

DUDLEY METROPOLITAN BOROUGH COUNCIL

AUDIT COMMITTEE

21st JULY 2005

REPORT OF THE DIRECTOR OF FINANCE

ANNUAL STATEMENT OF INTERNAL CONTROL

1. PURPOSE

- 1.1. This report deals with the Statement of Internal Control that is to be published with the accounts for the financial year 2004/2005.
- 1.2. The Statement of Internal Control is Appendix 1 to this report.

2. BACKGROUND

- 2.1. Every local authority is required to publish a Statement of Internal Control as part of the publication of its Financial Statements.
- 2.2. The legislation requires that the Chief Executive and the Leader of the Council sign the Statement of Internal Control, but it is considered good practice to present the draft to the Audit Committee for consideration prior to it being signed.
- 2.3. The Statement of Internal Control summarises the state of the Internal Control Environment within the Council and highlights any areas of concern. The Internal Control Environment includes matters such as:
 - Performance management
 - Business strategy and planning process
 - Annual budget & budgetary control
 - Local code of governance (Council's Constitution)
 - Project management procedures
 - Risk management
 - Anti-Fraud and Corruption strategy
 - Ethical governance
 - Financial policies and procedures
 - Codes of conduct
 - Confidential Reporting policy

- 2.4. Dudley MBC has appropriate policies and procedures in place covering the items identified in paragraph 2.3 above and the Statement of Internal Control highlights those elements where there may be an adverse effect on the internal control environment.

3. PROPOSALS

- 3.1. The Statement of Internal Control included as Appendix 1 to this report is accepted.
- 3.2. The Committee approve the submission of the Statement of Internal Control for signature by the Chief Executive and the Leader of the Council.

4. FINANCE

- 4.1. This report has no direct financial effect.

5. LAW

- 5.1. The Account and Audit Regulations 2003 (Regulation 4) require that “The relevant body shall conduct a review at least once in a year of the effectiveness of its system of internal control and shall include a statement on internal control, prepared in accordance with proper practices”.

6. EQUALITY IMPACT

- 6.1 This report does not raise any equal opportunities issues.

7. RECOMMENDATIONS

- 7.1. The proposals in Section 3 should be accepted.



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DIRECTOR OF FINANCE

Contact Officer Richard Clarke – Extension 4839

1. SCOPE OF RESPONSIBILITY

Dudley Metropolitan Borough Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

The Council also has duty under the Local Government Act 1999 to make arrangements to secure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness. In discharging this overall responsibility, the Council must also ensure that there is a sound system of internal control that facilitates the effective exercise of the Council's functions, including arrangements for the management of risk.

2. THE PURPOSE OF THE SYSTEM OF INTERNAL CONTROL

The system of internal control is designed to manage risk of failure to achieve policies, aims and objectives to a reasonable level, rather than to eliminate all risk. 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 and prioritise the risks to the achievement of the Council's policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The system of internal control has been in place at Dudley Metropolitan Borough Council for the year ended 31st March 2005 and up to the date of approval of the annual report and accounts and, except for the details of significant internal control issues at section 5, accords with proper practice.

3. THE INTERNAL CONTROL ENVIRONMENT

The internal control environment encompasses all the processes and procedures that the Council has in place to protect itself against risks, whether financial or otherwise, and to achieve its objectives. The internal control environment is based upon the Council's Code of Corporate Governance and consists of a whole framework of management information, financial regulations, administrative procedures (including segregation of duties), management supervision, and a system of delegation and accountability. Council members and managers are responsible for developing and maintaining the internal control environment. One significant development during the financial year 2004/5 was:

- The production of an Anti-Fraud and Corruption strategy that codifies the responsibilities of officers and members with regard to the prevention and detection of fraud and corruption.

The cornerstone of the internal control environment is the Council's Constitution, which sets out how the Council operates, how decisions are made and the procedures that are followed to ensure that these are efficient, transparent and accountable to local people. Some of these processes are required by the law, while others are a matter for the Council to determine. The Council's Constitution also contains detailed codes and protocols, such as Contract Standing Orders (defining how contracts must be let) and Financial Regulations (setting out procedures and principles for proper financial management). The Anti-Fraud and Corruption strategy has also been incorporated into the Constitution.

The arrangements for establishing and monitoring the Council's objectives are also key elements in the internal control environment. The Council's most important objectives are consolidated in its published Council Plan, the current version of which covers the period 2005/08 and includes over 200 improvement targets. Achievement against objectives is monitored regularly, and reported to senior staff, the Executive and full Council quarterly. The focus is on 52 key service indicators. The high level objectives in the above plans are supported by more detailed strategies and plans with their own monitored targets.

The Council has a legal duty to secure economy, efficiency and effectiveness in its use of resources and continuous improvement in its services. This duty is recognised in establishing the Council's policy agenda, but more specifically, in a range of services-based and thematic Best Value reviews linked to the priorities of the Council Plan. The Council has also entered into a Local Public Service agreement with the Government that covers twelve priority targets where the Council aims to improve services faster than normal.

Effective financial management is an essential aspect of the Council's internal control environment. This is achieved in particular through:-

- Comprehensive revenue and capital budgeting systems;
- A medium term financial planning process – three year indicative budgets are produced for both capital and revenue;
- Regular reporting and monitoring of actual performance against forecast;
- Post-completion review of major projects.

The Council is responsible for ensuring that risks that could frustrate the achievement of its objectives are properly managed and controlled. Part of this involves ensuring compliance with the Council's own policies and procedures and also with laws and regulations. The Council's Constitution sets out the responsibilities of members and senior managers for this, particularly the responsibilities of the three statutory posts:-

- The head of the paid service (Chief Executive) must ensure that the Council is properly organised and staffed;
- The monitoring officer (the Director of Law and Property) must ensure the lawfulness and fairness of decision-making;
- The chief finance officer (Director of Finance) must ensure the lawfulness and financial prudence of decision-making. The Director of Finance is also responsible for the proper administration of the Council's financial affairs.

There is also a statutory requirement for the Council to have an adequate and effective internal audit function, a responsibility delegated to the Director of Finance. Internal Audit operates in accordance with the Code of Practice for Internal Audit in local Government in the United Kingdom and is under the day-to-day control of the Head of Audit Services who acts independently. Internal Audit's primary role is to independently review and report on whether risks facing the Council are effectively managed and controlled. It has a rolling programme of audits that, over a period of years, is intended to review all areas of major risk within the Council. The priority of different areas of the programme is determined by Internal Audit's own assessment of risks and controls.

In the course of 2004/05, to further improve the internal control system, the Council continued to “embed” a formal system of risk management into its management processes. Senior managers in all Directorates have been involved in workshops to identify risks and controls, and to evaluate the importance of risks and the effectiveness of controls on a common basis. This has resulted in the production of a corporate risk register, and the identification of any areas where further actions are necessary to effectively manage risks. The corporate risk register and action plans will be reviewed on a regular basis and the latest review identified areas where the information risk register could be added to, to improve the usefulness of the process and work on this is continuing.

The Council has an Audit Committee with a remit to oversee the effective operation of both the internal and external audit function, and to ensure that appropriate action is taken in relation to audit recommendations. There are also six Select Committees that carry out a programme of reviews of Council services and decisions. Finally External Audit conduct annual audits of the Council and external inspectorates perform periodic reviews of Council services. All of these bodies form part of the Council’s internal control environment, as well as contributing to the review of the adequacy and effectiveness of that environment.

4. REVIEW OF EFFECTIVENESS

The Council has responsibility for conducting, at least annually, a review of the effectiveness of the system of internal control. 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 authority who have responsibility for the development and maintenance of the internal control environment, and also by comments made by the external auditor and other review agencies and inspectorates in their annual audit letter and other reports.

During 2004/05 Internal Audit carried out approximately 200 planned audit reviews as part of their four-year strategic plan. The findings were reported to relevant line managers and senior management, and appropriate action agreed.

The Audit Committee receives an annual report summarising the performance of Internal Audit in the previous financial year. The Committee also receives a series of reports setting out the results of Internal Audit’s work in each of the Council’s Directorates. These reports detail the higher importance findings, any unimplemented recommendations, and management feedback about the action they have taken. The Committee also receives more detailed reports on other areas where they consider it necessary. The Director of Finance will, under the Anti-Fraud and Corruption Strategy, report major losses, resulting from fraud and corruption, to the Audit Committee. No such reports were made during 2004/2005.

External Audit have completed their review of the internal control system for 2004/05. Their Annual Audit Letter for that year will be presented to the Audit Committee and the Executive. They have raised the internal control issues described in Section 5 of this Statement.

During 2004/2005 external inspections were carried out by the Audit Commission. The main inspections covered Waste Management and Cultural Services.

The Council’s six Select Committees also carried out an extensive programme of reviews of the Council’s activities and decisions.

In carrying out its review of the internal control system, the Council has considered the evidence provided by all of the sources referred to above. With the exception of the issues raised by External Audit, the evidence from these various sources did not reveal any deficiencies in the internal control system of such fundamental significance as to require reporting in Section 5 of this Statement.

5. SIGNIFICANT INTERNAL CONTROL ISSUES

Although significant progress has been made in the implementation of formal risk management, it is acknowledged that further work is required to fully 'embed' the process throughout the Authority. In particular, steps are needed to more fully engage members in the process, to identify corporate and cross-cutting risks, and to develop procedures for management to periodically review and confirm the effectiveness of controls.

Further work is in progress to publicise the Anti-Fraud and Corruption Strategy and the issues it addresses and this needs to continue.

A review of the operation of the Code of Corporate Governance was required and Internal Audit undertook this in the latter part of 2004/2005. This review identified that the Code was being implemented satisfactorily. A new standard for good governance in public services was published in January 2005 and Dudley's Code of Corporate Governance generally complies with the new standard. However, it is intended that Dudley's Code of Corporate Governance will be re-drafted during 2005 to follow the format of the new standard.

Councillor D. Caunt
Leader of the Council

A. Sparke
Chief Executive