

Audit Committee Meeting – 9 December 2009

Internal audit finance 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 requested to review and approve the report.

Background information

The Financial Systems Review report produced a satisfactory rating and one recommendation.

Resource implications

Nil

Financial implications

As budgeted.

Appendices

Appendix One – PFK Audit Report

Date of paper

29 November 2009

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Health Professions Council

Financial systems review 2009/10

Final November 2009

Confidential



Accountants &
business advisers

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Project timescales

Date project commenced	09/11/09
Date field work completed	13/11/09
Date draft report issued	23/11/09
Date final management comments received	24/11/09
Date final report issued	25/11/09

1 Introduction and scope

1.1 In accordance with the 2009/10 internal programme for the Health Professions Council (“HPC”) that was agreed with the Audit Committee in February 2009, 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 2009/10 were as follows:

Financial management	Financial processing
Mismatch between Council goals & approved financial budgets	Registrant credit card record fraud/ theft
Insufficient cash to meet commitments	Receipt of fee income as per collection schedule
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
Inability to collect from debtors	Financial distress of suppliers
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.

- PAYE/NI compliance;
- Corporate tax 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 scheme valuation deficit; 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. There has been no indication that controls have weakened in that area since the time of our last review and we have therefore focused our audit activity towards other areas where there is a greater need for assurance.

1.6 We also followed up the recommendations that we raised as part of our 2008/09 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 2009.

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 2009/10 anticipated that the organisation would receive around £15.6 million this year from applicants and registrants' fees (£13.7 million - 2008/09). This is the organisation's primary source of income. Around £175,000 was budgeted to be received from investment income. The HPC's original budget aimed to generate a small surplus of just under £13,000 for the year before investment income.
- 2.3 All financial processing is undertaken in-house by the Finance Department. A new Director of Finance was appointed in May 2009 but otherwise the team has remained largely as it was at the last time we reviewed this area. 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 system.

Our assessment

- 2.4 Based on our review work, we have concluded that the HPC's financial systems were **satisfactory** and were operating effectively at the time of our audit visit. However, we noted one area where there remains scope for improvement to enhance the control framework and to meet best practice going forward.
- 2.5 The principal findings of our work are set out in the paragraphs below.

Principal findings

- 2.6 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.
- 2.7 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 in November 2009.
- 2.8 The HPC is now forecasting that it will incur a deficit of around £150,000 compared with the original budgeted surplus of just under £13,000. We understand that this was largely due to a lower than anticipated level of international scrutiny fee income and a fall in international registrants generally.

- 2.9 To address these matters, EMT reviewed the HPC's expenditure budget and identified some areas where costs could potentially be reduced e.g. by deferring some staff appointments and by reflecting the re-phasing of some projects within the budget.
- 2.10 We also noted that a detailed paper on projected registrant numbers over the next five years was considered by the Finance & Resources Committee meeting. We believe that this analysis should assist the HPC in challenging the underlying assumptions behind its forecasts of registrant numbers going forward.
- 2.11 The HPC's reserves policy is to retain an amount equivalent to a minimum of three average months of operating expenditure (around £3.9 million) in the form of liquid investments and working capital (before deducting deferred income). We noted that the reserves policy was reviewed in detail at the 16th March 2009 meeting of the Finance & Resources Committee, when it was agreed to continue with the policy as it stood following a consideration of the likely impact on reserves of the current Five Year Plan.
- 2.12 The level of these reserves is monitored closely. As at 31st July 2009 we noted that the sum of working capital and investments amounted to £7.3 million before deducting deferred income. In our view, this approach should enable the HPC to manage any immediate financial pressures (such as tribunal exceptional costs) in the short term.
- 2.13 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.
- 2.14 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.
- 2.15 The Finance & Resources Committee approved the further diversification of the HPC's money market balances across several mainstream credit-worthy UK financial institutions and considered the performance of the HPC's fund managers in detail.
- 2.16 Our sample testing indicated that the key month end reconciliations and checks were all being performed on a timely basis.
- 2.17 We also noted that a suspense account is maintained as code 9999. This code includes various transactions that have been identified as requiring amendment or further investigation before the correct entry can be recorded. Our review of the suspense account transactions indicated that the required amendments related to duplicate claims and invoices, coding errors and invoices where the code had not been identified at the outset.
- 2.18 We noted that all of these items had been corrected by management on a timely basis and the balance on the suspense account as at 20th October was £Nil. We have not therefore raised a recommendation in relation to this matter.

- 2.19 Our testing indicated that tight control is maintained over cash, credit card receipts and expense claims. We only noted one isolated departure from the required procedures in relation to expense claims. The claim in question had however been appropriately authorised before payment as required.
- 2.20 We also noted that procedures were operating as expected over purchase ledger processing, although there is scope for refining these procedures now to ensure that the full benefits of the PRS automated purchase ordering system are delivered. We have therefore raised a recommendation in relation to this matter.
- 2.21 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 2009

3 Detailed findings

Background

- 3.1 The HPC's budget for 2009/10 anticipated that the organisation would receive around £15.6 million this year from applicants and registrants' fees (£13.7 million - 2008/09). This is the organisation's primary source of income. Around £175,000 was budgeted to be received from investment income. The HPC's original budget aimed to generate a small surplus of around £13,000 for the year before investment income. The HPC has also received a grant during 2009/10 amounting to around £360,000 from the Department of Health to fund a revalidation project.
- 3.2 The main components of the organisation's budgeted expenditure for 2009/10 related to the following departments:
- Communications (£1.0 million);
 - Fitness to practice (£5.6 million);
 - Registrations (£2.0 million);
 - IT department (£0.9 million); and
 - Facilities management (£0.9 million).
- 3.3 Payroll costs including temporary staff were budgeted to be around £5.3 million.
- 3.4 The HPC had net assets amounting to just over £2.4 million as at 31st March 2009. Tangible fixed assets amounted to around £3.7 million, over £3 million of which relates to the organisation's premises in Kennington. A capital budget of around £0.8million was set for 2009/10, which is primarily to be used to undertake various ICT projects.
- 3.5 Financial investments, including deposits and equities were valued at just over £1.3 million as at 31st March 2009. The HPC had cash holdings of just over £5.3 million as at 31st March 2009.

Financial management

Budget setting

- 3.6 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.

- 3.7 The Five Year Plan is updated between August and October following detailed discussions with budget holders to reflect updates to the assumptions previously made.
- 3.8 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.
- 3.9 Once EMT has approved the Five Year Plan, a final version is sent to the Chief Executive, Finance and Resources Committee & Council for approval. We noted that the latest version of the Five Year Plan was approved by the Finance & Resources Committee in November 2009.
- 3.10 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 at its March meeting.
- 3.11 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.
- 3.12 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.
- 3.13 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.
- 3.14 The Financial Controller prepares the income budget. This is produced following discussions with the Policy and Registrations Departments (to clarify the assumptions regarding registrant numbers) and the Operations Director and draws upon the latest estimate of current year income and the Five Year Plan.
- 3.15 The expenditure budget preparations include consideration of prior year actual expenditure together with known shifts in projects and programmes scheduled for the financial year.
- 3.16 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.
- 3.17 Once they have approved the budget it is then presented to the Finance & Resources Committee for consideration before being recommended to Council for approval.
- 3.18 Our review indicated that the annual budget for 2009/10 was prepared in accordance with the HPC’s strategic objectives and approved by the Finance & Resources Committee on 16th March 2009 and Council at its meeting on 26th March 2009.

- 3.19 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

- 3.20 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.
- 3.21 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 any potential loss in value of the HPC's investment portfolio (balance sheet).
- 3.22 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.
- 3.23 The HPC's reserves policy is to retain an amount equivalent to a minimum of three average months of operating expenditure (around £3.9 million) in the form of liquid investments and working capital (before deducting deferred income). We noted that the reserves policy was reviewed in detail at the 16th March 2009 meeting of the Finance & Resources Committee, when it was agreed to continue with the policy as it stood following a consideration of the likely impact on reserves of the current Five Year Plan.
- 3.24 The level of these reserves is monitored closely. As at 31st July 2009 we noted that the sum of working capital and investments amounted to £7.3 million before deducting deferred income. In our view, this approach should enable the HPC to manage any immediate financial pressures (such as tribunal exceptional costs) in the short term.
- 3.25 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.
- 3.26 This indicated that the HPC is now forecasting that it will incur a deficit of just under £150,000 compared with the original budgeted surplus of just under £13,000. We understand that this was largely due to a lower than anticipated level of international scrutiny fee income and a fall in international registrants generally.

- 3.27 To address these matters, EMT reviewed the HPC's expenditure budget and identified some areas where costs could potentially be reduced e.g. by deferring some staff appointments and by reflecting the re-phasing of some projects within the budget.
- 3.28 We also noted that a detailed paper on projected registrant numbers over the next five years was considered by the Finance & Resources Committee meeting. We believe that this analysis should assist the HPC in challenging the underlying assumptions behind its forecasts of registrant numbers going forward.
- 3.29 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.
- 3.30 A further forecast is scheduled at the nine month period to 31st December, which will be reported to the February 2010 meeting of the Finance & Resources Committee.
- 3.31 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. For example, the July financial position was reported to the Council meeting on 10th September 2009.

Financial processing

Income systems

- 3.32 Income from registration fees is charged in accordance with the Fees Order approved by Parliament. The following fees are currently chargeable across all professions:
- Initial registration fee of £53;
 - Readmission fee (registrant comes back on to the register) of £115;
 - Yearly registration renewal of £76;
 - One-off international scrutiny fee of £420; and
 - One-off grandparenting scrutiny fee of £420.
- 3.33 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.

- 3.34 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.
- 3.35 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.
- 3.36 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.
- 3.37 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.
- 3.38 Credit card income is received from the Registration Department. At the end of each day the Department prints off a reconciliation report from their Streamline credit card machines and checks it to a reconciliation listing of all the transactions posted to confirm that all credit cards payments have been received and recorded - thereby mitigating the risk of credit card fraud.
- 3.39 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."
- 3.40 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).
- 3.41 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.
- 3.42 The figures recorded in the main accounting system are reconciled to Netregulate on a monthly basis, with differences investigated as they arise.
- 3.43 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.

- 3.44 Only Finance Department staff members can action refunds on Netregulate and issue cheques.
- 3.45 Our sample testing indicated that these controls were operating effectively.
- 3.46 The HPC has also received a grant amounting to around £360,000 from the Department of Health to fund a revalidation project. This was received in advance by BACS. A project code has been set up on the financial system to monitor expenditure against the grant. We understand that only a small amount of expenditure has been incurred to date but purchases will be subject to the HPC's purchase ledger controls as set out in the following paragraphs.

Expenditure systems

- 3.47 Payroll costs are the most significant area of expenditure incurred by the HPC, representing around £5.3 million (34%) of total budgeted expenditure for 2009/10. 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.
- 3.48 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.
- 3.49 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.
- 3.50 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.
- 3.51 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.
- 3.52 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.
- 3.53 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.

- 3.54 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.
- 3.55 The remaining £10.2 million of the HPC's annual budgeted expenditure is subject to purchase ledger controls and procedures.
- 3.56 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.
- 3.57 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.
- 3.58 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.
- 3.59 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 Finance Officer date stamps the forms received.
- 3.60 The Finance 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.
- 3.61 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.

- 3.62 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.
- 3.63 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. We noted one instance where the claim form had not been signed by the claimant but the claim had been authorised by the appropriate budget holder.
- 3.64 Our testing indicated that this was an isolated event and we have not therefore raised a recommendation in relation to this matter.
- 3.65 Additional controls have been introduced to mitigate the risk of financial distress of suppliers. We were advised that the financial status of the HPC's key suppliers is now periodically monitored using Experian reports.
- 3.66 We were advised that around 40% of the HPC's purchasing is now conducted using the On-line Purchase Requisition System ("PRS") that was ultimately implemented in February 2009 following various enhancements that have previously been reported to the Audit Committee. Access to the PRS system is password protected. Authorised users are required to raise a purchase request, selecting from a drop down list of approved suppliers, cost codes and authorised "approvers".
- 3.67 This generates a purchase request that is automatically transmitted to the approver(s) assigned to the cost code. A purchase order can only be created once the approver has electronically confirmed the request. Different tiers of authorisation have also been built into the system. For example if a purchase request is made for £7,500 the individuals authorised to approve expenditure between £1,001 and £8,000 for that cost code are notified. There is an automated transfer of approved orders from the PRS system to the SAGE purchase ledger.
- 3.68 We noted that the HPC's manual ordering procedures also continue to operate as follows, where the PRS system is not used. 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.
- 3.69 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. The invoices are batched and posted to the purchase ledger "unauthorised invoices" control account.

- 3.70 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 or the Chair of the Finance & Resources Committee 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.
- 3.71 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.
- 3.72 Our sample testing indicated that controls over purchases from suppliers were operating as expected. However, the continuing use of the manual procedures alongside the automated purchase ordering processes indicates that the anticipated benefits of the PRS system are not at present being delivered in full. Whilst we concur with the decision to maintain the manual procedures in operation until the PRS system became established we believe that at some point soon the option to follow manual procedures should be removed and all suppliers orders should be raised on PRS. We have therefore raised the following recommendation.

Recommendation

R1. Management should begin to take the steps necessary towards removing the option for individuals to follow manual procedures when raising supplier purchase orders.

- 3.73 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.
- 3.74 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.
- 3.75 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. We noted that the bank mandate was most recently updated from 30th July 2009 as approved by the Finance & Resources Committee.
- 3.76 The signatories check the invoice details and the payment report before signing the cheques. We noted that manual cheques are rarely issued and are checked carefully. This should enable the HPC to mitigate the risk of forged cheques.
- 3.77 Our sample testing indicated that these controls were operating effectively.

Main accounting and balance sheet systems

- 3.78 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.
- 3.79 The Director of Finance 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. A copy of the month end trial balance is also attached.
- 3.80 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.
- 3.81 The HPC's sales income is recorded on the Netregulate system and then imported to the Sage nominal ledger in batches during the month.
- 3.82 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. We noted that a reconciliation between the figures recorded in the main accounting system to Netregulate was being undertaken on a regular basis.
- 3.83 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.
- 3.84 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.
- 3.85 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.
- 3.86 As at 18th August 2009 the HPC's invested funds comprised principally £2.3 million invested in various money market accounts and special interest bearing accounts, together with £1.9 million (at market value) held under management by Rensburg Sheppards. The annual fund performance is regularly reviewed by the Finance & Resources Committee in November each year, along with the Investment Policy.

- 3.87 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.
- 3.88 The Finance & Resources Committee also undertook a formal review of the performance of the HPC's fund managers in March 2009. At that time the Committee concluded that they were satisfied with Rensburg Sheppard's performance and the appointment of an additional fund manager would not be beneficial since by liquidating any of the investments held there was a risk that losses would be realised unnecessarily.
- 3.89 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.
- 3.90 In accordance with best practice, the HPC took steps during 2008/09 to review its investment approach in the light the turbulence in the global financial markets. In November 2008 The Finance & Resources 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. This resulted in three money market providers being appointed in February and March 2009.
- 3.91 Finally, we noted that a suspense account is maintained as code 9999. This code includes various transactions that have been identified as requiring amendment or further investigation before the correct entry can be recorded. Our review of the suspense account transactions indicated that the required amendments related to duplicate claims and invoices, coding errors and invoices where the wrong amount had been posted. We noted that all of these items had been corrected by management on a timely basis and the balance on the suspense account as at 20th October was £Nil. We have not therefore raised a recommendation in relation to this matter.

Follow up of our previous recommendations

- 3.92 In our previous report on the HPC's financial systems dated November 2008, we raised five recommendations in relation to the following areas:
- The introduction of monthly checks to confirm the integrity of key spreadsheets used in the preparation of accounting entries;
 - Reminding staff to ensure that suggested cheque payment reports should be signed by two signatories in all cases;
 - Clearing the £1 difference on the trial balance;

- Evidencing the check of the monthly management accounts back to the trial balance more clearly; and
- Considering the HPC's investment strategy in the light of market uncertainty.

3.93 We are pleased to note that action has been taken to implement all of the above recommendations and that controls have been strengthened accordingly. Our more detailed follow up of the specific recommendations is reported separately in our Follow up Review report dated November 2009.

4 Management action plan

Ref.	Findings	Recommendations	Priority	Management Response <i>Responsible Officer</i>	Due Date
	Expenditure systems				
R1	Our sample testing indicated that controls over purchases from suppliers were operating as expected. However, the continuing use of the manual procedures alongside the automated purchase ordering processes indicates that the anticipated benefits of the PRS system are not at present being delivered in full. Whilst we concur with the decision to maintain the manual procedures in operation until the PRS system became established we believe that at some point soon the option to follow manual procedures should be removed and all suppliers orders should be raised on PRS.	Management should begin to take the steps necessary towards removing the option for individuals to follow manual procedures when raising supplier purchase orders.	Medium	Agreed. This will be implemented by the agreed due date. <i>Director of Finance</i>	June 2010

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.