a description of the weakness and its impact will be given to provide context for the actions taken.
- 1.14 A single definition of a 'significant internal control' issue is not possible. The Council will exercise judgement in deciding whether or not a particular issue should be regarded as falling into this category. Factors which will be considered when exercising this judgement will include:
- the issue has affected or prevented the achievement of a principal objective
 - the issue has resulted in a need to seek additional funding to resolve it
 - the issue has led to a material impact on the accounts
 - the audit committee, or equivalent, has expressed significant concerns
 - the Head of Internal Audit has reported on it as significant, for this purpose, in the annual opinion on the internal control environment
 - the issue, or its impact, has attracted significant public interest or has seriously damaged the reputation of the organisation
 - the issue has resulted in formal action being taken by the Chief Financial Officer and/or the Monitoring Officer

Statement on Internal Control

- 1.15 The Council's SIC represents the end result of the review of internal control, including the process of risk management, which has been embedded across Council services. As such, production of the SIC is not conducted as an 'add-on' end-of-year activity, but explains the nature of control, and any material changes in control, exercised through the whole of the accounting period. Although published with the financial statements, the SIC is a broad reflection of the whole governance of the Authority.
- 1.16 The SIC is currently approved at a meeting of the Finance and Performance Management Cabinet Committee (from 2007/8, this may be approved by the proposed new Audit and Governance Committee). The SIC must be published with the financial statements and so the publication timetable for the financial statements drives the SIC approval timetable. In considering whether to approve the SIC, the Council will satisfy itself that it has obtained relevant and reliable evidence to support the disclosures made, and will also consider the reviews of the Chief Financial Officer and the Monitoring Officer on issues covered by their statutory responsibilities.