Audit Committee, 26 November 2015

National Audit Office Audit planning report on the 2015-16 external audit

Executive summary and recommendations

Introduction

The National Audit Office (NAO) external audit planning report is provided to the Committee for its consideration.

Decision

The Committee is asked to discuss the report.

Background information

Auditing standards require external auditors to explain their planned audit approach to "those charged with governance", ie the Audit Committee, on behalf of the Council. The planning report sets out the scope and timing of the audit, and the approach including the auditors' assessment of the significant risks.

The approach and the timetable are similar to previous years, and the NAO intends to hold the fee at the same level as in previous years. The Executive is confident of being able to work with the NAO to deliver an unqualified audit to the planned timetable.

In our case, the only significant risk the NAO expects to address is the risk that auditing standards require auditors to consider on *every* audit – the risk that management will override controls to misstate the results.

The external auditors are independent and it is their responsibility to determine the plan for the audit, so the Audit Committee does not approve or reject the audit plan, but the NAO will welcome the Committee's discussion and any feedback.

Resource implications

None

Financial implications

Audit fee of £39,000.

Appendix

National Audit Office Audit Planning Report 2015-16

Date of paper

18 November 2015

Health and Care Professions Council

Audit planning report on the 2015-16 financial statement audit

REPORT TO THOSE CHARGED WITH GOVERNANCE
November 2015

http://www.nao.org.uk/

Contents

We have pleasure in setting out details of our proposed financial statement audit approach for Health and Care Professions Council for the year ending 31 March 2016.

We have prepared this report for the Health and Care Professions Council's sole use although you may also share it with the Privy Council Office. You must not disclose it to any other third party, quote or refer to it, without our written consent and we assume no responsibility to any other person.

Financial statement audit plan

What work will we complete?

Our audit, which will be conducted in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK and Ireland)), will enable the C&AG to give an opinion on the financial statements.

How are we going to conduct the audit

Risk based approach

We plan our audit of the financial statements to respond to the risks of material[1]:

- misstatement to transactions and balances; and
- irregular transactions.

The significant financial statement risk which we have identified is:

- Presumed risk of fraud through management override of controls.

Given the predictable nature of HCPC's income streams, as in previous years, we will use predictive analytical procedures to provide us with the necessary assurances over amounts recorded in the financial statements. We will, however, perform further assessments throughout the audit process to support our predictive work.

We have considered findings from the prior year audit as well as performing a provisional risk assessment as part of our initial planning work.

We have identified other risk factors that may impact the audit. These and our audit responses are set out at appendix 1 (Financial statements risks - matters of audit emphasis).

Our team

The details of the key audit staff who will complete this audit are:

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[1] A matter is material if its omission or misstatement would reasonably influence the decisions of users of the financial statements. The assessment of what is material is a matter of the auditor's professional judgement and includes consideration of both the amount and the nature of the misstatement. Further information on materiality is included on page 12.

When do we plan to complete the audit

Timetable

The timetable comprises three short interim visits in November, January and March, and a final visit of two weeks in May with certification planned for early July 2016. Further details are provided in the table below.

Date	Activity
October 2015	**Planning:** review HCPC's operations, assess risk for our audit and evaluate the control framework.
November 2015 to March 2016	**Interim audit work:** two visits of 2 days in November and 2 weeks in March to carry out controls and transactions testing. During our March visit, we will complete our audit work on the hard close accounts, incorporating month 10 actuals and estimates for periods 11 and 12.
March 2016	**Interim Report:** present any significant findings from our interim work.
May 2016	**Receipt of the 1st draft accounts** **Final audit work:** 1 week visit to complete our testing of transactions, year-end balances and disclosures, plus 1 week off site for completion.
June 2016	**Audit Completion Report:** present the results of our audit.
July 2016	**Certification:** seek representations and C&AG issues opinion.

Fees

The fee for the audit is £39,000 (2014-15: £39,000).

Completion of our audit in line with the timetable and fee is dependent upon HCPC:

- delivering period 10 hard close accounts and a complete year end Annual Report and Accounts of sufficient quality (and subjected to an appropriate internal review process) on the date agreed;
- delivering good quality supporting evidence and explanations within the agreed timetable; and
- making appropriate staff available during the audit.

If significant issues arise that require us to perform additional work which would result in a change in our fee, we will discuss this with you as soon as possible.

Our audit approach

Our assessment of materiality

Materiality	The concept of materiality recognises that financial statements are rarely absolutely correct, and that an audit is designed to provide reasonable, rather than absolute, assurance that the financial statements are free from material misstatement or irregularity. For the purposes of determining whether the financial statements are free from material misstatement or irregularity we consider whether: 1. the magnitude of misstatement; or 2. the nature and cause of misstatements (e.g. because of the sensitivity of specific disclosure or regularity requirements) would influence the users of the accounts. In line with generally accepted practice, we have set our quantitative materiality threshold as approximately 2% of expenditure, which equates to £570,000. Other elements of the financial statements that we consider to be more sensitive to users of the accounts will be assessed using a lower qualitative materiality threshold. These elements include the remuneration report, our audit fee, comparative figures and related party transactions. We apply the concept of materiality in planning and performing our audit and in evaluating the effect of misstatements on our audit and on the financial statements. As the audit progresses our assessment of both quantitative and qualitative materiality may change.
Error reporting threshold	For reporting purposes, we will treat any misstatements below £5,000 as “trivial” and therefore not requiring consideration by the Audit Committee. Please note that this is a separate threshold to our consideration of materiality as described above. It is materiality, not the error reporting threshold, which is used in forming our audit opinion.

Our audit approach

Other matters

Independence	We comply with relevant ethical requirements regarding independence and have developed important safeguards and procedures in order to ensure our independence and objectivity. Information on NAO quality standards and independence can be found on the NAO website: http://www.nao.org.uk/about-us/role-2/what-we-do/audit-quality/audit-quality/ We will reconfirm our independence and objectivity to the Audit Committee following the completion of the audit.
Management of personal data	During the course of our audit we have access to personal data to support our audit testing. We have established processes to hold this data securely within encrypted files and to destroy it where relevant at the conclusion of our audit. We confirm that we have discharged those responsibilities communicated to you in the NAO's Statement on Management of Personal Data at the NAO. The statement on the Management of Personal Data is available on the NAO website: http://www.nao.org.uk/freedom-of-information/publication-scheme/how-we-make-decisions/our-policies-and-procedures/policies-and-procedures-for-conducting-our-business/
Using the work of internal audit	We liaise closely with internal audit through the audit process and seek to take assurance from their work where their objectives cover areas of joint interest. Following our review of internal audit's plans we will aim to take assurance from the following audit assignments: • Review of HCPC's core financial controls • Review of HCPC's registration project

Appendix 1: Financial statement risks: Overview

We plan our audit of the financial statements to respond to the risks of material misstatement and material irregularity. We are required to perform additional audit work for the most significant risks. Our assessment of the level of risk for the particular issues we consider relevant to the financial statements is shown below.

Impact →

Probability ↓

Low impact/probability	**High impact/low probability**
Registration systems project Plans for HCPC's offices	Changes to HCPC's accounting system
Low impact/high probability	**Significant risk**
	Presumed ISA risk of fraud through management override of controls

Appendix 1: Financial statement risks:
Significant risks

ISA 240 presumed risk of fraud through management override of controls

Audit areas affected

- Pervasive risk (i.e. could impact all areas of the financial statements if the risk was to be realised)

Key features

The Auditing Standard ISA 240 states that there is a risk in all entities that management override controls to perpetrate fraud. The standard requires that auditors perform audit procedures to address this risk in the following areas for **ALL** clients:
- Journal entries
- Bias in accounting estimates
- Significant unusual transactions

No change in risk from prior year

Audit response

We will review the controls in place and carry out substantive testing on:
- Material journals
- Accounting estimates
- Significant unusual transactions

Appendix 1: Financial statement risks: Matters of audit emphasis

We have outlined below matters of emphasis for the 2015-16 audit. These are mainly issues brought forward from the previous financial year but continue to be areas we wish to focus some of our audit work. As decisions are made or systems introduced, we will track these 'matters of audit emphasis', with a view to assessing any potential impact on our audit work and the accounts. At present, there is no expectation that these would crystallise into significant risks to the audit.

Plans for HCPC offices	The Council has agreed to a £720k per annum lease on a new building and £840k of leasehold improvements, both of which will fall in 2015/16. No significant further work is expected on 186 Kennington Park Road in 2015/16. We do not at present consider transactions relating to HCPC's freehold or leasehold properties to be a significant risk to the financial statements.
Changes to HCPC's accounting system	HCPC upgraded Sage in March 2015, as the previous operating system was no longer supported, Management indicated that this was a straightforward upgrade and hence the impact on the financial statements was considered minimal. This year they are introducing additional enhancements including electronic recoding and approval of purchase invoices and changing the partner payment systems so that partners are paid based on HCPC attendance records, rather than those records being used to check the partner-provided invoices. For the purpose of our audit, we consider that should issues arise as a result of these changes, this could have a significant impact on the accounts production process and accuracy of the financial statements. We will, therefore, carry out controls testing at the interim audit stage to gain additional assurance over the control environment and the implementation of the new arrangements.
Registration systems project	HCPC commenced a project to review its registration processes in the last financial year. Some project costs have been capitalised to date. The build stage of the project is starting in 2015/16. We will continue to monitor the project and associated costs to ensure appropriate recognition and treatment of costs and to assess any implications for our audit as the project continues to completion.

Appendix 2: Scope and responsibilities

In line with ISAs (UK and Ireland) we are required to agree the respective responsibilities of the C&AG/NAO and the Accounting Officer/Client, making clear that the audit of the financial statements does not relieve management or those charged with governance of their responsibilities.

In summary:

Area	Accounting Officer/management responsibilities	Our responsibilities as auditor
Scope of the audit	• Prepare financial statements in accordance with the Health and Social Work Professions Order 2001 and HM Treasury guidance and give a true and fair view. • Process all relevant general ledger transactions and make these, and the trial balance, available for audit. • Support any amendments made to the trial balance after the close of books (discussing with us). • Agree adjustments required as a result of our audit. • Provide access to documentation supporting the figures and disclosures within the financial statements. • Subject the draft account and period 10 hard close accounts to appropriate management review prior to presentation for audit.	• Conduct our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK and Ireland)). • Report if the financial statements do not, in any material respect, give a true and fair view. • Review the information published with the financial statements (e.g. annual report) to confirm it is consistent with the accounts and information obtained during the course of our audit.

Appendix 2: Scope and responsibilities

Area	Accounting Officer/management responsibilities	Our responsibilities as auditor
Regularity	• Ensure the regularity of financial transactions. • Obtain assurance that transactions are in accordance with appropriate authorities, including the organisation's statutory framework and other requirements of Parliament and HM Treasury.	• Conduct our audit of regularity in accordance with Practice Note 10 (revised), 'Audit of financial statements of public sector bodies in the United Kingdom', issued by the Auditing Practices Board (Financial Reporting Council). • Confirm the assurances obtained by HCPC that transactions are in accordance with authorities. • Have regard to the concept of propriety, i.e. Parliament's intentions as to how public business should be conducted.
Fraud	• Primary responsibility for the prevention and detection of fraud. • Establish a sound system of internal control designed to manage the risks facing the organisation; including the risk of fraud.	• Provide reasonable assurance that the financial statements (as a whole) are free from material misstatement, whether caused by fraud or error. • Make inquiries of those charged with governance in respect of your oversight responsibility.

Appendix 2: Scope and responsibilities

Area	Accounting Officer/management responsibilities	Our responsibilities as auditor
Governance statement	• Review the approach to the organisation's governance reporting. • Assemble the governance statement from assurances about the organisation's performance and risk profile, its responses to risks and its success in tackling them. • Board members, with the support of the Audit Committee, evaluate the quality of internal control and governance, and advise on any significant omissions from the statement.	• Confirm whether the governance statement is consistent with our knowledge of the organisation, including its internal control. • Consider whether the statement has been prepared in accordance with HM Treasury guidance, including Managing Public Money.
Accounting estimates and related parties	• Identify when an accounting estimate, e.g. provisions, should be made. • Appropriately value and account for estimates using the best available information and without bias. • Identify related parties. • Appropriately account for and disclose related party transactions.	• Consider the risk of material misstatement in respect of accounting estimates made by management. • Perform audit procedures to identify, assess and respond to the material risks of not accounting for or disclosing related party relationships appropriately. • Other than the presumed significant risks to the financial statements (ISA 240) of management override of controls as set out in appendix 1, we have not identified any significant risks at this stage.

Appendix 3 Follow up to recommendations we made in the previous year

Title and area covered	What was the recommendation?	Response/Progress	Status
Accounts Direction: Application of HMT's 'Managing Public Money' rules and spending controls.	PCO's Accounts Direction for HCPC is non-standard, and differs to those we are aware of for other, similar regulators, that we also audit. In these cases, the form of words in the accounts direction affords the regulator more flexibility by, typically, requiring the regulator only to "…have regard to the principles of Managing Public Money". HCPC's view is that, in practice, this is also the standard it is required to adhere to. **We recommended** as a priority for HCPC to discuss and clarify its accounts direction with the Privy Council.	Management responded that the Executive agreed with the Audit Committee's view and the Chief Executive wrote to the Privy Council Office on 18 June. We note that clarification has now been received from the Privy Council and a new Accounts Direction issued.	**Closed**
Expenditure: Self-certification of expenses.	We noted in our management letter last year that the Council has an expectation that self-certified expenses will be subject to annual audit. As set out in the letter of understanding, we plan our audit so that we have a reasonable expectation of detecting material misstatements in the financial statements or accounting records. Although our sample populations include expenses, our work should not be relied on to provide assurance over compliance with the expenses policy or effectiveness of internal controls. **We recommended** that HCPC considers periodically testing a sample of self-certified expense claims for compliance with the expenses policy, using assistance from internal audit as necessary.	Management have clarified that the reference to audit in the Council papers of 4 December 2014 was to internal rather than external audit, and that management intend that internal audit will perform annual checks over self-authorisation for domestic travel and subsistence claims and bookings under £500.	**Closed**

Appendix 4: Fraud matters

ISA inquiries

Our inquiries relate to your oversight responsibility for:

- Management's assessment of the risk that the financial statements may be materially misstated owing to fraud, including the nature, extent and frequency of such assessments;
- Management's process for identifying and responding to the risks of fraud, including any specific risks of fraud that management has identified or that has been brought to its attention;
- Management's communication to the Audit Committee (and others charged with governance) on its processes for identifying and responding to the risks of fraud; and
- Management's communication, if any, to its employees on its views about business practices and ethical behaviour.

We are also required to ask whether you have any knowledge of any actual, suspected or alleged fraud.

Audit approach

We have planned our audit of the financial statements so that we have a reasonable expectation of identifying material misstatements and irregularity (including those resulting from fraud). Our audit, however, should not be relied upon to identify all misstatements or irregularities. The primary responsibility for preventing and detecting fraud rests with management.

We will incorporate an element of unpredictability as part of our approach to address fraud risk. This could include, for example, completing procedures at locations which have not previously been subject to audit or adjusting the timing of some procedures.

We will report to the Audit Committee where we have identified fraud, obtained any information that indicates a fraud may exist or where we consider there to be any other matters related to fraud that should be discussed with those charged with governance.

Appendix 5: Sector updates - developments

FReM 2015-16 changes: adoption of IFRS 13 and changes to structure and content of Annual Report and Accounts

Fair Value – Adoption of IFRS 13 and adaptation of IAS 16

The IASB issued IFRS 13 Fair Value Measurement in May 2011. This Standard applied to the private sector for accounting periods beginning on or after 1 January 2013. It has now been considered from a public sector perspective and will apply to central government entities following the FReM from 2015-16 . The Standard has not been adapted and will apply in full.

Following consideration of IFRS 13, HM Treasury have adapted IAS 16 Property, Plant and Equipment. This adaptation means that assets which are held for their service potential (i.e. operational assets used to deliver either front line services or back office functions) should be measured at their current value in existing use. For non-specialised assets current value in existing use should be interpreted as market value in existing use which is defined in the RICS Red Book as Existing Use Value (EUV). For specialised assets current value in existing use should be interpreted as the present value of the asset's remaining service potential, which can be assumed to be at least equal to the cost of replacing that service potential.

Where an asset is not held for its service potential it should be valued in accordance with IFRS 5 or IAS 40 depending on whether the asset is actively held for sale.

Where these standards require the asset to be held at fair value then it should be valued in accordance with IFRS 13. This will mean that the valuation would be the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date.

Further details and some less commonplace examples are included in chapter 7 of the 2015-16 FReM.

The Performance Report, the Accountability Report and the Financial Statements

In 2013-14 the FReM adopted the Companies Act requirements for a Strategic Report and Directors' Report within the Annual Report. As part of the Simplification and Streamlining Project the 2015-16 FReM introduces changes to the structure of the Annual Report and Accounts. There is now a requirement for these to be split into three parts; the Performance Report, the Accountability Report and the Financial Statements.

Main changes – all entities

- Accounting policies or disclosure notes are only required in relation to material items (although where wider commentary would be helpful to the user this may be included);

- The Accountability Report includes a redesigned "Remuneration and staff report". This combines the disclosures for average number of persons employed and related costs and exit packages (previously included in the notes to the financial statements) with the remuneration report disclosures.

The scope of the external audit has not been reduced and the C&AG will continue to provide the same level of assurance. We will continue to review all other areas of the Annual Report and Accounts and report for consistency with the information obtained during the course of the audit.

Appendix 5: Sector updates - developments

FReM 2015-16 changes: Annual Report and Accounts structure and content

Performance Report

Overview
- Minister or Chief executive's perspective on performance
- A statement of performance and activities
- The key issues and risks facing the entity
- Explanation of the adoption of the going concern basis
- A performance summary

Performance analysis
- Information on how the entity measures performance
- Analysis and explanation of the development and performance of the entity
- Other matters, including sustainable development, as required by the PES papers

Accountability Report

Corporate governance report
- The directors' report
- The statement of Accounting Officer's responsibilities
- The governance statement

Remuneration and staff report
- Remuneration policy
- Single total figure of remuneration and pension entitlements for each minister and director
- Compensation for loss of office and early retirement for ministers and directors
- Fair pay disclosures
- Staff report : exit packages
- Staff report : analysis of staff costs

Audit Opinion

- Staff report: other - includes
  - staff composition (gender analysis)
  - sickness absence data
  - staff policies

Parliamentary accountability and audit report
- Statement of Parliamentary Supply (Departments only)
- Regularity of expenditure
- Fees and charges

Audit Opinion

- Remote contingent liabilities
- Long-term expenditure trends
- The Certificate and Report of the Comptroller and Auditor General

Financial Statements
- Statement of Financial Position
- Statement of Comprehensive Net Expenditure
- Statement of Cash Flows
- Statement of Changes in Equity
- Notes to the accounts

Audit Opinion

Appendix 5: Sector updates - Recent NAO work and work in progress

A Short Guide to Department of Health

In July 2015, we published a Short Guide to the Department of Health. The guide is designed to provide a quick and accessible overview of the Department and focuses on what the Department does, how much it costs and recent and planned changes.

The guide has five sections. The first section is an overview with data on spending levels and staff numbers and costs.

There are further sections on NHS Services, Adult Social Care Services, Public Health and Regulation and Oversight.

http://www.nao.org.uk/report/a-short-guide-to-the-department-of-health/

Managing conflicts of interest in NHS clinical commissioning groups

We found that the Department of Health and NHS England recognised the potential for conflicts of interest in the NHS commissioning system and took a proportionate response to managing such conflicts. We found almost all CCGs had put in place most key elements of the legislative requirements which help them to prevent and manage conflicts.

However, the NAO could not always assess from publicly available information how CCGs had managed such conflicts of interest.

From April 2015, CCGs can choose to co-commission primary care services from GPs which is likely to increase significantly the number and scale of conflicts of interest.

http://www.nao.org.uk/press-releases/managing-conflicts-of-interest-in-nhs-clinical-commissioning-groups-2/

WIP: Managing NHS clinical staff numbers

The NHS employs some 1.4 million people, of whom approximately half are clinical staff. The costs relating to managing NHS staff numbers are significant with, for example, Health Education England spending £5 billion annually on training new staff and NHS bodies spending some £3.3 billion on temporary staffing in 2014-15 to cover shortfalls. Ensuring there are the right number of staff is essential to the delivery of high quality, safe and sustainable health services.

This study will evaluate whether clinical staff numbers in the NHS are being effectively managed, covering:

- are responsibilities and accountabilities for managing workforce numbers clear?
- is the processes for developing a long term national workforce plan for the NHS robust?
- are short term shortfalls in clinical staff numbers being addressed efficiently?

WIP: Sustainability and financial performance of acute hospital trusts

This work will build upon our previous report; *The financial sustainability of NHS bodies* (November 2014), with a specific focus on acute hospital trusts that provide general acute and specialist healthcare to understand whether they are financially sustainable, what is driving their financial position, and the role of the Department and oversight bodies in supporting and managing the sector.

This study will also explore: the variation in key factors that affect the financial performance of the acute trust sector – such as funding arrangements; the behaviour of costs; the Department of Health's understanding of these factors; and the financial plans and cost improvement programmes of acute trusts.

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