National Audit Office

Helping the nation spend wisely

NAO Reflections on 2018-19 Cycle

Reflections on 2018-19 cycle

Introduction

In the past we have issued you with a high level letter capturing our reflections on the accounts preparation and audit cycle. In reflecting on the 2018-19 cycle we considered it more appropriate to widen our communications and provide more substantial and detailed examples to illustrate the points found.

To inform this we have collated evidence from the audit teams of each of the ministerial Departments. The following slides are split into themes, throughout each we capture both our findings or reflections and suggestions for future changes. Themes include:

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- Working together in 2019-20 12

Our work with HM Treasury and finance teams to promptly certify high quality financial statements is reliant on working in partnerships. The areas where we are focusing on working together in 2019-20 can be found at the end of this document

Reflections on 2018-19 cycle

Success

The right accounts certified pre recess
The number of accounts certified are similar to prior years, however in 2018-19 this included key accounts like NHS Property Services, the Academies Sector Report and all ministerial Departments, reflecting improved prioritisation.

Departmental group engagement success
We saw certain Departments tightening their relationship and engagement with their significant components, often performing tripartite engagements with the NAO to improve project management and understanding the risks in the group. On occasion we identified Departments providing technical support to the group on new standard implementation to improve the quality of the response.

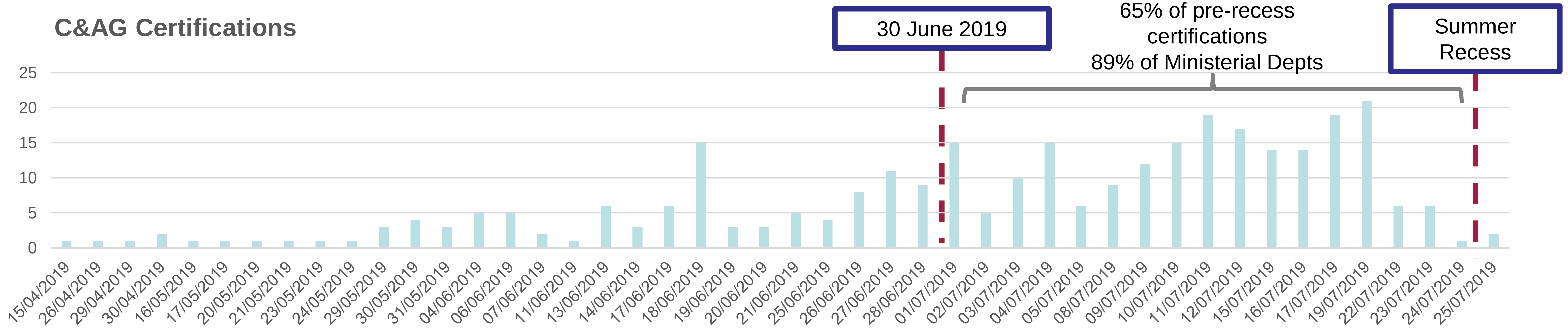
Owning recommendations
In Departments where an accountability and governance process was put around management letter recommendations there was clear success in addressing these points.

Cases of systems progress
We have seen an increase in bodies moving away from excel based bookkeeping solutions to systems, resulting in reduced errors.

Examples of annual reports and accounts readiness
In Departments where a project management officer is in place to support the accounts production process there has been greater success in meeting certification timetables. To support prompt turnaround of Annual Reports and Accounts we identified Audit Committees who have a lead individual engaging with the Annual Report and Accounts to ensure the version that reaches the Committee is high quality and very near final.

Reflections on 2018-19 cycle

2018-19 Profile



What could be different?

There is still a large proportion of certifications occurring in July.
There are now greater requirements in evidence and data to support balances e.g. LGPS pension assets, in some cases this can impact the earliest certification date possible.

Though we continue to move audit work forward in the year, before April, 30 June is not a realistic deadline for a large proportion of bodies. Communicating this as a deadline results in unrealistic timetables that move right through the process and impact the servicing of these and other audits. We recommend HMT reflect on 30 June as the communicated deadline for laying in Parliament

Financial Controls & Financial Management

Points of Reflection

Work is needed on the basics. Weaknesses have been identified in the following area, these control weaknesses resulted in inefficient use of public funds and poor financial management:

Bank reconciliations
Incomplete or inaccurate bank reconciliations were identified in a number of Departments, one even caused a £500m understatement of cash and consequently this cash had not been budgeted for or used effectively.

Balance sheet reconciliations
Failure to produce other balance sheet reconciliations led to high error counts in Departmental financial statements and demonstrated a lack of control over areas like accruals or capital build projects. The issues where information was required from areas outside the finance team.

Shared service centres and HR self service systems
7 ministerial departmental audit teams identified insufficient controls in shared services. IT auditors found occasions where management had not implemented controls intended to provide assurance that third party systems ie Cloud based or shared services were effectively operating controls or managing their providers. 4 Departments each using HR self service functions were found to have overpaid those leaving or taking breaks from their organisation. Similarly increased errors were identified when expenditure receipting was delegated from the centre.

Journal processes
Weaknesses were identified in journal approval and review processes in some cases this required multiple journals to correct the errors generated

Financial Controls & Financial Management

What could be different?

- Bank and balance sheet reconciliations should be undertaken and reviewed as standard each month. Aged reconciling items should be investigated and cleared.
- Finance teams should review and challenge data provided by sources outside the finance team. Where responsibilities are devolved there should be business partners in place to support effective functioning of the processes with communications and guidance issued to support individuals in these roles.
- This should be a particular focus when third parties are providing services. In these cases management should take the lead setting the controls they require over their systems and data and then monitor the third parties meeting these control expectations and where appropriate managing this performance and or putting in complementary controls.
- Journals should be reviewed. An audit trail is required to support why the journal was processed and the independent review of that journal.

Annual Report & Financial Reporting Quality Control

Points of Reflection

Audits have been identified as key parts of the quality control process, considered the case for 10/18 ministerial departments. We have examples of quality control issues covering:

Annual reports
In only 9/18 cases did ministerial Departments in the first instance issue complete Annual Reports and Accounts to the Audit Committees. The success of the annual report reflecting the performance of the business was varied, weak performance reporting often arises when there is lack of clarity or specificity in the Single Departmental Plans (SDPs)

First drafts often included information that had not been updated from the previous years or typos. Where elements of annual reports produced outside the finance team there is a higher rate of non-compliance with the FReM.

Financial Statements
In excess of £20bn adjustments were required to financial statements
Specific reflections on new standard implementation can be found on page 10

Signed Annual Report and Accounts
On average 19 amendments were required to the Annual Reports and Accounts signed by Accounting Officers ahead of certification. Many of these arise due to the variations in accounts directions issued by Treasury and sponsor departments which are not considered as closely as the FReM

Requests to alter accounts post certification
We have received an increased number of requests to change accounts post certification, an activity which should be rare. Such requests are taken seriously and only made at the C&AG's discretion where material or significant.

Annual Report & Financial Reporting Quality Control

What could be different?

- Where teams outside the finance team are providing evidence or data to support the Annual report and accounts process, they should be briefed on the requirements on the FReM

- Finance teams should review all information provided externally to the finance team, i.e. elements like the Remuneration Report if produced by HR or reports provided by shared service centres. The communications and relationships with the business outside the finance team has become more significant with financial reporting standards like IFRS 15 and 16 requiring far greater active communication, by exception communications are no longer sufficient.

- Firm project plans set for both annual report and financial statements, factoring in review time ahead of the audit committee. The audit committee arranged to complement the accounts production process.

- Reflection on the consistency of the Accounts Directions issued by HM Treasury and sponsor Departments and where relevant reissuing these to ensure the requirements remain relevant. Are Accounts Directions clear which Managing Public Money or FReM disclosures are required or what level of assurance is anticipated?

- It is the Accounting Officer’s responsibility that the Annual Report and Accounts they sign are fair, balanced and understandable, there should procedures in place outside the audit to provide assurances that this is the case.

New standard implementation

Points of Reflection

12/18 audit teams for ministerial departments noted difficulties in the implementation in IFRS 9 and 15:

Varying success
Most significant difficulties were generally on lower profile bodies where there was less capacity to explore the new accounting standards and consider the implications. In some of these cases the Department stepped in to support ALBs in their implementation. Those bodies where the issues of implementing were significant and had been identified in advance implemented well.

IFRS 15 or IFRS 9
We identified more significant issues on the implementation of IFRS 15 than IFRS 9, either as it was more commonly deemed immaterial or where there were challenges in interpreting how legislation should be interpreted as a contract. Proving immateriality was more challenging than preparers had initially anticipated.

Earlier consideration required
We identified many clients looking at these standards for the first time in 2019, which resulted in rushed non-compliant or poor quality accounting policies and disclosures often using the language of the previous standards. This occurred even when NAO checklists and HMT application guidance was considered. We expect new standards should be considered at least 12 months ahead of implementation.

New standard implementation

What could be different?

IFRS 9 and 15 implementation has now happened, but there are still areas that could be learned from ahead of IFRS 16 implementation.

We support the Government Finance Academy’s work in providing professional training on the new financial reporting standards and note the high take up and interest this training has had. We would support HMT increasing the number of these sessions run and ensuring different Departments and ALBs have representatives at these

The implementation of the newer financial reporting standard, IFRS 16 requires far greater engagement with the wider business and buy in from teams outside finance. This will be required to identify all the leases present within the organisation and to continue to monitor the data points in each of the leases over the lease term

We support HM Treasury’s Finance Director letter communications already issued on IFRS 16 setting out readiness and milestone expectations. We agree, for implementation of IFRS 16 to be successful there needs to be a clear project plan in place key areas that need to be covered in this are:

- Identifying all leases – communicating with key teams procurement, estates, digital etc;
- Considering what system will be used to account for this both on day one of implementation and subsequent to this;
- Identifying which key practical expedients or significant judgements will be employed;
- Drafting IAS 8 disclosures for those implementing in 2019-20; and
- Drafting Accounting policies

Working together in 2019-20

In partnership

Our work is in partnership with all those contributing to timely, central government financial reporting. We have set out a number of recommendations in this document and will also be making changes in the 2019-20 cycle. Most importantly we will be focusing on working together:

- We will be sharing our considerations on 2018-19 with the finance leadership group, audit committee chairs and through engagements with the government finance academy.
- We will continue to work with HM Treasury to set clear expectations for IFRS 16 implementation. As part of our standard communications we will provide commentary and accountability on progress against IFRS 16 to finance teams and audit committees.
- We consider the coordinated work on responding across central government to the McCloud case in 2018-19 a success and will continue to have key points of contact for specialist issues that have cross–cutting impacts. We will continue to this in responding to the financial audit and value for money implications of EU Exit.
- We should be having conversations on annual reports and accounts some time before certification to focus on clarity, reflecting the current business and its performance as opposed to compliance alone. To facilitate these earlier and refocused discussions we need to receive quality assured draft annual reports and accounts ahead of year end.
- We extend the offer to meet with each Director General of Finance to discuss each Department’s specific focuses for 2019-20, consider the themes in this paper and agreeing a joint timetable for the next audit cycle between Department and NAO.