



NHS Management Executive
St. Andrew's House
Edinburgh EH1 3DG

15th February 1999

Dear Colleague

**CORPORATE GOVERNANCE IN THE NHS: INTERNAL
FINANCIAL CONTROL STATEMENT**

Background

In keeping with Corporate Governance in the NHS, a new statement on Internal Financial Control will be required in 1998-99. The implementation of this statement should not pose a problem as the level of disclosure at this stage does not represent a significant departure from the responsibilities set out in the current Directors' statements. However, the Management Executive recommend dialogue with both your internal and external auditors regarding the statement and adherence to it. The scope of the Internal Financial Control Statement may be extended in future years.

Action

There are three Directors' statements which are required in 1998-99. The Directors' statements relate to the whole of 1998-99 and should also take account of material developments between the balance sheet date and the date upon which the annual accounts are signed. They should not be seen as position statements as at 31 March.

Details of these statements and useful information is provided at Appendix A. The actual Directors' statements are in Appendix B. For the purpose of the statements, the term Directors refers to both executive and non-executive Board Directors.

Addressees

For action:
General Manager,
Health Boards

Chief Executive,
NHS Trusts

General Manager,
Common Services Agency

General Manager,
State Hospital

Chief Executive,
HEBS

Executive Director,
SCPMDE

For information:
Chairman,
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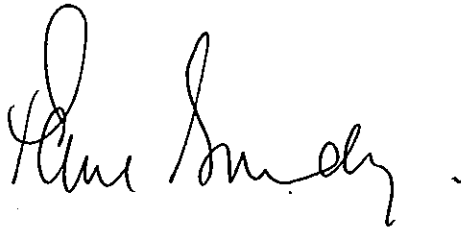
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The form of the auditor's report that will accompany the Director's Statement on internal financial control is under consideration by the Accounts Commission. The Commission has advised that it will issue guidance to external auditors shortly.

This guidance has been issued for 1998/99. It is intended to review the format and content of the Internal Financial Control Statement for 1999/00. This review will consider the impact of the Combined Code, which supercedes both the Cadbury and Greenbury reports in corporate governance and changes arising from the implementation of the White Paper.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Paul A. Brady', written in a cursive style.

DR PAUL A. BRADY
Director of Finance

APPENDIX A

Statements

Health Boards and Special Health Boards

1.a) Statement of the General Manager's Responsibilities as the Appointed Officer of the Health Board

This statement remains largely the same as in previous years.

NHS Trusts

1.b) Statement of the Chief Executive's Responsibilities as the Appointed Officer of the NHS Trust

This statement is new and will be required for the 1998-99 Annual Accounts.

2. Statement of Health Board Members'/NHS Trust Board Members' Responsibilities in Respect of the Accounts

This statement remains largely the same as in previous years. The only difference is that the reference to the safeguarding of assets or taking reasonable steps regarding the prevention and detection of fraud and other irregularities is now to be included in the new Internal Financial Control Statement.

3. Statement of Directors' Responsibility in Respect of Internal Financial Control

This statement is new for 1998-99 for all health bodies. The internal financial control standards for the NHS have been covered in previous correspondence issued by the Management Executive including, but not limited to, MEL 1994(80) and Treasury Officer of Accounts letter DAO 13/97. Two areas which have not specifically been identified previously, but that require to be reviewed for 1998-99 are Fraud and Corruption Policy and Risk Assessment.

The Management Executive considers that these controls should have been in place throughout the financial year.

Directors will be required to make additional disclosure in the Director's Statement where:

- action has been taken, or proposed, to correct weaknesses in the system of internal financial control, or an explanation of why corrective action is not considered necessary.
- where a material loss, contingency or uncertainty has arisen which requires disclosure in either the Financial Statements or the Auditor's Report on the accounts because of a weakness in internal financial control. In such instances, the Directors should

describe what corrective action has been or is intended to be taken, or explain why no corrective action is required;

The role of external audit is discussed below. It is however important to highlight that it will be the responsibility of each health body to provide appropriate evidence for the external auditor that the controls referred to in the statements are in existence.

Key components within the control environment

To facilitate the introduction of the Internal Financial Control Statement in 1998-99 it is helpful to identify the key individuals or groups and briefly identify their indicative roles. These are discussed below.

Director of Finance

The Director of Finance will play a significant role in ensuring that the necessary Corporate Governance measures have been appropriately implemented within your organisation. With regard to the Internal Financial Control Statement, we would expect the Director of Finance to arrange for the provision of the necessary compliance evidence.

The Management Executive would expect the evidence to:

- identify where there is a significant control weakness and that this will be disclosed in the statement; and/or
- show where a control has been introduced during the financial year. This should also be referred to in the statement.

The Audit Committee

The Audit Committee's role should be to ensure that the organisation has the relevant controls in place to allow the Directors to sign the required statement. This should include ensuring that, in conjunction with the Director of Finance, a review has been undertaken and that appropriate compliance evidence is available for the external auditor. It is not intended that the review would be included in the annual accounts.

Consistent with the role outlined in the Audit Committee handbook, the Audit Committee should provide appropriate assurance to the Directors that the necessary controls are in place to allow the Directors to sign the Internal Financial Control Statement.

Internal audit function

The external auditor, as is currently the situation, will review the adequacy of the internal audit function. Through the internal audit plan having been agreed with the Audit Committee, the Management Executive would expect no internal audit function to have difficulty in complying with its role in reviewing and monitoring internal financial controls. Internal audit is also likely to have a key role in the production of evidence of adherence.

Directors and General Manager/Chief Executive

The Internal Financial Control Statement should be seen as the Directors' collective responsibility with the General Manager/Chief Executive signing the statement on their behalf.

Outline of the external audit process

The objective of the external auditor's review will be to conclude whether:

- the Directors have provided the disclosures required by this MEL; and
- that the assurance statement is not inconsistent with the findings from the audit.

It should be noted that neither the health body nor the external auditor are giving any opinion or certification regarding the effectiveness of individual controls.

Where your health body provides appropriate evidence of adherence to the external auditor, the Management Executive expects that there will be no additional audit fee implications. Where appropriate evidence of adherence is not provided, there are adherence difficulties or the statement is inconsistent with audit findings, there may be additional audit cost implications.



APPENDIX B

1.(a) **STATEMENT OF THE GENERAL MANAGER'S RESPONSIBILITIES AS THE APPOINTED OFFICER OF THE HEALTH BOARD**

As General Manager of [] Health Board, the Chief Executive of the NHS in Scotland has designated me as appointed officer. This designation carries with it certain responsibilities, the essence of which are ensuring the proper stewardship of public money and assets for which I am answerable and for the keeping of proper records as set out in the appointed officer memorandum issued by the Management Executive.

To the best of my knowledge and belief, I have properly discharged my responsibilities as appointed officer as set out in my letter of appointment.

General Manager

Date

1.(b) **STATEMENT OF THE CHIEF EXECUTIVE'S RESPONSIBILITIES AS THE APPOINTED OFFICER OF THE NHS TRUST**

As Chief Executive of [] NHS Trust, the Chief Executive of the NHS in Scotland has designated me as appointed officer. This designation carries with it certain responsibilities, the essence of which are ensuring the proper stewardship of public money and assets for which I am answerable and for the keeping of proper records as set out in the appointed officer memorandum issued by the Management Executive.

To the best of my knowledge and belief, I have properly discharged my responsibilities as appointed officer as set out in my letter of appointment.

Chief Executive

Date

2.(a) **STATEMENT OF HEALTH BOARD MEMBERS' RESPONSIBILITIES IN RESPECT OF THE ACCOUNTS**

Under the National Health Service (Scotland) Act 1978, the Health Board is required to prepare accounts in accordance with the directions of the Secretary of State for Scotland which require that those accounts give a true and fair view of the state of affairs of the Health Board as at 31 March 19. and its income and expenditure for the year then ended. In preparing these accounts the Directors are required to:

Apply on a consistent basis the accounting policies and standards approved for the NHS in Scotland by the Secretary of State.

Make judgements and estimates that are reasonable and prudent.

State where applicable accounting standards have not been followed where the effect of the departure is material.

The Health Board is also responsible for keeping proper accounting records.

The Health Board members confirm they have discharged the above responsibilities during the financial year and in preparing the accounts.

Chairman

Director of Finance

Date

2.(b) STATEMENT OF NHS TRUST BOARD MEMBERS' RESPONSIBILITIES

The National Health Service (Scotland) Act 1978 requires [] NHS Trust to prepare accounts for each financial year which give a true and fair view of the state of affairs of the NHS Trust and of its income and expenditure for that period. In preparing those accounts, the Trust board members are required to (a) select suitable accounting policies and then apply them consistently, (b) make judgements and estimates that are reasonable and prudent, (c) state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts, and (d) prepare the accounts on the going concern basis unless it is inappropriate to presume that the Trust will continue to operate.

The Trust board members are responsible for ensuring proper accounting records are maintained which disclose with reasonable accuracy at any time the financial position of the Trust and enable them to ensure that the accounts comply with the National Health Service (Scotland) Act 1978 and the requirements of the Management Executive.

The Trust board members confirm they have discharged the above responsibilities during the financial year and in preparing the accounts.

Chairman

Director of Finance

Date

3. **STATEMENT OF DIRECTORS' RESPONSIBILITY IN RESPECT OF INTERNAL FINANCIAL CONTROL**

As Appointed Officer, I acknowledge my responsibility for ensuring that an effective system of internal financial control is maintained and operated by (name of body).

The system can provide only reasonable and not absolute assurance that assets are safeguarded, transactions authorised and properly recorded, and that material errors or irregularities are either prevented or would be detected within a timely period.

The system of internal financial control is based on a framework of regular management 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 [a committee of] the Management Board [or other appropriate description];
- Regular reviews by the Management Board of periodic and annual financial reports which indicate financial performance against the forecasts;
- Setting targets to measure financial and other performance;
- Clearly defined capital investment control guidelines;
- As appropriate, formal project management disciplines;

(Name of body) has an internal audit function which operates to standards defined in the NHS Scotland Internal Audit Manual. The work of internal audit is informed by an analysis of the risk to which the body is exposed, and annual internal audit plans are based on this analysis. The analysis of risk and the internal audit plans are endorsed by the body's Audit Committee and approved by me. At least annually, the Chief Internal Auditor (CIA) provides me with a report on internal audit activity in the body. The report includes the CIA's independent opinion on the adequacy and effectiveness of the body's system of internal financial control.

I have reviewed the effectiveness of the system of internal financial control; informed by the work of the internal auditors; the Audit Committee which oversees the work of the internal auditor; the executive managers within the body who have responsibility for the development and maintenance of the financial control framework; and comments made by the external auditors in their management letter and other reports.

[Details of the action taken, or proposed, to correct weaknesses in the system of internal financial control, or an explanation of why corrective action is not considered necessary, should be given here. The wording should be tailored to reflect the circumstances of the case.]

General Manager/Chief Executive

Date