

Audit Committee, 19 March 2015

Internal audit report – Core Financial Systems

Executive summary and recommendations

Introduction

Mazars' internal audit report on core financial systems is attached.

Decision

The Committee is asked to review and discuss the report.

Background information

The internal audit programme includes a review of core financial systems each year. The audit supports the Head of Internal Audit's opinion on the overall system of internal control, which is provided to the Accounting Officer and in turn supports the description of the system of internal control within the governance statement section of the Annual Report & Accounts.

In 2014-15, Mazars have focused on procurement, treasury management and budget setting and control. The audit report gives substantial assurance. Three level three (housekeeping) recommendations have been made.

The Executive has accepted the first two recommendations in full. In relation to the third recommendation, we are already implementing a change which will strengthen control over supplier details changes, so we do not propose to adopt the change recommended in the report.

Resource implications

None

Financial implications

Mazars' agreed fees in 2014-15 are £24,000 including VAT and expenses.

Appendices

Mazars' internal audit report on core financial systems

Date of paper

10 March 2015



Internal Audit Report

**Core Financial Systems –
Procurement, Treasury
Management, and Budget Setting
and Control
(07.14/15)**

March 2015

FINAL REPORT

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Appendix 1 – Definitions of Assurance Levels and Recommendations

AUDIT CONTROL SCHEDULE:

| | | | |
|---|---|---|---|
| Client contacts | Andy Gillies: Director of Finance Charlotte Avery: Head of Financial Accounting | Internal Audit Team | Graeme Clarke: Director James Sherrett: Manager Edward Simms: Auditor Edward Martin: Auditor |
| Finish on Site \ Exit Meeting: | 26 February 2015 | Management responses received: | 10 March 2015 |
| Draft report issued: | 4 March 2015 | Final report issued: | 10 March 2015 |

In the event of any questions arising from this report please contact James Sherrett, Mazars LLP james.sherrett@mazars.co.uk or Graeme Clarke, Mazars LLP graeme.clarke@mazars.co.uk

Status of our reports

The responsibility for maintaining internal control rests with management, with internal audit providing a service to management to enable them to achieve this objective. Specifically, we assess the adequacy of the internal control arrangements implemented by management and perform testing on those controls to ensure that they are operating for the period under review. We plan our work in order to ensure that we have a reasonable expectation of detecting significant control weaknesses. However, our procedures alone are not a guarantee that fraud, where existing, will be discovered.

Mazars LLP is the UK firm of Mazars, an international advisory and accountancy group. Mazars LLP is registered by the Institute of Chartered Accountants in England and Wales to carry out company audit work.

1. INTRODUCTION

- 1.1 As part of the Internal Audit Plan for 2014/15, we have undertaken a review of the Health and Care Professions Council's (HCPC) Core Financial Systems, namely: Procurement, Treasury Management and Budget Setting and Control.
- 1.2 This audit formed part of our rolling annual coverage of the HCPC's core financial systems and processes and will support the financial management objectives of HCPC, the financial statements, and inform the work of HCPC's external auditors.
- 1.3 Our review of this area in 2013/14 focused on Asset Management, General Ledger and Payroll (report 02.13/14 refers). Overall we provided 'Substantial' assurance and made one Priority 2 (Significant) and two Priority 3 (Housekeeping) recommendations. Progress on implementing these recommendations was considered as part of our Follow Up review (02.14/15).
- 1.4 We are grateful to the Director of Finance, Director of IT, the Head of Financial Accounting, the Procurement Manager and other members of staff for their assistance during the course of the audit.
- 1.5 This report is for the use of the Audit Committee and senior management of HCPC. The report summarises the results of the internal audit work and, therefore, does not include all matters that came to our attention during the audit. Such matters have been discussed with the relevant staff.

2. BACKGROUND

- 2.1 Core Financial systems are an integral part of an organisation's internal control mechanisms. With increasing economic pressures to reduce costs and improve efficiencies it is becoming more imperative that organisations have effective monitoring of their finances, with robust scrutiny over the figures and regular reporting to management and council.

Procurement

- 2.2 Procurement is managed out of the finance office under the Procurement Manager's remit with authority for spending retained by the relevant budget holders. The method of selection of suppliers is dependent on the value of the procurement with budget holders having discretion for spending for values below £1,000 and an escalating level of competition and approval required as the value increases. A clear workflow for authorisation and supporting documentation is maintained.
- 2.3 The organisation increasingly utilises framework contracts and agreements for procurement activities. We completed our audit prior to the planned update of HCPC's procurement policy due for review in the upcoming year.

Treasury Management

- 2.4 HCPC's cash position at the time of the audit was approximately £16 million. £7.52 million of this is held in long-term deposits between Santander, Lloyds and Barclays. Approximately £6 million is currently held in Instant Access accounts, and HCPC has recently changed their processes to allow all receipts of cash to be deposited straight into the Lloyds account, which currently attracts the highest interest rate of 1.25%.
- 2.5 HCPC is not dependant on investment income, and the performance of bank deposit investments is not reported to the Executive Management Team (EMT). The Investment Policy states that deposit accounts are the most appropriate investment vehicle, as it is the most consistent with the risk appetite of the Council.

Budget Setting and Control

- 2.6 HCPC has a four year Strategic Plan 2012-15 that outlines the key strategic objectives of the organisation and sets the context for the budget setting process.
- 2.7 Annual budget setting is created through a collaborative process in HCPC's EMT. Department heads draw up their planned activities for the year and proposed key projects. These are discussed by EMT in November at a meeting specifically looking at business plans. From there budgets bids are submitted through standard templates and reviewed by Finance prior to discussion and finalisation at an EMT meeting in January. The budgets are then proposed to the Council by the Chief Executive for approval in March. The approved budget is then uploaded to the Sage finance system used by HCPC.
- 2.8 Management accounts are produced monthly for discussion at the EMT. These budgets include actual against budgeted spend (in both Operational expenditure and Capital expenditure) as well as a variance analysis. Narratives are required on any large variance by budget holders and reforecasts are done twice per year, once in Month Six and once in Month Nine.
- 2.9 For 2014/15, HCPC has budgeted income of £26,013,349 with budgeted operating expenditure of £25,798,031. The month 10 management accounts show cumulative favourable variances compared to budget of 0.4% and 4.6% respectively. The Month Nine budgetary reforecast predicts full year variances of 0.3% unfavourable on income and 1.6% favourable on expenditure, and an overall deficit after depreciation and investment income of £90,483 for the year.

3. SCOPE AND OBJECTIVES OF THE AUDIT

3.1 Our audit considered the following risks relating to the area under review:

- Failure to apply good procurement practice (contracts below OJEU threshold) leads to poor value for money and/or criticism (*HCPC, Risk Register, Ref 15.24*);
- Failure to adhere to OJEU Procurement and Tendering requirements leads to legal challenge and costs (*HCPC, Risk Register, Ref 15.25*);
- Bank insolvency: permanent loss of deposits or temporary inability to access deposits (*HCPC, Risk Register, Ref 15.20*);
- Losses due to fraud or error, inefficient processing or inappropriate activity; and
- Poor decision-making due to poor quality or timeliness of information provided to management.

3.2 In reviewing the above risks, our audit considered the following areas:

Procurement

- Procurement policy and procedures;
- Procurement training for staff;
- Authorisation processes for purchase requisitions, orders and invoices including segregation of duties etc.;
- Use of framework agreements to achieve compliance with EU procurement rules plus savings in time and costs; and
- Audit trail/maintenance of tenders/quotations and associated documentation, as appropriate.

Treasury Management

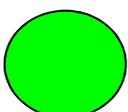
- Reserves, Investment and Treasury Management policies and procedures;
- Processes for approval and authorisation when entering loan or investment agreements;
- Cash flow projections;
- Monitoring of bank deposits and authorisations/approvals for making and changing deposits; and
- Reporting on treasury management activities to EMT/Council.

Budget Setting and Control

- Timetable for the production of the Annual Budget and in-year forecasts;
- Assumptions - use of and approval of those used in the budget-setting process;
- Profiling of income and expenditure and sensitivity analysis;
- Consultation with Budget Holders at budget-setting and training on budgetary control;
- Authorisation of the Budget – EMT, Council; and
- Communication of approved budgets to Budget Holders.

- 3.3 The objectives of our audit were to evaluate the adequacy and effectiveness of HCPC's arrangements for core financial systems, specifically key controls and processes in the areas highlighted in 3.2 above, and the extent to which controls have been applied, with a view to providing an opinion on the extent to which risks in this area are managed. In giving this assessment, it should be noted that assurance cannot be absolute. The most an Internal Audit service can provide is reasonable assurance that there are no major weaknesses in the framework of internal control.
- 3.4 This is not a substantive audit of the accuracy and integrity of the figures included within the financial records of HCPC. Testing was on a sample basis only and focussed on transactions in the 2014/15 financial year.
- 3.5 We are only able to provide an overall assessment on those key controls and processes for core financial systems that we have tested or reviewed. The responsibility for maintaining internal control rests with management, with internal audit providing a service to management to enable them to achieve this objective. Specifically, we assess the adequacy of the internal control arrangements implemented by management and perform testing on those controls to ensure that they are operating for the period under review. We plan our work in order to ensure that we have a reasonable expectation of detecting significant control weaknesses. However, our procedures alone are not a guarantee that fraud, where existing, will be discovered.

4. AUDIT FINDINGS: ONE PAGE SUMMARY

| Assurance on effectiveness of internal controls | |
|---|------------------------------|
|  | Substantial Assurance |
| Recommendations summary | |
| Priority | No. of recommendations |
| 1 (Fundamental) | None |
| 2 (Significant) | None |
| 3 (Housekeeping) | 3 |
| Total | 3 |

| Risk Management |
|---|
| <p>HCPC's Risk Register contains several risks associated with core financial systems. Those risks relevant to our review are: "failure to apply good procurement practice (contracts below OJEU threshold) leads to poor value for money and/or criticism" (<i>HCPC, Risk Register, Ref 15.24</i>), "failure to adhere to OJEU Procurement and Tendering requirements leads to legal challenge and costs" (<i>HCPC, Risk Register, Ref 15.25</i>), and "bank insolvency: permanent loss of deposits or temporary inability to access deposits" (<i>HCPC, Risk Register, Ref 15.20</i>). Testing undertaken as part of this audit has confirmed that the main mitigating control actions identified by HCPC on its Register are in place and operating effectively. We have, however, identified some further opportunities to improve the control environment as identified in Section 6 below.</p> |
| Value for money |
| <p>Value for money implications arise in this area through the robustness of the core financial system process itself and the outcomes associated with the budget. Implications also arise in respect of the related administrative processes such as populating and collating of budgetary templates, through to the ability to monitor and analyse budgetary spend. The organisation makes good use of analysis of actual spend against budget and implementing actions to address variances, alongside a risk averse investment strategy and robust tendering process.</p> <p>The organisation has a low risk appetite towards investments and while this could limit possible returns on investment this is counterbalanced by the possible costs if riskier investments failed or cash reserves were required and found to be unavailable. Additionally, the low risk approach to treasury management has ensured that HCPC has no outstanding loans or debts.</p> <p>HCPC generally follows good tendering processes whereby for several suppliers a thorough bidding process was followed ensuring the best value goods and services.</p> <p>This review has highlighted further opportunities for improvement in respect to procedures for managing financial systems with the aim of further securing budgets and ensuring contracts provide HCPC with their greatest potential value.</p> |

5. SUMMARY OF FINDINGS

Overall conclusion on effectiveness and application of internal controls

- 5.1 Taking account of the issues identified in paragraphs 5.2 and 5.3 below, in our opinion the key control framework for procurement, treasury management and budget setting and control, as currently laid down and operated at the time of our review, provides **substantial** assurance that risks material to the achievement of HCPC's objectives are adequately managed and controlled.

Areas where controls are operating effectively

- 5.2 The following are examples of key controls which we have considered are operating effectively at the time of our review:

Procurement

- Sample testing revealed supplier arrangements were in line with financial regulations and OJEU requirements, such as advertising for multiple tenders with clear use of criteria to support decision-making, were followed when relevant;
- Professional legal advice is sought in all aspects of the tendering process if OJEU directives need to be followed, and an appropriate framework contract is not available, otherwise procurement policy provides clear guidance for tendering;
- HCPC retains scanned copies of authorised signatories for bank accounts which have in all cases been signed off by the Chair and Chief Executive;
- For the purchase ordering system staff have to raise purchase orders and the system controls the approval routes and thresholds.

Treasury Management

- Investment and Reserves policies are in place which are consistent with the Financial Regulations;
- Funds are held across four banks, all holding at least an 'A-' credit rating by Standard and Poor's;
- The Assistant Treasury Accountant and Head of Financial Accounting have the authority to deal with all HCPC accounts with all of the HCPC banks on a daily procedural basis. Transfers between HCPC bank accounts must be initiated by either the Assistant Treasury Accountant or the Head of Financial Accounting on the authority of either the Chief Executive or the Finance Director;
- Testing revealed the organisation maintains enough liquidity to account for varying cash flow levels.

Budget Setting and Control

- Budget planning is documented and timetabled through the budget setting and process document;
- Budgets are produced by each department using standard templates, all of which possess in-built calculations and controls;
- Detailed monthly management accounts are produced; variances and irregular costs are reviewed at a senior level;

- Budget reforecasting is done twice a year, once after six months, and a second time after nine months; and
- Testing confirmed approved budgets had been accurately uploaded to the Sage accounting system.

Areas for further improvement

- 5.3 We identified certain areas where there is scope for further improvement in the control environment. The matter arising has been discussed with management and has been, or is being, addressed as detailed in the management action plan (Section 6 below).
- 5.4 HCPC is validating the suppliers and contracts database to identify when contracts are due for retendering, and if there are any suppliers or services which should be tendered via an EU compliant route. The HCPC Procurement Policy is scheduled to be revised in 2015/16 and will promote the use of framework arrangements where possible.
- 5.5 There is currently no formal process documented in the financial procedures for removing authorised bank signatories from the bank mandate if they leave HCPC. However, bank signatories are all Council members, EMT or 'Band B' managers and Management consider that it is unlikely that a signatory leaving will not be noticed. As such there are no proposals to change the leaver process.

6. ACTION PLAN

| | Observation/Risk | Recommendation | Priority | Management response | Timescale/ responsibility |
|-----|---|--|----------|---|--|
| 6.1 | <p><i>Observation:</i> While reviewing the procurement policy we noted some inconsistencies between the policy and the Financial Regulations, namely that the Chief Executive authorisation values are inconsistent between the two policies, and the OJEC tendering threshold has not been updated in the Procurement Policy.</p> <p><i>Risk:</i> Staff may use incorrect information for procurement activities which could result in non-compliance or inefficiency.</p> | The Procurement Policy should be updated to be consistent with the Financial Regulations. | 3 | Agreed. The Procurement Policy will be updated during 2015-16. | <p>Draft for discussion at June 2015 Audit Committee and approval at June 2015 Council</p> <p>Finance Director</p> |
| 6.2 | <p><i>Observation:</i> Council members are required to make declarations of interest, which are listed on HCPC's website. Members of the EMT are currently not required to pro-actively make declarations of interest.</p> <p><i>Risk:</i> Self-interest of EMT members could result in bias when choosing contracts. Where any conflicts of interest are not declared and appropriately managed there is also the risk of reputational damage through adverse perceptions by external parties.</p> | EMT members should be required to fill an annual declaration of interests form; this will ensure recognised good practice is being open and transparent. | 3 | Agreed. EMT members will make an annual declaration of interests which will be collected by the HR Department | <p>First declarations in March 2015 and annually thereafter</p> <p>HR Director</p> |

| | Observation/Risk | Recommendation | Priority | Management response | Timescale/ responsibility |
|-----|---|---|----------|---|-------------------------------------|
| 6.3 | <p><i>Observation:</i> While HCPC follows best practice by retaining requests for a change in supplier details and contacting suppliers to confirm change, other organisations adopt a formal documented process to ensure this procedure is followed correctly and consistently, even during a period of staff turnover.</p> <p><i>Risk:</i> A fraudulent change of details request may be mistakenly completed.</p> | <p>A form should be created for every time a supplier details amendment takes place allowing confirmation that procedure has been followed and that the change in details is correct. This provides a safeguard for staff involved in the process.</p> <p>This should allow staff to speedily tick off to confirm suppliers have been contacted and the change confirmed. Additionally the form should specify and confirm that the supplier is contacted by the phone number already retained by the organisation, not a number supplied with the request for the amendment.</p> | 3 | <p>We are implementing a change which will achieve the objective of ensuring that the supplier details change process is followed correctly and consistently.</p> <p>As part of the finance systems upgrade, an audit trail module is being introduced. This will track every change to supplier details incl who made the change and a reason for the change. This is then reviewed by either the Head of Financial Accounting or the Finance Director.</p> <p>Any notifications of change in details will be attached to the supplier record within Sage.</p> | <p>March 2015</p> <p>Head of FA</p> |

Appendix 1 – Definitions of Assurance Levels and Recommendations

We use the following levels of assurance and recommendations in our audit reports:

| Assurance Level | Adequacy of system design | Effectiveness of operating controls |
|------------------------|---|---|
| Substantial Assurance: | While a basically sound system of control exists, there is some scope for improvement. | While controls are generally operating effectively, there is some scope for improvement. |
| Adequate Assurance: | While a generally sound system of control exists, there are weaknesses which put some of the system objectives at risk. | While controls are generally operating effectively, there are weaknesses which put some of the system objectives at risk. |
| Limited Assurance: | Control is generally weak leaving the system open to significant error or abuse. | Control is generally weak leaving the system open to significant error or abuse. |

| Recommendation Grading | Definition |
|---------------------------|--|
| Priority 1 (Fundamental) | Recommendations represent fundamental control weaknesses, which expose, HCPC to a high degree of unnecessary risk. |
| Priority 2 (Significant) | Recommendations represent significant control weaknesses which expose, HCPC to a moderate degree of unnecessary risk. |
| Priority 3 (Housekeeping) | Recommendations show areas where we have highlighted opportunities to implement a good or better practice, to improve efficiency or further reduce exposure to risk. |