Audit Committee - 13 March 2013

NAO Interim Audit Letter

Executive summary and recommendations

Introduction

The NAO letter is provided to the Committee for its consideration.

Decision

The Committee is asked to discuss the letter and note its contents.

Background information

The NAO carried out an interim audit visit in February 2013 and their Interim Audit Letter is attached.

Resource implications

Nil

Financial implications
NAO audit fee £39,000

Appendices
Appendix 1 : NAO Interim Audit Letter

Date of paper
4 March 2013

REPORT TO THE ACCOUNTING OFFICER
AND AUDIT COMMITTEE

Health and Care Professions Council

Interim Management Letter on the 2012-13 Financial Statement Audit

Our vision is to help the nation spend wisely.

We apply our unique perspective of public audit to help Parliament and government drive lasting improvement in public services.

The National Audit Office scrutinises public spending for Parliament and is independent of government. The Comptroller and Auditor General (C&AG), Amyas Morse, is an Officer of the House of Commons and leads the NAO, which employs some 860 staff. The C&AG certifies the accounts of all government departments and many other public sector bodies. He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively, and with economy. Our studies evaluate the value for money of public spending, nationally and locally. Our recommendations and reports on good practice help government improve public services, and our work led to audited savings of more than £1 billion in 2011.

Contents

Executive Summary

Introduction

1 This interim management report summarises the key matters, including recommendations for improvement in internal financial controls, which have come to our notice during our audit to date of the Health and Care Professions Council's (HCPC) financial statements for the year ending 31 March 2013. The report provides an update on the progress of the audit including our planning and interim audits.

2 This report has been prepared for the sole use of the HCPC. It must not be disclosed to any other third party, or quoted or referred to, without the written consent of the National Audit Office (NAO) and no responsibility is assumed by the NAO to any other person.

Significant Risks

3 We set out what we considered to be the significant risks for the audit in our Audit Planning Report presented to the Audit Committee in September 2012. An update of audit action to date is shown in Annex A. No critical issues that may impact on our overall audit opinion have been identified in our work to date on the areas identified as significant risks. We did not identify any additional matters of significant risk and our work to date has confirmed that our initial risk assessment remains appropriate.

Planning and interim audit work

4 Our approach is primarily risk-based. We updated the information we had from the previous year through interviews with HCPC staff. We also reviewed key documents to improve our understanding of HCPC's business and operations. This enabled us to form a preliminary view of the strengths and weaknesses of the overall control environment. We reviewed management controls and tested their operation in order to determine those on which we can place assurance and those where we need to direct more audit effort.

5 We undertook audit procedures on specific key account areas and evaluated results in order to support our audit opinion. We reviewed accounting systems and management controls operated by the HCPC only to the extent we considered necessary for the effective performance of the audit. As a result, our review may not have detected all weaknesses that exist or all improvements that could be made. The responsibility for public accountability and the implementation and monitoring of internal and management controls rests with the management of the HCPC.

6 We are due to undertake a further audit visit (20-22 March) to complete further transaction testing (covering period 10 and 11) and so reduce the amount of work that needs to be completed during our final audit visit.

Reporting

7 You will appreciate that, while our audit is carried out in accordance with International Standards on Auditing (UK and Ireland), it cannot, and should not, be relied upon to detect every instance of misstatement, fraud, irregularity or inefficiency, which is not material in terms of the financial statements.

8 This interim management report, which is part of the continuing dialogue between HCPC and external audit, is not prepared for any other purpose than to inform the Audit Committee and management of the key audit issues and weaknesses in the systems of internal financial controls identified during our interim audit. For this reason, we consider it inappropriate for the report to be relied upon by third parties.

Audit summary

9 We carried out our interim audit in February 2013 following the approach noted in our Audit Planning Report. Our work included:

- Review of the template period 9 account
- Controls testing on the new outsourced payroll process
- Substantive testing on expenditure;
- Testing on fixed asset additions and disposals;
- Reconciliation of Trial Balance to draft accounts;
- Starters and leavers testing; and
- Follow-up of prior year management letter points.

10 We have made two recommendations following our work. This is reported in the Audit Findings section of this report.

Other Matters of Interest

Annual Governance Statement

11 The role of the external auditor in relation to the Governance Statement will remain the same as in the prior year. Namely, the external auditor will review the Governance Statement for consistency with the audited financial statements and may report on any inconsistency with the findings of their audit or their knowledge of the business.

12 It is for the Accounting Officer to determine how to take account of input from within the organisation and from the Council and its committees. The Annual Governance Statement should be assembled from work through the year to gain assurance about the organisation's performance and risk profile, its responses to the identified and emerging risks and its success in tackling them. Council members, with the support of the Audit Committee where appropriate, should evaluate the quality of the systems of internal control and governance, assess the risks facing the organisation, and advise on any significant omissions from the statement which may necessitate further disclosure.

13 All bodies producing a Governance Statement (including Executive Agencies and Arm's Length Bodies) are required to comply with (in so far as their organisational status means that it is practicable for them to do so), or explain any departures from, the Corporate Governance Code for Departments. The external auditor may report any failure to comply with or explain any departures from the Corporate Governance Code (http://www.hm-treasury.gov.uk/d/corporate_governance_good_practice_july2011.pdf) or other authoritative guidance.

14 The NAO has recently issued a Good Governance Factsheet which provides good practice observations from our audits and aims to assist organisations when they are preparing and reviewing their own governance statement. It is available on the NAO website at: http://www.nao.org.uk/idoc.ashx?docId=0EE18D1D-567B-4826-A1F2-7FED9CDF8F37&version=-1. This document contains links to further guidance such as HM Treasury's recent publication on Assurance Frameworks which the Audit Committee may find of interest.

Sustainability Report

15 HCPC continues to fall below the threshold for exemption on the grounds of the number of staff that it employs. As such, HCPC is not required to produce a Sustainability Report, although it may still choose to do so.

Audit Findings

16 This section outlines the findings arising from our audit to date, as well as management's response to these recommendations. In order to aid the Audit Committee's and management's understanding we have prioritised our findings.

17 We have included the significant and other, less significant findings arising from our audit. Each issue has been given a priority rating to assist in assessing the level of potential risk associated with the finding. The levels are:

- **Priority 1** – major issues for the attention of senior management which may have the potential to result in a material weakness in internal control;
- **Priority 2** – important issues to be addressed by management in their areas of responsibility;
- **Priority 3** – problems of a more minor nature which provide scope for improvement.

18 As outlined in our Audit Planning Report our procedures included a review of the internal controls and accounting systems and procedures only to the extent considered necessary for the effective performance of the audit. Audit findings and observations therefore should not be regarded as representing a comprehensive statement of all the weaknesses which exist, or all improvements which could be made to the systems and procedures operated.

Observations and recommendations

19 Our audit findings from the planning and interim audit visits are noted below.

1. Disclosure of Director's remuneration in the Remuneration report (Priority 2)

Observation	In previous years only the remuneration of the Chief Executive and Council members has been disclosed in the Remuneration Report included in the Annual Report and Accounts. This was because the remainder of the Executive Management Team were not considered by HCPC to have responsibility for the strategic direction of HCPC. During 2012/13 we understand that there have been significant increases in responsibility for some Directors and so the extension of the disclosures in the Remuneration Report to include Executive Directors may now be appropriate. The Treasury's Financial Reporting Manual (FReM) requires that entities prepare a Directors' Remuneration Report in accordance with the requirements set out in the Companies Act 2006 as interpreted for the public sector by paragraphs 5.2.16-5.2.21 of the FReM. The term 'directors' for the purposes of the Remuneration Report is interpreted in the FReM (5.2.6) as: *"The composition of the management board (including advisory and non-*

executive members) having authority or responsibility for directing or controlling the major activities of the entity during the year. This means those who influence the decisions of the entity as a whole rather than the decisions of individual directorates or sections with the reporting entity."

Risk	There is a risk that HCPC's approach to Director's disclosures in the Remuneration Report may be out of step with the reporting requirements set out in the Financial Reporting Manual (FReM) and with general practise.
Recommendation	HCPC should consider whether any of its current Executive Directors, in addition to the Chief Executive, fall within the definition of 'directors' as set out in the FReM. The 2012-13 Remuneration Report should include disclosure of the remuneration of all those individual officers who meet this definition.
Management Response	We will discuss this at the Audit Committee Meeting A template remuneration report will be prepared by the end of March.

Annex A – Significant Risks of Material Misstatement

20 We identified issues that could impact on the financial statements in our Audit Planning Report presented to the Accounting Officer and Audit Committee in September 2012. The following table describes how we addressed these matters through our audit process to date.

Significant risks of material misstatement

Risk 1 – Outsourcing of payroll function	Action taken to date and outcome
The payroll function of HCPC will be outsourced to an external provider (Action file) in November 2012. A risk exists that: • the controls put in place by HCPC are not sufficient to prevent erroneous payments being made, or to detect such payments; and • the new process may result in errors in the staff costs recorded in HCPC's annual accounts.	Prior to our interim visit we documented the controls around the new payroll process. At our interim audit we have performed testing to confirm that the documented controls have been fully implemented. To date no errors have been identified. This work will be completed during our final visit.
Risk 2 – Procurement	**Action taken to date and outcome**
During the completion of the audit work on the 2011/12 financial statements NAO received an anonymous letter relating to HCPC's procurement process. The additional work that we undertook following receipt of this correspondence did not identify any issues suggesting irregularity in 2011-12 or in prior years. Our review did, however, identify weaknesses in HCPC's approach to procurement and we made recommendations to HCPC in a separate letter for improvement in this area; and on the need for staff to receive training on their responsibilities under the Bribery Act 2010.	During our final audit visit we will examine the procurement process to establish whether our recommendations have been introduced. We will also review the process that HCPC has operated for any significant procurement activity undertaken during the year. We will seek confirmation that HCPC has adhered to relevant legislative requirements and assess the processes in place to ensure that it achieves value for money through its procurement activity.

Risk	Action taken to date and outcome
Risk 3 – Liability related to Flexiplan Scheme One of HPC's occupational pensions scheme is in the process of being closed. There is an on-going court case to ascertain the liability to each of the employers involved. In the previous two years HCPC's accounts have included a contingent liability disclosure for this scheme. Due to changes that may occur during the year, a risk remains that HCPC's accounts do not adequately disclose their liability in relation to this scheme.	**Action taken to date and outcome** At the time of our interim audit we understand that no decision has been made by the Court. A new actuarial valuation is due in March 2013. HCPC is continuing to pay the agreed monthly contributions. At our final audit will consider the need for a liability to be recognised in the financial statements, or if a contingent liability disclosure remains sufficient, based on the information available at that time.
Risk 4 – Risk of Fraud through Management Override of Controls The International Auditing Standard 240 (ISA 240) states that there is a risk in all entities that management override controls to perpetrate fraud. The standard required that auditors perform audit procedures to address this risk in the following areas; • Journal entries • Bias in accounting estimates • Significant unusual transactions	**Action taken to date and outcome** During our interim visit we have undertaken specific testing to address the risk involved in these areas, No issues have been identified at this stage. This work will be completed during our final audit visit.
Risk 5 – Revenue recognition There is a presumption in ISA 240 that there is a risk of fraud in revenue recognition, in particular where performance is measured in terms of revenue growth or profit. HCPC's reliance on fee income to cover costs, and the issues we identified with respect to revenue recognition in 2010-11, mean that revenue recognition is considered to a significant risk area for this audit.	**Action taken to date and outcome** At final audit we will undertake specific testing to address the risk of fraud in income recognition by reviewing HCPC's processes for gaining assurance over the timing of recognition and completeness of this income.

Areas of audit emphasis

In addition to the significant risks we have also identified the following key areas which may require special attention in our audit.

Transfer of Regulatory Function from General Social Care Council

The regulatory function of the General Social Care Council (GSCC) transferred to HCPC on 1 August 2012. Four staff transferred from GSCC to HCPC but we understand that no assets or liabilities were transferred. As in 2011/12, HCPC will receive specific grant funding from the Department of Health this year to cover additional expenditure relating to this transfer. This will be accounted for in the same way as the previous year. The major impact on HCPC's financial statements will be the increase in income and expenditure that will result from the transfer of approximately 85,000 social workers onto the HCPC register. We will seek confirmation that this significant new area of activity is properly controlled and brought to account correctly.

The social worker register successfully transferred to HCPC from 1 August 2012. Since then social workers have gone through registration renewal and this has seen an increase in income and expenditure as expected.

We have not identified any issues that suggest that this risks represents a significant risk of misstatement and so our assurance will be derived from our standard audit testing. Results from this testing completed as at Month 9 have not identified any errors.

Purchase of Adjacent Building

During 2011/12 HCPC paid a deposit of £1m to the Evangelical Alliance towards the purchase of the adjacent building. Completion of this purchase is not due to take place until April 2013 and we would expect the treatment of this deposit in HCPC's financial statements to remain as it was in 2011/12.

From the draft accounts prepared as at December 2012 we confirmed that the treatment of the deposit in HCPC's financial statements to remain as it was in 2011/12. The building will be purchased in full by HCPC in April 2013 which will therefore impact on the 2013/14 accounts.

We will continue to monitor any decisions made over the future of this building and ensure that any expenditure is accounted for in the correct way.

Annex B - Implementation of Prior Year Recommendations

21 We reviewed management's implementation of recommendations made in our prior year Audit Completion Report. We have summarised the response and provided our evaluation, based on the audit work we have undertaken in respect of internal controls.

No.	Recommendation	Management Response
1	**Capitalisation of software licenses as Tangible fixed assets** At the interim visit for 2011/12 it was identified that a software license had been capitalised as property, plant and equipment instead of intangible assets. Although the amounts involved were not material, we recommended that the software licenses should be reclassified to the correct category of non-current assets. .	Management agreed with our recommendation and reclassified the licenses as at end of March 2012 and so they were correctly shown in 20111/12 accounts. **Auditor Follow-up** From our work on additions and disposals in 2012/13 we have not identified any further issues with incorrect classification.

No.	Recommendation	Management Response
2	**Fixed Asset Register (FAR)** During our testing on fixed assets we identified that the fixed asset register included items that have been disposed of that were still showing on the register, albeit at a nil net book value. We recommended that HCPC reviews the fixed asset register regularly to ensure that it is accurate and that a process is introduced to ensure that the Finance team is notified of disposals as they occur so that the FAR can be updated accordingly.	HCPC agreed that the Finance team would remind department managers to complete asset disposal reports on a monthly basis. **Auditor Follow-up** From our work on disposals in 2012/13 we have not identified any further issues with incorrect classification.