

Audit Committee Meeting – 10 December 2008

FINANCE AUDIT REPORT

Executive summary and recommendations

Introduction

Following the completion of the internal audit of the financial systems and procedures during quarter three, the audit report is attached.

Decision

The Committee is asked to review and approve the report.

Background information

The Financial Systems Review report produced a “satisfactory” rating and five recommendations.

Resource implications

Nil

Financial implications

Audit fee, 10 days.

Appendices

Appendix One – PKF Audit Report

Date of paper

28 November 2008



Health Professions Council

Financial Systems Review

November 2008

Confidential



Accountants &
business advisers

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Project timescales

Date project commenced	10/11/08
Date field work completed	20/11/08
Date draft report issued	24/11/08
Date management comments received	25/11/08
Date final report issued	27/11/08

1 Introduction

1.1 In accordance with the 2008/09 internal programme for the Health Professions Council (“HPC”) that was agreed with the Audit Committee in February 2008, we have undertaken a review of the controls in operation over the organisation’s financial systems.

Key risks and scope of our work

1.2 The key financial risks identified by the HPC for 2008/09 were as follows:

Financial management	Financial processing
Mismatch between Council goals & approved financial budgets	Registrant credit card record fraud
Insufficient cash to meet commitments	Total receipt of correct fee income
Large capital project cost over-runs	Unauthorised payments to organisations
Unexpected rise in operating expenses (especially tribunal exceptional costs)	Unauthorised payments to personnel
Loss in value of investment portfolio	Mis-signing of cheques (forgery)
Inability to pay creditors	Unauthorised removal of assets (custody issue)
Inability to collect from debtors	
Fund Manager or Money Market provider insolvency	

1.3 Our review therefore focused on the internal control arrangements for managing the above risks.

1.4 The following financial risks identified by the HPC are managed through the external audit and other processes. In order to avoid duplication of audit effort, we have not included these as part of this review.

- Tax law non-compliance;
- Non compliance with Privy Council/FReM;

- Qualified opinion received by the Auditors on the Annual Financial Statements;
 - Under-funded pension liabilities (CPSM Retirement Benefits Scheme*);
 - Section 75 (Pensions Act 1995) liability resulting if the number of active members of the Capita Flexiplan scheme drops to zero;
 - Capita Flexiplan liability resulting from new scheme specific funding standard (“SSFS”) and insufficient Pensions Capital to meet fund obligations; and
 - Late submission of the Financial Statements/Annual Report, beyond sector standards.
- 1.5 The risk of fraudulent applications by registrants has previously been addressed by our review of the Registration Department, the findings of which were reported in March 2008.
- 1.6 We also followed up the recommendations that we raised as part of our 2007/08 review to confirm that these had been implemented by management.
- 1.7 The work was carried out primarily by holding discussions with relevant staff and management, reviewing any available documentation and undertaking detailed testing on a sample basis, where required. The audit fieldwork was completed in November 2008.
- 1.8 This report has been prepared as part of the internal audit of the Health Professions Council under the terms of the contract for internal audit services. It has been prepared for the Health Professions Council and we neither accept nor assume any responsibility or duty of care to any third party in relation to it.
- 1.9 The conclusions and recommendations are based on the results of audit work carried out and are reported in good faith. However, our methodology is dependent upon explanations by managers and sample testing and management should satisfy itself of the validity of any recommendations before acting upon them.

2 Executive Summary

- 2.1 This report summarises the work undertaken by PKF within the agreed scope of our review of the financial systems in operation at the HPC.

Background

- 2.2 The HPC's budget for 2008/09 anticipates that the organisation will receive around £13.7 million this year from applicants and registrants' fees (£12.3 million - 2007/08). This is the organisation's primary source of income. Around £175,000 is budgeted to be received from investment income. The HPC's original budget aims to generate a small surplus of just under £250,000 for 2008/09.
- 2.3 All financial processing is undertaken in-house by the Finance Department. The financial system was upgraded to Sage 200 from 1st April 2008. Payroll is processed on a separate standalone Sage payroll system and registrants' income is recorded on the Netregulate Debtors ledger.
- 2.4 During the year the HPC also purchased the On-line Purchase Requisition System ("PRS") and Project Accounting. The systems went live on 1st July but both were taken offline from 1st September following implementation difficulties and the organisation reverted to manual purchase ordering from that time onwards.

Our assessment

- 2.5 Based on our review work, we have concluded that the HPC's financial systems were **satisfactory**. However, we noted some areas where there remains scope for improvement to tighten up controls and meet best practice going forward and to be alert to potential shifts in the organisation's financial risk profile.
- 2.6 There is an inherent likelihood that many of the key financial risks of the HPC will increase over the coming months in the light of recent turbulence in the financial environment. Investment losses and income shortfalls may begin to emerge during 2009 and the number of registrants could also potentially decline.
- 2.7 The principal findings of our work are set out in the paragraphs below.

Principal findings

- 2.8 Our testing indicated that the HPC's budget setting and financial reporting arrangements were operating effectively. Detailed steps are taken to refine the annual budget each year and to evaluate the underlying assumptions behind the HPC's forecasts within the context of the organisation's Five Year Plan.

- 2.9 We noted that detailed management accounts and a commentary on the key variances were prepared every month and a revised forecast had been produced as at 30th September and considered by the Finance & Resources Committee. The HPC remains on course to generate a modest surplus. A further forecast is scheduled at the nine month period end at 31st December.
- 2.10 The HPC's reserves policy is to retain an amount equivalent to three average months of operating expenditure (around £3.3 million) in the form of liquid investments and working capital (before deducting deferred income).
- 2.11 The level of these reserves is monitored closely. As at 30th September 2008 we noted that the sum of working capital and investments amounted to £5.8 million. In our view, this approach should enable the HPC to manage any immediate financial pressures (such as tribunal exceptional costs) in the short term.
- 2.12 The HPC's Council and the Finance & Resources Committee were also provided with the reports necessary to enable them to undertake their functions. Additional papers are regularly prepared on key emerging issues. For example, we noted that an update on the planning work that has already been undertaken to ensure that the HPC is able to meet IFRS will be presented to the coming Audit Committee meeting.
- 2.13 In accordance with best practice, the HPC has taken steps to review its investment approach in the light of recent turbulence in the global financial markets. The Finance & Resources Committee approved the further diversification of the HPC's money market balances across several mainstream credit-worthy UK financial institutions.
- 2.14 However, we believe that the approach should be consistently applied across all of the HPC's funds and consideration should also be given to the potential exposures in placing all the HPC's funds under management with one fund manager that have recently become more apparent in the current economic climate. We therefore raised a recommendation in relation to this area.
- 2.15 There remains some scope for improving financial processing, although the key month end reconciliations and checks were all being performed on a timely basis.
- 2.16 Some disruption to the financial processing arose as a result of the difficulties experienced by the HPC with the implementation of the PRS system. These had an immediate impact and created a backlog in purchase order processing and a difference on the purchase ledger reconciliation that needed to be cleared. Additional staff resources were deployed to address this matter and we understand that the backlog has now been cleared and the difference has been reconciled.

- 2.17 The implementation has now also been deferred until such time that the business case for the systems can be revisited and a full lessons learned analysis has been completed. We concur with this approach and also note that the Director of Finance will be providing the Audit Committee with a separate paper on this matter at its December 2008 meeting.
- 2.18 Our testing also indicated that tight control is maintained over cash, credit cards and expense claims. However, we noted that the HPC's procedures were not being followed in all cases and some month end procedures need to be tightened to meet best practice. We raised four further recommendations in relation to these matters.
- 2.19 Finally, we wish to thank all members of staff for their availability, co-operation and assistance during the course of our review.

PKF (UK) LLP
November 2008

3 Detailed findings

Background

- 3.1 The HPC's budget for 2008/09 anticipates that the organisation will receive around £13.7 million this year from applicants and registrants' fees (£12.3 million - 2007/08). This is the organisation's primary source of income. Around £175,000 is budgeted to be received from investment income. The HPC's original budget aims to generate a small surplus of just under £250,000 for 2008/09.
- 3.2 The main components of the organisation's budgeted expenditure for 2008/09 relates to the following departments:
- Communications (£1.0 million);
 - Fitness to practice (£4.6 million);
 - Registrations (£1.7 million);
 - IT department (£1.1 million); and
 - Facilities management (£0.9 million).
- 3.3 Payroll costs including temporary staff amount to around £5 million each year.
- 3.4 The HPC has net assets amounting to just over £2.1 million as at 30th September 2008. Tangible fixed assets amounted to just over £4 million, over £3.3million of which relates to the organisation's premises in Kennington. A capital budget of around £1million was set for 2008/09, which is to be used to continue the renovation of 22-26 Stannary Street and to undertake various ICT project. Financial investments, including deposits and equities were valued at around £1.6 million as at 30th September 2008, although these are expected to fall in value to £1.5 million by year end due to the present economic environment. The HPC had cash holdings of just over £5.6 million as at 30th September 2008. Almost all of this balance is held on a special interest bearing account earning 4.5% per annum at present rates.

Financial management

Budget setting

- 3.5 The Five Year Plan quantifies HPC's Strategic Intent in financial terms. It is used for longer term planning, including fee setting. It is an Excel spreadsheet model containing two years actual results, five years forecasts and the current year budget. The model also includes the main non-financial trends (e.g. growth of registrant numbers) together with inflation estimates.

- 3.6 The Five Year Plan is generally updated between August and October following detailed discussions with budget holders to reflect updates to the assumptions previously made. A draft version of the revised plan is then considered by the Executive Management Team (“EMT”) and reviewed against the HPC’s strategy and objectives going forward.
- 3.7 Once EMT has approved the Five Year Plan, a final version is sent to the Chief Executive, Finance and Resources Committee & Council for approval. The latest version of the Five Year Plan was approved by the Finance & Resources Committee in November 2008.
- 3.8 The preparation of the annual budget is co-ordinated by the Finance Department in accordance with a timetable designed to enable the Finance & Resources Committee and the Council to approve the budget in March.
- 3.9 The Financial Controller prepares a budget preparation pack for budget holders including the Five Year Plan targets, prior year actual results, latest estimated spend for the current year, budget lines and instructions.
- 3.10 Budget holders are required to complete a standard template setting out their expected expenditure budgets for the coming year. These are then discussed with them in detail by the Chief Executive, the Director of Finance and the Financial Controller.
- 3.11 The budget is then updated to reflect these discussions and further review meetings are held where necessary to arrive at a final version. Budget holders are required to sign up formally to confirm their ownership of the budget.
- 3.12 The Financial Controller prepares the income budget. This is produced following discussions with the Policy and Registrations Departments and the Operations Director and draws upon the latest estimate of current year income and the Five Year Plan.
- 3.13 The expenditure budget preparations include consideration of prior year actual expenditure together with known shifts in projects and programmes scheduled for the financial year.
- 3.14 Once all the budget submissions have been received, the Financial Controller collates the data to produce an overall draft HPC budget for discussion with the Director of Finance and the Chief Executive.
- 3.15 Once they have approved the budget it is then presented to the Finance & Resources Committee for consideration before being recommended to Council for approval.
- 3.16 Our review indicated that the annual budget for 2008/09 was prepared in accordance with the HPC’s strategic objectives and approved by the Finance & Resources Committee and Council.
- 3.17 In our view the arrangements set out above enable the HPC to effectively manage the risk that there may be a mismatch between Council goals and approved financial budgets.

Budgetary control and financial reporting

- 3.18 We noted that management accounts are produced on a monthly basis. The Finance Department aims to issue these within fifteen working days of each month end. These include detailed management accounts for income and operating expenditure, income by profession, expenditure report by department, balance sheet, capital expenditure analysis against budget and a cash flow forecast.
- 3.19 In our view the detailed information provided in the management accounts enables EMT and the Finance Department to monitor and to take the necessary action to address cash flow shortfalls (the cash flow forecast), unexpected rises in operating expenses - especially tribunal exceptional costs- (income and expenditure account) and loss in value of the HPC's investment portfolio (balance sheet).
- 3.20 The balance sheet also highlights the HPC's working capital position enabling management to assess the organisation's success in collecting debts when they fall due and its capacity to pay creditors on time.
- 3.21 The HPC's reserves policy is to retain an amount equivalent to three average months of operating expenditure (around £3.3 million) in the form of liquid investments and working capital (before deducting deferred income). The level of these reserves is monitored closely. As at 30th September 2008 we noted that the sum of working capital and investments amounted to £5.8 million. In our view, this approach should enable the HPC to manage any immediate financial pressures (such as tribunal exceptional costs) in the short term.
- 3.22 The management accounts are reviewed in detail by EMT each month. The Financial Controller prepares a narrative summary (Variance Commentary) explaining the key variances and drivers of the HPC's financial position.
- 3.23 As at 30th September, the HPC was over £525,000 in surplus against budget reflecting an adverse income variance of just under £180,000 and an under-spend of over £600,000 against budgeted expenditure for the year to date.
- 3.24 As was the case during 2007/08, we are advised that the financial position will continue to be scrutinised closely by EMT as the year progresses. A revised financial forecast was prepared as at 30th September and considered by the November meeting of the Finance & Resources Committee. A further forecast is scheduled at the nine month period to 31st December. The Finance & Resources Committee routinely receives a copy of the latest year to date Variance Commentary and Management Accounts. The Council routinely receives a copy of the summarised financials which is presented as part of the Chief Executive's Report to Council.

Financial processing

Income systems

- 3.25 Income from registration fees is charged in accordance with the Fees Order approved by Parliament. Since June 2007, the following fees have been chargeable across all professions:
- Initial registration fee of £50;
 - Readmission fee (registrant comes back on to the register) of £110;
 - Yearly registration renewal of £72/ six monthly renewal of £36;
 - One-off international scrutiny fee of £400; and
 - One-off grand-parenting scrutiny fee of £400.
- 3.26 Payment methods include direct debit, credit cards and cheques. It is the HPC's policy not to accept cash payments. Our sample testing did not identify any such payments. Scrutiny fees cannot be paid for by direct debit. Just over 80% of registration income is received by direct debit thereby significantly reducing the HPC's exposure to debt collection risks or mail strikes. As part of the registration process, potential registrants are encouraged to provide the Registration Department with direct debit instructions. These details are then scanned and input into the Netregulate system and the physical mandate is sent off to the bank of the registrant. A period of fifteen working days is permitted between sending the mandate to the bank and collecting the fee so that the bank can activate the direct debit instruction.
- 3.27 The Finance Department match and post direct debit receipts to the Registrants' accounts on the Netregulate system using payment reports downloaded from BACS. Rejections arise when the HPC receives notice from the registrant's bank (bank statement) that their direct debit mandate arrangement has been rejected. In these circumstances, the Transactions Manager contacts the registrant by letter within 10 days of receiving bank notification, and three weeks grace is allowed for them to pay the fee owing or to set up a new direct debit.
- 3.28 If no contact is made by the end of the three weeks, the registrant is advised in writing by the Finance Department that they will be lapsed from the register and will have to go through the readmission process to come back onto the register.
- 3.29 Credit card income is received from the UK and International Registrations Departments. The receipts are significantly different. At the end of each day both departments print off a reconciliation report from their Streamline credit card machines and check it to a reconciliation listing of all the transactions posted by their individual departments to confirm that all credit cards payments have been received and recorded - thereby mitigating the risk of credit card fraud.

- 3.30 Cheques for fee income are received through the post. Mail is received in the post room and distributed to the various departments. The Registration Department inputs the money received from the registration applicant onto the Netregulate system and records the income on individual logs titled "General Cheques Received."
- 3.31 On a daily basis the cheques are taken to the Finance Department and kept overnight in a locked safe. There are two keys for the safe (one is kept by the Financial Accountant and other kept by the Facilities Manager).
- 3.32 Each morning the Transactions Officer checks the cheques received to the log and to Netregulate and evidences this check on the log. The paying in slip is completed and monies are banked daily. The Courier company (TNT Express) signs for receipt of the cheques and postal orders and the Finance Department also signs the courier sheet.
- 3.33 Registrants can seek a refund of their registration, by three methods – voluntary removal, becoming lapsed from the register with credit on their account and overpayment. Refunds can only be paid by cheque in accordance with the HPC's cheque payment procedures. Only Finance Department staff members can action refunds on Netregulate and issue cheques.
- 3.34 Our sample testing indicated that these controls were operating effectively.
- 3.35 However, the September 2008 management accounts include an adverse income variance of some £83,000 relating to the recognition of dietitians renewal fee income one month early in the 2007/08 financial statements. We understand that this was due to an error in the whole income analysis model used by the Finance Department to account for income from registrants.
- 3.36 Following a recent investigation by HPC, we are advised that the error was created by a timing issue regarding the Income Transfer report, which was run late (on 3rd January and not 1st January).
- 3.37 Management intends to amend existing procedures to require the Registrations and IT Departments to notify the Finance Department of any report delays in the future so that any potential errors can be identified quickly and corrected. Since management is already taking action to address this matter, we have not raised a recommendation.
- 3.38 The external auditors previously recommended that the whole income analysis model spreadsheet should be password to ensure only suitable authorised personnel can access the key spreadsheet. Consideration should also be given as to protecting key calculation cells within the spreadsheet to protect against accidental overtyping of key cells. We are advised that this has now been implemented.

3.39 Nevertheless, we believe that spreadsheets such as the income analysis model and fixed asset register are inherently prone to inadvertent input errors and there may still be a risk that other spreadsheets used by the Finance Team may contain formula errors.

3.40 We have therefore raised a recommendation in relation to this matter.

Recommendation

R1. An inventory of all the key spreadsheets used by the Finance Team for accounting purposes should be prepared. This inventory should then be used as the basis for scheduling periodic checks of the integrity of the data and formulae contained within each spreadsheet.

3.41 In their last management letter the external auditors also recommended that the Finance team should reconcile the figures recorded in the main accounting system to Netregulate on a monthly basis, with differences investigated as they arise.

3.42 At the time of our visit a reconciliation of the balances recorded on the two systems as at September 2008 had been completed. Management recognise that this now needs to be taken forward and undertaken on a monthly basis as recommended.

3.43 We have not therefore raised a further recommendation in relation to this matter, although the external auditors will no doubt expect to see that the reconciliation has indeed been completed on a monthly basis from now on, when they undertake their final accounts audit.

Expenditure systems

3.44 Payroll costs are the most significant area of expenditure incurred by the HPC, representing around £5 million (37%) of total budgeted expenditure for 2008/09. As a result, the number of full time equivalent staff is considered carefully as part of the annual budget setting process. The Financial Controller obtains details of all proposed new posts from budget holders. These are sent to the Director of Human Resources in the first instance to obtain a salary rating ("IDS"). Posts are then discussed with the Chief Executive before being incorporated within the HPC's annual budget.

3.45 Payroll is processed on a Sage stand alone system within the Finance Department. System access is password restricted to two members of the Finance Team.

3.46 Permanent payroll changes such as starters, leavers and salary changes are initiated upon receipt of the relevant supporting documentation from the HR Department. For example for all new employees a copy of their employment contract, P45 and payroll detail form are required before the individual can be set up on the HPC's payroll.

3.47 Temporary amendments to the payroll such as overtime can only be processed upon receipt of an overtime claim form that has been signed by the relevant line manager.

- 3.48 Before processing the payroll, each departmental manager is emailed the staff cost break down for their department requiring them to confirm the amount to be charged against their budget.
- 3.49 The Human Resources Department is also emailed the total number and names of employees that are about to be paid so that these can be checked for “ghost” employees.
- 3.50 Two pay runs are undertaken each month: one for employees and one for Council and Committee members. An excel spreadsheet (payroll summary form) is used to update the payroll system for any amendments required. The pay run is then prepared and a pre-check folder is also produced including the key payroll reports for the month.
- 3.51 The reports are reviewed and signed by the Director of Human Resources, the Director of Finance and the Chief Executive before the payment is authorised. Payments are made using the Natwest Autopay facility. The Autopay and Credit Transfer forms require the signature of two individuals included on the HPC’s bank mandate before being faxed to Natwest for processing. Our sample testing indicated that these controls were operating effectively and should ensure that the risk of unauthorised payments to personnel is mitigated.
- 3.52 The remaining £8.5 million of the HPC’s annual budgeted expenditure is subject to purchase ledger controls and procedures.
- 3.53 There are four main categories of purchase ledger transaction as follows:
- Council/ committee members’ allowances and expenses;
 - Partners’ expenses;
 - Employees’ expenses; and
 - Purchases from suppliers.
- 3.54 There are three possible tax categories for Council/ Committee members. Category 1 members are treated as office holders and payments to them are therefore processed through the HPC payroll in accordance with the procedures described in the paragraphs above.
- 3.55 Category 2 members claim expenses through their employer. The employer invoices the HPC and the invoice is processed through the purchase ledger. Category 3 members are registered as self-employed. Members are required to declare their tax status upon appointment and complete the declaration forms. These are held on file in the Finance Department. Category 2 and 3 members are required to complete a claim form, attaching the supporting receipts for all claims above £5 before submitting the claim to the Finance Department for processing. The Transaction Officer date stamps the forms received.

- 3.56 The Purchase Ledger Officer then completes a Purchase Ledger Detail form and records the claim as “unauthorised” on the purchase ledger. The claim is then sent to the relevant budget holder for authorisation.
- 3.57 Partners include visitors, registration, legal and medical assessors, panel members and chairmen. In almost all cases they are deemed to be self-employed and are required to complete a Partners Expense Claim form, attaching the relevant invoice, which is checked and authorised in the same way as for category 2 and 3 members.
- 3.58 Employees are required to complete an expense claim form, attaching the supporting receipts for all claims above £5 and obtaining authorisation from their line manager (or the Chief Executive) before submitting the claim to the Finance Department for processing in accordance with the purchase ledger procedures noted above. Claims made by the Chief Executive require the authorisation of the President and the Director of Finance.
- 3.59 Our sample testing indicated that the HPC’s procedures for processing were operating effectively and should mitigate the risk of expense claim abuse by members, partners and employees.
- 3.60 During the year the HPC purchased the On-line Purchase Requisition System (“PRS”) and Sage Project Accounting. PRS went live on 1st July but both systems were taken offline from 1st September following implementation difficulties and the organisation reverted to manual purchase ordering from that time onwards.
- 3.61 The immediate impact of this was that there was a backlog in purchase order processing and a difference on the purchase ledger reconciliation that needed to be cleared. Additional staff resources were deployed to address this matter and we understand that the backlog has now been cleared.
- 3.62 The implementation has now been deferred until such time that the business case for the systems can be revisited and a full lessons learned analysis has been completed. We concur with this approach and also note that the Director of Finance will be providing the Audit Committee with a separate paper on this matter at its December 2008 meeting.
- 3.63 The manual procedures that have been reintroduced are as follows. Purchases from suppliers are to be made in accordance with the following procedures.
- 3.64 Each department is required to complete a pre-numbered, three part purchase order which must be approved by a budget holder or their delegate named on the purchase order/ invoice signatory list. The department send the white copy of the order to the suppliers directly and retain the blue and pink copies.

- 3.65 Invoices are sent to the Finance Department by the supplier. Upon receipt of the supplier invoices, the Finance Department date stamp and sign these and attach them to a Purchase Ledger Detail form.
- 3.66 The invoices are batched and posted to the purchase ledger “unauthorised invoices” control account.
- 3.67 The supplier invoice and payment authorisation sheet is then sent to the budget holder for payment approval. Transactions above £8,000 require the additional authorisation of the Chief Executive. The President is required to countersign transactions above £25,000. The budget holder signs the Purchase Ledger Detail form, codes the expense and attaches the pink copy of the purchase order.
- 3.68 These controls should mitigate the risk of unauthorised purchases from suppliers. The Financial Accountant subsequently reviews the expense codes and amends as necessary e.g. capitalises the item before updating the invoice details on the purchase ledger. Our sample testing indicated that controls over purchases from suppliers were operating effectively.
- 3.69 Purchase ledger payments are made by BACS, manual cheque or e-banking. Payment runs are undertaken every two weeks. The Purchase Ledger Officer prepares a Suggested Payment Run report and attaches the relevant invoices, which are reviewed by the Director of Finance who signs and dates the relevant report. The e-banking report is reviewed by the Chief Executive. For BACS payments, a BACS form is completed and checked back to the relevant payment report before it is faxed to Natwest for processing.
- 3.70 Blank manual cheques are held securely in the safe. All cheques need to be signed by two individuals included on the HPC’s bank mandate. The signatories check the invoice details and the payment report before signing the cheques.
- 3.71 We noted that manual cheques are rarely issued and are checked carefully. This should enable the HPC to mitigate the risk of forged cheques.
- 3.72 Our testing indicated that these controls were operating effectively in most cases. However we noted that on two occasions the suggested payment report for purchases ledger payments had only been signed by one authorised signatory. This has subsequently been corrected and the relevant cheques were appropriately authorised. However, we have raised a recommendation in relation to this matter.

Recommendation

R2. Suggested cheque payment reports should be signed by two signatories in all cases as required by procedures.

Main accounting and balance sheet systems

- 3.73 The HPC upgraded its financial system Sage Line 200 on 1st April 2008. A trial balance is produced routinely at month end and the HPC's income and expenditure and balance sheet items are clearly set out in the organisation's coding structure. From our review of the trial balance, we noted that there is an imbalance of £1.
- 3.74 Although the difference between debit and credit entries is small, it may be indicative of potential system related problems that may have a larger impact in the future if it is not addressed now. We have therefore raised the following recommendation.

Recommendation**R3. The £1 difference on the trial balance should be investigated and corrected.**

- 3.75 The Finance Director documents his review of the month end balances on the face of a copy of the management accounts. This includes evidencing that he has checked the balances in the accounts back to source documents such as the key control account reconciliations and reports from the HPC's Fund Managers on investments.
- 3.76 However, we noted that the trial balance is not routinely printed off each month with the result that the check of the trial balance to the reported management accounts is not clearly evidenced. We have therefore raised a further recommendation in relation to this matter.

Recommendation**R4. The review of the trial balance against the reported management accounts should be formally evidenced at least on a quarterly basis in line with reporting to the Finance & Resources Committee.**

- 3.77 The key routines that are undertaken to close down the various ledgers at month end are as follows. Before closing down the purchase ledger the Purchase Ledger Officer confirms that there are no remaining invoices or expenses to be posted. An aged creditors report is then printed off and reviewed to ensure that no duplicate or incorrect postings have been made and checked to confirm that the total agrees to the balance recorded on the nominal ledger.
- 3.78 Our review of the purchase ledger reconciliations indicated that they had been prepared and reviewed as required. However, we noted that at the time of our review there was a difference of just over £2,000 between the report listing invoices awaiting approval and the main accounting system code balance that was being investigated by the Financial Controller. This matter has since been resolved. We have not therefore raised a recommendation in relation to this matter.
- 3.79 The HPC's sales income is recorded on the Netregulate system and then imported to the Sage nominal ledger in batches during the month.

- 3.80 Interface reports are produced to confirm that the transactions recorded on the Netregulate system have been correctly imported into Sage. The unused Sage sales ledger still however needs to be closed down at month end. As noted in the previous section of this report, a reconciliation between the figures recorded in the main accounting system to Netregulate on a monthly basis has now also been prepared as at 30th September 2008.
- 3.81 As noted above, the HPC's payroll is processed on a standalone system and journalled into the main accounting system when the pay runs have been processed. The fixed asset register is Excel based and any movements on fixed assets are also entered into the nominal ledger by journal.
- 3.82 Written procedures have been established to control the purchase and disposals of fixed assets, thereby mitigating the risk of unauthorised purchases or theft of assets.
- 3.83 Once the bank reconciliation has been completed the Sage cash book can be closed down. Bank reconciliations are then prepared and reviewed on a monthly basis. Our sample testing indicated that these controls were operating effectively.
- 3.84 As at 30th September the HPC's invested funds comprised principally £5.6 million invested in a Special Interest Bearing (money market) Account and £1.5 million held under management by Rensburg Sheppards. The annual fund performance is reviewed by the Finance & Resources Committee in November each year, along with the Investment Policy.
- 3.85 The fund managers also provide the HPC with a monthly investment valuation report (summary and detail) to the Financial Controller to update the valuation in the Management Accounts. In our view, these regular review and reporting procedures should enable the HPC to identify and manage the impact of any fall in the value of its investment portfolio and to identify any concerns relating to the ongoing solvency and capability of its fund managers.
- 3.86 In accordance with best practice, the HPC has taken steps to review its investment approach in the light of recent turbulence in the global financial markets. We noted that a paper was considered by the Finance & Resources Committee in November 2008 regarding the HPC's money market investments. The Committee approved the further diversification of the HPC's money market balances across several mainstream credit-worthy UK financial institutions. The aim of this step being to mitigate the HPC's exposure to the failure of any one financial institution. We concur with this approach.
- 3.87 However, we believe that the approach should be consistently applied across all of the HPC's funds and consideration should also be given to the potential exposures in placing all the HPC's funds under management with one fund manager that have recently become more apparent in the current economic climate.

3.88 We have therefore raised the following recommendation in relation to this area.

Recommendation

R5. The HPC should reconsider its approach to placing funds under management. Specific consideration should be given to diversification of the investment across a number of fund managers and the credit-worthiness of each fund manager selected.

Follow up of our previous recommendations

3.89 In our previous report on the HPC's financial systems dated November 2007, we raised three recommendations in relation to the following areas:

- Non-aggregation of assets and liabilities in balance sheet reporting;
- Invoice authorisation; and
- Date stamping purchase ledger invoices.

3.90 We are pleased to note that, our sample testing did not identify any departures from the strengthened procedures recommended in our previous report.

4 Action plan

Ref.	Findings	Recommendations	Priority	Management Response <i>Responsible Officer</i>	Due Date
	Income systems				
R1	The external auditors previously recommended that the whole income analysis model spreadsheet should be password to ensure only suitable authorised personnel can access the key spreadsheet. Consideration should also be given as to protecting key calculation cells within the spreadsheet to protect against accidental overtyping of key cells. We are advised that this has now been implemented. Nevertheless, we believe that spreadsheets such as the income analysis model and fixed asset register are inherently prone to inadvertent input errors and there may still be a risk that other spreadsheets used by the Finance Team may contain formula errors.	An inventory of all the key spreadsheets used by the Finance Team for accounting purposes should be prepared. This inventory should then be used as the basis for scheduling periodic checks of the integrity of the data and formulae contained within each spreadsheet.	Medium	The Financial Controller will action and undertake monthly checks. The Director of Finance will also review key spreadsheets used in preparing accounting entries on a quarterly basis. <i>Financial Controller</i>	March 2009

Ref.	Findings	Recommendations	Priority	Management Response <i>Responsible Officer</i>	Due Date
	Expenditure systems				
R2	We noted that on two occasions the suggested payment report for purchases ledger payments had only been signed by one authorised signatory. This has subsequently been corrected and the relevant cheques were appropriately authorised.	Staff should be reminded that suggested cheque payment reports should be signed by two signatories in all cases as required by procedures.	Medium	The Financial; Controller will remind the Purchase Ledger Officer to always ensure two signatories on the reports for purchase ledger payments <i>Financial Controller</i>	December 2008
	Main accounting / balance sheet systems				
R3	From our review of the trial balance, we noted that there is an imbalance of £1. Although the difference between debit and credit entries is small, it may be indicative of potential system related problems that may have a larger impact in the future if it is not addressed now	The £1 difference on the trial balance should be investigated and corrected.	Medium	The Financial Controller will investigate and action. <i>Financial Controller</i>	December 2008

Ref.	Findings	Recommendations	Priority	Management Response <i>Responsible Officer</i>	Due Date
	Main accounting / balance sheet systems				
R4	We noted that the trial balance is not routinely printed off each month with the result that the check of the trial balance to the reported management accounts is not clearly evidenced.	The review of the trial balance against the reported management accounts should be formally evidenced at least on a quarterly basis in line with reporting to the Finance & Resources Committee.	Medium	The Director of Finance will print and check records on a quarterly basis. <i>Director of Finance</i>	December 2008

Ref.	Findings	Recommendations	Priority	Management Response <i>Responsible Officer</i>	Due Date
	Main accounting / balance sheet systems				
R5	<p>We noted that a paper was considered by the Finance & Resources Committee in November 2008 regarding the HPC's money market investments. The Committee approved the further diversification of the HPC's money market balances across several mainstream credit-worthy UK financial institutions.</p> <p>However, we believe that this approach should be consistently applied across all of the HPC's funds and consideration should also be given to the potential exposures in placing all the HPC's funds under management with one fund manager that have recently become more apparent in the current economic climate.</p>	<p>The HPC should reconsider its approach to placing funds under management. Specific consideration should be given to diversification of the investment across a number of fund managers and the credit-worthiness of each fund manager selected.</p>	Medium	<p>The Director of Finance will implement the recommendation.</p> <p><i>Director of Finance</i></p>	December 2008

5 Assurance definitions

Assurance Level	Definition
Sound	Satisfactory design of internal control that addresses risk and meets best practice and is operating as intended.
Satisfactory	Satisfactory design of internal control that addresses the main risks but falls short of best practice and is operating as intended.
Satisfactory in Most Respects	Generally satisfactory design of internal control that addresses the main risks and is operating as intended but either has control weaknesses or is not operating fully in some significant respect.
Satisfactory Except For.....	Satisfactory design of internal control that addresses the main risks and is operating as intended in most respects but with a major failure in design or operation in the specified area.
Inadequate	Major flaws in design of internal control or significant non operation of controls that leaves significant exposure to risk.