

# Brent PCT

## 2005/06 Annual Audit Letter



The Board  
Brent Teaching PCT  
Wembley  
HA0 4UZ

March 2007

Ladies and Gentlemen

We are pleased to present our Annual Audit Letter summarising the results of our 2005/6 audit.

We look forward to presenting it to the PCT Board.

Yours faithfully

PricewaterhouseCoopers LLP  
Encs

**Code of Audit Practice and Statement of Responsibilities of Auditors and of Audited Bodies**

*In March 2005 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and of audited bodies'. It is available from the Chief Executive of each audited body. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is to be expected of the audited body in certain areas. Our reports and management letters are prepared in the context of this Statement. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.*

# Contents

<b>Section</b>	<b>Page</b>
Introduction .....	4
Audit findings .....	6
Appendix 1 – ISA 260 Report – issued to those charged with governance in September 2006 .....	9
Audit of the financial statements .....	11
Use of Resources .....	16
Audit plans and fees update .....	18
ISA 260 requirements .....	19
Appendix A to ISA 260 report: Audit reports issued in relation the 2005/06 financial year .....	21
Appendix B to ISA 260 report: Summary of unadjusted misstatements and material adjusted misstatements .....	22
Appendix C to ISA 260 report: Use of Resources conclusion .....	24
Appendix 2: Summary of key recommendations .....	26

# Introduction

## The purpose of this letter

The purpose of this letter is to provide a high level summary of the results of the 2005/06 audit work we have undertaken at Brent tPCT, that is accessible for the Board and other interested stakeholders.

We have already reported the detailed findings from our audit work to those charged with governance in the following reports:

- Internal control report
- ALE Update Report
- Audit opinion for 2005/06 financial statements, incorporating the conclusion on Use of Resources
- Report to those charged with Governance (ISA (UK&I) 260).

The ISA 260 report included in this letter was originally presented to the Audit Committee in September 2006, detailing each of these matters. This was consolidated into a draft Annual Audit Letter at that time which was presented to PCT management

Since that time the PCT has been going through fundamental change. It is facing a considerable overspend in 2006/07 and there has been a major change in the senior management (executive and non-executive) in the PCT,

including in the finance function which is currently being operated at senior level through interim managers.

The PCT also identified significant concerns in respect of elements of the internal control arrangements, which it is working to address for the 2006/07 accounts.

The PCT is currently investigating the reasons underpinning the financial position and pressures and the background to the control issues identified.

Whilst these were being reviewed by the PCT, finalisation of this letter was placed on hold to determine whether these matters should be reflected in the 2005/06 or 2006/07 letters. It is however a requirement under the Code of Audit Practice that we present the final 2005/06 Annual Audit Letter to the Board.

To avoid further delays to this letter, we have agreed with the PCT therefore that we will issue the attached to the Board and Audit Committee, and will then review these more recent matters in detail as part of our work on the 2006/07 accounts and report accordingly on them in our 2006/07 Annual Audit Letter.

A summary of our recommendations made in September 2006 is included in Appendix 2.

### Scope of work

Our audit work is conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

The PCT is responsible for preparing and publishing its financial statements, including the statement on internal control. It is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- forming an opinion on the financial statements and the PCT's statement on internal control;
- forming a conclusion on the arrangements that the audited body has in place to secure economy, efficiency and effectiveness in its use of resources; and
- undertaking any other work specified by the Audit Commission.

Our 2005/06 audit work has been undertaken in accordance with the Audit Plan that we issued in May 2005.

# Audit findings

## Accounts

We audited the PCT's accounts in line with approved Auditing Standards and issued an unqualified audit report on 19 September 2006.

The following key issues should be noted:

- Material late adjustment of £1.9 million for continuing care costs which had not been included in the budget or initial accounts.
- The inclusion of a further £2.8 million contingent liability in the accounts relating to this liability.
- Late submission of accounts to the DoH.

A number of other issues are set out in Appendix in the ISA 260 report (Appendix 1) and a summary of recommendations is included in Appendix 2.

We highlighted financial risks for the PCT associated with intra-NHS and continuing care liabilities in our ISA 260 report, issued prior to the accounts being approved by the Board. In particular around the level of disputed balances and the potential financial impact on the PCT in the event that amounts included as contingent liabilities fell to be paid following negotiation with counterparties. Through discussion with management, we understand that the PCT is experiencing very significant cost pressures in 2006/07 in relation to the negotiated settlement of 2005/06 balances declared as

disputed. Final figures are not yet available, as negotiations continue in some areas, but we understand that the majority of the disputed items are falling to be settled by the PCT, with the effect that much of the contingent liability in the 2005/06 accounts is crystallising as payments in 2006/07.

We also understand that the PCT have identified controls issues associated with these liabilities which could give rise to greater financial pressures in 2006/07 related to prior year activity. The PCT is working to resolve these control weaknesses and identify the potential financial impact. We in turn are working with the PCT, reviewing the final settlement position with regard to amounts related to 2005/06 liabilities, and evaluating the new controls being implemented to resolve related control issues.

We are also reviewing the outturn on settling NHS balances with a view to ensuring that the PCT has not overpaid against its proper liabilities due to its control weaknesses.

## Financial forecast 2006/07

The PCT is currently part of the national "turnaround" programme and as such has agreed a savings plan with the London Strategic Health Authority. The plan originally required the PCT to make savings of £14 million in 2006/07. In December 2006, this target was revised to £11.2 million of savings in 2006/07.

The PCT reported a forecast overspend against its revenue resource limit of £17.6 million at month 9. This was an increase from £10.9 million reported at month 8. The forecast also includes the impact of an assessment of the achievability of planned savings.

### Auditors Local Assessment (ALE)

The Auditor's Local Assessment requires us to assess the overall arrangements that the PCT has in place in the following five areas:

- Financial Reporting.
- Financial Standing.
- Financial Management.
- Internal Control.
- Value for Money.

We evaluated the arrangements against criteria set by the Audit Commission in underlying Key Lines of Enquiry (KLoE) and reached a score for each based on the following:

- 1 – below minimum requirements – inadequate performance;
- 2 – only at minimum requirements – adequate performance
- 3 – consistently above minimum requirements –performing well; or
- 4 – well above minimum requirements –performing strongly.

The scores for these KLoEs then determines the overall score for each area, using rules issued by the Commission. The Commission in turn then determines an overall ALE score for the PCT which is used by the Healthcare Commission in its Annual Healthcheck.

### Final Scores

Below is a summary of the scores for all KLoEs:

ALE Key Line of Enquiry	Score
1.1 The organisation produces annual accounts in accordance with relevant standards and timetables, supported by comprehensive working papers	1
1.2 The organisation promotes external accountability	2
2.1 The organisation's medium-term financial strategy/plan, budgets and capital programme are soundly based and designed to deliver its strategic priorities	2
2.2 The organisation manages performance against budgets	2
2.3 The organisation manages its asset base.	2
3.1 The organisation manages its spending within the available resources	2
4.1 The organisation manages its significant business risks	2
4.2 The organisation has arrangements in place to maintain a sound system of internal control	1
4.3 The organisation has arrangements in place that are designed to promote and ensure probity and propriety in the conduct of its business	2
5.1 The organisation has put in place proper arrangements for securing strategic and operational objectives	3
5.2 The organisation has put in place proper arrangements to ensure that services meet the needs of patients and taxpayers, and for engaging with the wider community	2
5.3 The organisation has put in place proper arrangements for monitoring and reviewing performance, including arrangements to ensure data quality	2
5.4 The organisation has established arrangements for managing its financial and other resources which demonstrate value for money is being managed and achieved	2

Please see Appendix 1 for the details supporting these judgements.

### **Conclusion on Use of Resources**

In 2005/6, for the first time, we were required to issue a conclusion on the adequacy of the PCT's arrangements for ensuring economy, efficiency and effectiveness in its use of resources. This conclusion is measured against twelve criteria published by the Audit Commission, which are closely linked to the ALE KLOEs.

We issued a modified conclusion on the PCT's arrangements for its Use of Resources on 19 September 2006.

We qualified our conclusion due to the weaknesses identified in certain elements of the PCT's arrangements to maintain and monitor a system of internal control, as described in Appendix 1.

### **Statement on Internal Control (SIC)**

The SIC disclosed whether the PCT had risk management and review processes, as evidenced by the Department of Health's Assurance Framework, in place for the whole of the period 1 April 2005 to the date that the accounts were signed.

We reviewed the SIC to consider whether it complied with relevant guidance and whether it was misleading or inconsistent with other information known to us from our audit work. We found no areas of concern to report in this context.

# Appendix 1 – ISA 260 Report – issued to those charged with governance in September 2006

## The purpose of this report

This report summarises the results of our audit work from our 2005/06 audit of accounts.

It includes the issues arising from our audit of the financial statements and those issues which we are formally required to report to you under International Standard of Auditing (UK & Ireland) (ISA(UK&I)) 260 - "Communication of audit matters with those charged with governance".

It also includes the results of the work we have undertaken on 'Use of Resources' under the Code of Audit Practice, to support our formal conclusion in this area.

Our work during the year was performed in line with the plan that we presented to you in May 2005. We have issued a number of reports during the audit year, detailing the findings from our work and making recommendations for improvement, where appropriate. A list of these reports is included at Appendix A to this letter.

We have set out below the most important issues that we have discussed with you in the course of our work so far.

## Financial Statements

The financial statements of the PCT were submitted after the NHS deadline due to the late inclusion of additional continuing care liabilities. On 19 July, the PCT notified PwC of a potential additional £7.8 million of expenditure relating to continuing care costs. These were invoices raised by other bodies such as the London Borough of Brent for the PCT's share of joint placements. The invoices were deemed as "disputed", and as such part of the £7.8 million of costs had not been recognised in the PCT's financial statements. Our review of the invoices and supporting correspondence indicates that there has been a lack of continuity within the continuing care team and issues have not been resolved on a timely basis. The extent of Board awareness of the issues prior to reporting to us and the Board in July 2006 is unclear. In our meetings with Director of Finance and the Audit Committee in planning for and during the Audit, we were not made aware of the issue.

The detailed review of the invoices and supporting documentation has consequently led to a delay in completing the audit.

A significant number of controls and accounting weaknesses were noted during the course of the audit. The detailed substantive nature of our audit approach was in response to these weaknesses and we highlight the main issues identified below. We will provide a detailed report to the Audit Committee after we have finalised our work and agreed this report with PCT management.

## Financial Standing

The PCT is reporting an underspend against its Revenue Resource Limit (RRL) of £430,000, having reported an underspend of £750,000 in 2004/05. The underspend has been achieved against a backdrop of significant financial challenges within the PCT and in the local health economy. The PCT is therefore reporting it has met this financial target. It should be noted however that this result has been achieved after the PCT has made a non-recurring profit of £4.2 million from the disposal of the Willesden Hospital and Pound Lane sites.

Pressures in the local health economy continue and the PCT is required to achieve an underspend against its RRL of £16.5 million in 2006/07. The PCT Board has agreed a detailed financial strategy and appointed a Director of Performance Improvement to lead the delivery of the savings programmes. This is a challenging target to achieve and the Board will need to monitor this closely.

## Use of Resources

We issued the following provisional Auditor Local Evaluation (ALE) scores for the first three areas earlier this year:

- Financial management – 2;
- Internal control – 2; and
- Value for money – 2.

These results have now been confirmed. Following work on the other two areas, our scores are:

- Financial reporting – 1;
- Financial standing – 2.

Following the systems and underlying data weaknesses identified during the audit, we have scored KLOE 4.2 a “1”. This KLOE was scored “2” earlier in the year. A “1” score for KLOE 4.2 has led us to qualify our use of resources opinion.

# Audit of the financial statements

## Accounts

We have completed the audit of the PCT's accounts in line with approved Auditing Standards. We have issued an unqualified financial statements audit report. The PCT did not submit its accounts by the 22 July deadline due to the additional work required on continuing care liabilities. Significant additional work was required by the PCT and PwC in verifying additional liabilities.

There have been reductions in staff within the finance team and this has led to pressure on their resources. This was compounded by a number of staff illnesses for key contacts during the audit. We have also had limited access to staff in the Human Resources department due to the implementation of the Electronic Staff Records (ESR) system. The net effect of these difficulties has led to the audit taking longer than expected this year.

We also noted that monitoring and automated controls did not operate effectively throughout the year, in that our testing of controls identified a number of areas of weaknesses in design or compliance. We therefore needed to adopt a more substantive approach in a significant number of areas for the final accounts audit.

## International Standard on Auditing 260 (ISA 260) requirements - communication of audit matters with those charged with governance

In addition to the requirements covered in our 2005/06 external audit plan, we are also required to communicate the following findings from audit to those

charged with governance:

- Our views about the qualitative aspects of the entity's accounting practices and financial reporting- this is included below;
- The final draft of the representation letter that we are requesting management and those charged with governance to sign- this is included in the other papers for this Audit Committee;
- Our list of uncorrected misstatements – discussed below;
- Modifications to the auditor's report- we have qualified our use of resources opinion, as discussed below in this report;
- Material weaknesses in internal control identified during the audit - we have identified a number of issues, as discussed later in this report;
- Matters specifically required by other ISAs to be communicated to those charged with governance – we confirm that we remain independent within the requirements of ethical and auditing standards - we have no other issues to report; and
- Any other audit matters of governance interest- we have no other issues to report.

## Unadjusted misstatements

We are required to report to you all unadjusted misstatements which we have identified during the course of our audit, other than those of a trifling nature.

We identified misstatements that have a total net impact of decreasing the underspend (OCS) and fixed assets (balance sheet) by £410,334. We have discussed these adjustments with management, and the PCT has made adjustments of £34,000 relating to the QOF accrual. The PCT Board has not adjusted the accounts for £376,334 of errors identified following its review of the items. These amounts are not material however and therefore we have not qualified our opinion.

### Accounting issues

During our audit testing, we identified a number of accounting issues that required resolution prior to the signing of the accounts, and gave rise to the delay in signing the financial statements. These are detailed below:

### Continuing care liabilities

The PCT has made an additional accrual of £1.9 million relating to continuing care costs. The total value of invoices is £7.8 million per the counterparties, although the PCT disputes a significant proportion of these costs. The accrual was calculated based on judgements made by the PCT Board. This is summarised below:

Description	£000
Total liabilities	7,796
Disputed	(2,889)
Already Paid	(1,575)
Held invoices (on the ledger and already included in expenditure)	(1,279)
Recharges	(131)
<b>Net accrual</b>	<b>1,925</b>

The PCT has disclosed the disputed balances as a contingent liability of £2.8 million in its 2005/06 accounts.

Whilst we have accepted the PCT's estimate of the likely eventual payments as being reasonable for the purposes of the accounts, we note that there is scope for the final cost to vary substantially from this estimate with potentially significant impact on 2006/07 resources.

### Adjustment to NHS Creditors

The PCT has made an adjustment to its NHS creditors balance of £3 million which relates to invoices it disputes. The NHS Manual for Accounts states that the adjustment to balances should only be used for invoices in dispute and at arbitration stage. Our work on creditors indicates that the invoices in dispute are not at arbitration stage.

Following a review by the Board, the PCT has "provided" for £301,000 in the accounts for amounts within the £3 million that the PCT may have to pay in 2006/07. A contingent liability of £3 million relating to these invoices has been included in the accounts. There is a further £877,000 of debtors relating to continuing care included within the accounts which the PCT Board feels is fully recoverable. No provision has been made for this amount.

As with continuing care liabilities, whilst we have accepted the PCT's estimate of the likely eventual payments as being reasonable for the purposes of the accounts, we note that there is scope for the final cost to vary substantially from this estimate with potentially significant impact on 2006/07 resources.

### Capitalisation of expenditure

Our testing of expenditure relating to fixed assets has shown that, in our view, the PCT incorrectly capitalised items that are revenue expenditure. These items include £18,950 for consultancy advice, £31,247 of items below the de minimus level (£250) and £253,275 of maintenance expenditure.

The PCT Board has decided not to adjust the accounts for these items following its review.

### Incorrect calculation for depreciation

The PCT does not charge depreciation for assets brought into use in-year because additions are only reviewed at the year end. This is not in line with the PCT's accounting policies and the Manual for Accounts. Based on our sample the value is not material, however arrangements should be put in place to ensure that the PCT complies with its accounting policies.

### Provision for doubtful debts

The PCT is proposing to provide £54,000 for doubtful non-NHS debtors, based upon providing for a few specific, old invoices. We have not been able to validate whether this is understated due to the aged debtor analysis provided by the PCT being incorrect. Any understatement will not be material, but the PCT should look to improve this information for 2006/07.

### Service Level Agreements and GMS Contracts

In our work on healthcare expenditure, we were unable to validate the completeness and accuracy of expenditure in the accounts against signed Service Level Agreements (SLAs). PCT staff were unable to locate copies of a number of the key SLAs. In our work on GMS expenditure we were also informed that contracts had been "lost".

The Director of Finance has located the copies of the agreements and will ensure that they are readily available.

### Accruals for holiday pay and payroll "extras" in period 12

Consistent with prior years, the PCT does not accrue for the liability in respect of the following payroll costs:

- Balance of holiday pay carried over the year end; and
- Additional payments in relation to month 12 overtime and shift allowances (paid in month 13). An accrual of £15,000 has been made in the 2005/06 accounts.

Management expect that, were provision to be made for the items above, the balances would be consistent with the prior year equivalents, and therefore

that doing so would not have a material impact on the 2005/06 OCS. Management have estimated the extent of these provisions and these are not material in the Balance Sheet. The process of matching all expenditure to the period and activity to which it relates is becoming increasingly important in the NHS under the payment by results regime. As such, assuming the balance sheet amount above is not material, we have agreed with management that they will review these balances in detail as part of the 2006/07 accounts process.

The implementation of Electronic Staff Records in 2006/07 may provide an appropriate facility to review this area of payroll costs and generate reliable data in a cost effective manner.

### Control Issues

Under ISA (UK & I) 260 we are required to report to those charged with governance on material weaknesses in the systems in internal control.

In the course of our audit we have noted significant controls weaknesses in the following areas:

- **Segregation of Duties:** certain staff have system access rights to set up vendors, process transactions and execute payments. This is a fundamental systems weakness that exposes the PCT to risk of fraud or error.
- **System access rights:** an excessive number of staff have access to the vendor system.
- **General Ledger Controls:** issues were noted around the frequency, timeliness, accuracy and review of a number of key reconciliations, which in aggregate served to undercut the reliance we could place on the effectiveness of the control environment.

These represent the most significant issues; this list is not exhaustive, and we will be preparing a separate internal controls report for the next Audit Committee.

The controls issues noted have meant that we have been required to adjust our audit approach accordingly.

### Auditors Local Assessment (ALE)

To support the Healthcare Commission's Annual Health Check, we have assessed the Trust's arrangements against a series of Key Lines of Enquiry (KLoEs) grouped into five areas. We comment on two of these areas – Financial Reporting and Financial Standing – in this section of the report. We comment on Financial Management, Internal Control and Value for Money in the Use of Resources section of this report.

KLoEs are scored as follows:

- 1 – below minimum requirements – inadequate performance;
- 2 – only at minimum requirements – adequate performance
- 3 – consistently above minimum requirements – performing well; or
- 4 – well above minimum requirements – performing strongly.

### ALE score for Financial Reporting

We have scored the ALE KLoEs for financial reporting as follows:

ALE Key Line of Enquiry		Score
1.1	The organisation produces annual accounts in accordance with relevant standards and timetables, supported by comprehensive working papers	1
1.2	The organisation promotes external accountability	2

1.1 Based on audit procedures performed to date, the supporting working papers for the accounts have not been to the expected standard. In particular, the PCT did not prepare complete working papers for income and expenditure areas. We also noted on a number of occasions that supporting papers did not agree with financial ledger balances and we have therefore worked with PCT staff to reconcile differences in a significant number of areas. Our queries have taken

longer to resolve due to differences with ledger balances and staff absence.

The PCT has revised its summarisation schedules (ASFs) four times and accounts twice by the submission date and again after this to reflect the changed continuing care provisions.. There were significant movements in creditors (£7 million) in the last set of ASFs in July. We understand that the PCT revised its ASFs in line with guidance from North West London Strategic Health Authority and are now in line with the requirements of the Manual for Accounts (MfA). It should be noted that the first set of ASFs submitted to the Department of Health was referred back to the PCT due to differences in creditors/debtors and income/ expenditure reconciliations.

Therefore the PCT did not meet the minimum requirements specified by this KLoE.

1.2 The score for 1.2 is informed by the 2005/06 annual report, which we have reviewed, and timely and comprehensive publication of minutes, agendas and other documents.

### ALE score for Financial Standing

ALE Key Line of Enquiry		Score
3.1	The organisation manages its spending within the available resources	2

3.1 The PCT initially recorded an underspend of £2.8 million before adjustment for misstatements. The underspend has decreased to just under £0.5 million following these adjustments.

3.2 The PCT has also:

- an under spend of £650,000 against its Capital Resource Limit (CRL);
- remained within its cash limit of £360 million; and
- over recovered by £21,000 its full costs for provider services.

3.3 As the PCT has achieved all of its financial targets for the year, it therefore meets the minimum requirements of this KLoE, however, the unpredictability of the underspend clearly indicates that improvements are required in the management of financial standing.

#### Outlook for 2006/07:

Pressures within the local health economy require the PCT to deliver £16.5 million in savings in 2006/07. The PCT Board considered a financial savings plan at its Board meeting on 25 May 2006. The plan proposes to achieve savings of £16.5 million and comprises of the following:

- Provider services - £ 3.5 million;
- Prescribing - £1.7 million;
- Acute Commissioning - £ 7.2 million;
- Joint Commissioning - £ 3.3 million; and
- Management Costs - £ 0.8 million.

The savings target is challenging and the PCT has engaged a Project Director for Business Improvement to lead the delivery. The financial forward planning group will have oversight of the savings programme and report to the Board.

The PCT will also have to monitor closely any resource impacts arising as disputed balances are settled and adjust their plans accordingly to live within allocated resources.

"The NHS in England: the operating framework for 2006/07" (published in January 2006) makes it clear that the NHS as a whole must stay within its resources. This means that all NHS bodies are expected to achieve operational financial balance in 2006/07.

#### Performance against targets

The PCT has a duty to meet a number of financial targets. In 2005/06, its performance was as follows:

Target	Performance	
Remain within the Revenue Resource Limit	The PCT underspent by £430,000 [£750,000 in 2004/05] against this target.	✓
Remain within Capital Resource Limit	The PCT underspent by £650,000 million [£9,000 in 2004/05] against this target.	✓
Remain with the Cash Limit	The PCT remained within its cash limit of £360 million.	✓
Achieve full cost recovery on provider services	The PCT over-recovered costs by £21,000 [(£1 million) in 2004/05].	✓
At least 90% of invoices (NHS and non- NHS) must be paid within 30 days.	This target has been not met by the PCT. The results were as follows: 84.6% of bills were paid within 30 days (84.3% in 2004/05), by number. The percentage by value was 95.1% (94.6% in 2004/05).  The target is an absolute one, i.e. 100%, and in practice the PCT should aim for over 90% in both calculations.	✗

# Use of Resources

## Work performed

We have performed sufficient work to conclude on the PCT's arrangements for achieving economy, efficiency and effectiveness in its use of resources. Our work to support our conclusion comprised the following elements:

- The Auditors' Local Evaluation (ALE)
  - Financial Management
  - Internal Control
  - Value for Money
  - Financial Standing (described above)
- Use of Resources conclusion.
- Statement on Internal Control.

## Auditors' Local Evaluation (ALE)

We have already reported the detailed results and findings in respect of Financial Management, Internal Control and Value for Money to the PCT in a separate ALE report presented to the Audit Committee in April 2006. We have summarised below the provisional ALE scores for each of these areas.

KLoEs are scored as follows:

- 1 – below minimum requirements – inadequate performance;
- 2 – only at minimum requirements – adequate performance
- 3 – consistently above minimum requirements – performing well; or
- 4 – well above minimum requirements – performing strongly.

## Financial Management

ALE Key Line of Enquiry		Score
2.1	The organisation's medium-term financial strategy/plan, budgets and capital programme are soundly based and designed to deliver its strategic priorities	2
2.2	The organisation manages performance against budgets	2
2.3	The organisation manages its asset base (applicable to organisations with a significant asset base only)	2

## Internal Control

ALE Key Line of Enquiry	Score
4.1 The organisation manages its significant business risks	2
4.2 The organisation has arrangements in place to maintain a sound system of internal control	1
4.3 The organisation has arrangements in place that are designed to promote and ensure probity and propriety in the conduct of its business	2

## Value for Money

ALE Key Line of Enquiry	Score
5.1 The organisation has put in place proper arrangements for securing strategic and operational objectives	3
5.2 The organisation has put in place proper arrangements to ensure that services meet the needs of patients and taxpayers, and for engaging with the wider community	2
5.3 The organisation has put in place proper arrangements for monitoring and reviewing performance, including arrangements to ensure data quality	2
5.4 The organisation has established arrangements for managing its financial and other resources which demonstrate value for money is being managed and achieved	2

## Conclusion on Use of Resources

We are required to conclude on the adequacy of the PCT's arrangements for economy, efficiency and effectiveness in its Use of Resources. In reaching this conclusion, we are required to have regard to 12 Code of Practice criteria published by the Audit Commission.

These Code criteria are linked to the ALE KLoEs (except for financial reporting). A score of Level 2 or higher under the KLoEs will usually result in an assessment of 'adequate' arrangements for the purposes of the Code

criteria. Appendix C shows the linkage between the Criteria and ALE KLoEs.

In reaching our conclusions, we also consider whether the ALE scores should be adjusted for other factors such as whether the arrangements have been in place for the whole financial year.

As detailed on page 5 of this report, we have issued a qualified use of resources opinion. This is due to:

- the impact of controls not operating effectively throughout the year and issues with underlying financial data on financial reporting on the score for KLOE 4.2 (internal control). Details of these weaknesses are set out in the 'Controls Issues' section of this report on page 8.

As this qualification has been triggered by only one issue, an 'except for' opinion has been issued.

This qualification has been reflected in the PCT's Statement of Internal Control and the statement of the Accountable Officer's responsibilities.

## Statement on Internal Control

In 2005/06, all NHS bodies in England are required to produce a Statement on Internal Control (SIC) which is consistent with the guidance issued by the Department of Health on 5 April 2005 and in the format specified in the letter from Sir Nigel Crisp dated 15 September 2003. The SIC was included in the financial statements and in the Annual Report.

The SIC disclosed whether the PCT had risk management and review processes, as evidenced by the Assurance Framework, in place for the whole of the period 1 April 2005 to the date of that the accounts were signed.

We reviewed the SIC to consider whether it complied with Department of Health guidance and whether it is misleading or inconsistent with other information known to us from our audit work. We found no areas of concern to report in this context.

# Audit plans and fees update

## Audit Plan 2005/06

We issued our Audit Plan for 2005/06 and presented it to the Audit Committee in May 2005.

We have performed appropriate reporting procedures for each of the risks identified in our Audit Plan of 2005/06. In this report we comment only on those areas where we believe we need to communicate with those charged with governance.

## Fees update for 2005/06

We reported our fee proposals as part of the Audit Plan for 2005/06. We have not varied our fees, however, there are overruns on the 2005/06 audit due to reduced reliance on PCT controls (leading to increased substantive testing), differences between financial statements and underlying records, late changes to the accounts and PCT staff unavailability. We are currently discussing these with the Director of Finance.

Our fees charged to date were:

	2005/06 Outturn	2005/06 Fee proposal
Accounts	93,000	93,000
Use of Resources and ALE	62,000	62,000
Sure Start Audits	5,000	N/A
Total	160,000	155,000

# ISA 260 requirements

ISA 260 requires us to communicate relevant matters relating to the audit of the financial statements to those charged with governance of the organisation, sufficiently promptly to enable them to take appropriate action. We have agreed with you that these matters should be communicated to the Audit Committee, and in turn to the Board.

ISA 260 specifically requires us to communicate the following matters to those charged with governance:

- Expected modifications to the auditors' report;
- Unadjusted misstatements;
- Material weaknesses in the accounting and internal control systems identified during the audit;
- Views about the qualitative aspects of the entity's accounting practices and financial reporting;
- Matters specifically required by other auditing standards to be communicated to those charged with governance; and
- Any other relevant matters relating to the audit.

Those charged with governance should give consideration to the issues contained within this report prior to final approval of the accounts.

ISA 260 also requires us to communicate with those charged with governance about:

- The concept of materiality and its connection to our audit approach;
- Our approach in addressing the risk of material misstatement;
- Our approach to the assessment of, and reliance on, internal controls;
- Intended reliance on the work of internal audit; and
- The independence and objectivity of the audit team.

These matters have already been communicated to you in the 2005/06 Audit Plan and there are no updates to report.

We have set out below our comments on each of the matters that we are required to report to you under ISA 260.

## **Expected modifications to the Audit Report**

At this stage, we anticipate issuing an unqualified audit opinion on the financial statements, but a qualified opinion on use of resources.

### **Unadjusted misstatements**

We are required to consider with the Committee any misstatements in the draft accounts which management have not corrected, other than those that are 'clearly trifling'. Unadjusted misstatements include both factual items and matters involving judgement. We do not report changes that have already been made to the draft accounts during the course of our audit. Where the PCT chooses not to adjust the accounts, we include the items in our letter of representation and ask that reasons are provided.

At the time of writing we have had discussions with management about a number of adjustments to be made to the Statement of Accounts, which they are considering. These items are detailed in Appendix B.

### **Weaknesses in the accounting and internal control systems**

It is the responsibility of the PCT to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. We obtain an understanding of the accounting and internal financial control systems in order to assess their adequacy as a basis for the preparation of the financial statements and to establish whether proper accounting records have been maintained.

Our approach has been to consider the overall control environment in place, and key management controls operating in relation to significant financial systems and processes for the compilation of the Statement of Accounts. We have also considered the control environment as it relates to computer and IT controls. We have placed reliance on the work of the PCT's internal auditors, where appropriate.

We have appraised the Committee of the significant issues identified in our audit in this report

### **Qualitative aspects of the entity's accounting practices and financial reporting**

The accounts of the Association are prepared in accordance with the NHS Manual of Accounting and UK GAAP. All PCTs must follow the accounting policies specified in these documents. Our audit work has not identified any significant departures from these accounting policies.

### **Matters specifically required by other auditing standards to be communicated to those charged with governance**

There are no such matters which we are required to bring to your attention at this stage.

### **Any other relevant matters relating to the audit**

There are no other matters that we wish to bring to your attention at this stage.

# Appendix A to ISA 260 report: Audit reports issued in relation the 2005/06 financial year.

We have issued the following reports during 2005/06

- Draft ALE findings and conclusions report (Financial Management, Internal Control and Value for Money)
- Audit opinion for 2005/06 financial statements, incorporating the conclusion on Use of Resources;
- 2005/06 external audit plan; and
- Audit committee update reports.

# Appendix B to ISA 260 report: Summary of unadjusted misstatements and material adjusted misstatements

We have identified the following errors during our audit of the financial statements that have not been adjusted by management. The Audit Committee are requested formally to consider the listed unadjusted errors and determine whether the accounts should be amended. If the errors are not adjusted we will require a written representation from you explaining your reasons for not making the adjustments.

Unadjusted Misstatement	Income & Expenditure Account		Balance Sheet	
	Dr £	Cr £	Dr £	Cr £
Depreciation understated as not applied in first quarter of use	Expenditure Amount not calculated but assessed as immaterial			Fixed Assets Amount not calculated but assessed as immaterial
Incorrect capitalisation	Expenditure 31,247			Fixed Assets (plant & Equipment) 31,247
Incorrect capitalisation	Expenditure £18,950			Fixed Assets (Buildings) £18,950
Incorrect capitalisation	Expenditure 253,275			Fixed Assets (Buildings) 253,275
Accruals for holiday entitlement carried forward to 06/07	Expenditure Amount estimated as not material			Accruals Amount estimated as not material
Provision for doubtful debts (including non-NHS debtors over 1 yr old - £1 million)	Expenditure Amount estimated as not material			Provision for Doubtful debts Amount estimated as not material

The following entries were posted by management in August 2006 and relate to an adjustment for understated Continuing Care liabilities, as set out earlier in this report.

Adjusted Material Misstatement	Income & Expenditure Account		Balance Sheet	
	Dr £	Cr £	Dr £	Cr £
Adjustment to non-NHS creditors in relation to understated Continuing Care liabilities	Expenditure 1,925,000			Creditors 1,925,000

# Appendix C to ISA 260 report: Use of Resources conclusion

The Audit Commission has published 12 Code of Practice criteria on which auditors will be required to reach a conclusion on the adequacy of an audited body's arrangements for economy, efficiency and effectiveness in its Use of Resources.

These code criteria are linked to the Auditor's Local Evaluation (ALE) Key Lines of Enquiry (KLoEs). A score of Level 2 or higher under the KLoEs will result in an assessment of adequate for the purposes of the Code criteria. The Code criteria and the linked KLoEs are shown in the table below:

Code Criteria	Description	Associated ALE KLoE	ALE Score	Use of Resources Conclusion
1	The body has put in place arrangements for setting, reviewing and implementing its strategic and operational objectives.	5.1	3	Adequate
2	The body has put in place channels of communication with patients and their representatives, and other stakeholders including partners, and there are monitoring arrangements to ensure that key messages about services are taken into account.	5.2	2	Adequate
3	The body has put in place arrangements for monitoring and scrutiny of performance, to identify potential variances against strategic objectives, standards and targets, for taking action where necessary, and reporting to the board.	5.3	2	Adequate
4	The body has put in place arrangements monitor the quality of its published performance information, and to report the results to board members.	5.3	2	Adequate
5	The body has put in place arrangements to maintain a sound system of internal control.	4.2	1*	Inadequate

Code Criteria	Description	Associated ALE KLoE	ALE Score	Use of Resources Conclusion
6	The body has put in place arrangements to manage its significant business risks.	4.1	2	Adequate
7	The body has put in place arrangements to manage and improve value for money.	5.4	2	Adequate
8	The body has put in place a medium-term financial strategy, budgets and a capital programme that are soundly based and designed to deliver its strategic priorities.	2.1	2	Adequate
9	The body has put in place arrangements to ensure that its spending matches its available resources.	3.1	2	Adequate
10	The body has put in place arrangements for managing performance against budgets.	2.2	2	Adequate
11	The body has put in place arrangements for the management of its asset base [ <i>only applicable to organisations with a significant asset base</i> ].	2.3	2	Adequate
12	The body has put in place arrangements that are designed to promote and ensure probity and propriety in the conduct of its business.	4.3	2	Adequate

- *Score has been revised since initial assessment in May 2006.*

# Appendix 2: Summary of key recommendations

No	Description	Implication	Recommendation
1	<p>Our review of the monitoring and reporting of continuing care liabilities needs to be improved. The backlog of “disputed” liabilities between the PCT and other NHS bodies and Local Authorities is significant. The issues with London Borough of Brent date back to 2002/03.</p>	<ul style="list-style-type: none"> <li>Continuing liabilities could be understated, as discussed in the ISA 260 report.</li> <li>Board is not informed of cost pressures in this service and is unable to take mitigating actions.</li> <li>Operational managers are unable to proactively manage continuing care cases to minimise the cost impact on the PCT.</li> </ul>	<p>We recommend that the PCT :</p> <ul style="list-style-type: none"> <li>Resolves disputes and monitors this area on a regular basis.</li> <li>Implements reporting up to and including the Board.</li> </ul>
2	<p>Our review of inter-NHS balances between the PCT and other NHS bodies, showed a significant value of “disputed” invoices. The value is higher than other PCTs we audit and in-year resolution of disputes (as agreed during 2004/05 audit) was not carried out. We recognise that the Board undertook a detailed review of this area during the audit. This value is not monitored and reported on during the year.</p>	<ul style="list-style-type: none"> <li>NHS liabilities could be understated, as discussed in the ISA260 report.</li> <li>Board is not informed of ongoing disputes and is unable to take mitigating actions and/or help resolve disputes.</li> <li>Operational managers are unable to proactively resolve disputes.</li> </ul>	<p>We recommend that the PCT:</p> <ul style="list-style-type: none"> <li>Reviews and resolves disputed balances regularly.</li> <li>Implements reporting up to and including the Board.</li> </ul>

No	Description	Implication	Recommendation
3	<p>Through review and discussions with finance staff it was noted that depreciation is not calculated and charged on additions as and when they are brought into use, but charged in the first full financial year.</p> <p><i>NHS Capital Accounting Manual 3.17 – “Depreciation is payable on assets from the start of the quarter in which the asset first became available for use”.</i></p>	Depreciation is not being charged in accordance with the requirements of the Capital Accounting Manual and as stated in the PCT’s accounting policies. This may result in depreciation being understated and the value of assets being overstated	Management should ensure that depreciation is charged in line with the requirements of the Capital Accounting Manual.
4	A significant number of items had been capitalised that did not meet the £250 de minimis limit for grouped capital additions.	Management is not complying with Fixed Asset policy/NHS guidelines as stated in the summary notes to the Financial Statements	Management should ensure that staff are given regular update training on accounting policy and NHS regulations, and should ensure that these policies are complied with when compiling the financial statements.
5	A large number of invoices had not been properly authorised. In addition, there was no authorised signatory list with defined responsibilities for authorisation and approval of capital invoices.	Inappropriate invoices may be approved if a strict authorisation hierarchy is not maintained and adhered to	Management should ensure an appropriate scheme of delegation and authorised signatory list is maintained which is communicated to all staff and adhered to.
6	Invoices relating to Capital Maintenance expenditure do not contain a summary of work completed and variance in costs from expectation as per tender specification to final figures.	Management may not be monitoring costs of work completed allowing unauthorised expenditure to be processed unapproved	Management should ensure a full cost summary be provided with every invoice and any variation against tender should be reviewed and signed off by a senior member of the finance team.
7	The Disaster Recovery (DR) planning and testing on the finance applications including WESSIS, PEPS, PASS (administered by K&C PCT) E-financials and Pro4 was not carried during the year.	The PCT may not be able to successfully recover data in a timely manner in the event of a disaster. The PCT has a contract with NDR for this service.	Although the PCT has a contract with NDR, we recommend that it has a formal Disaster Recovery Plan (DRP) and it should be tested regularly.
8	<p>Out review of access rights to E-Financials found that 16 users have rights to set-up and process vendors. Some staff have left the PCT and we also note that only 5 staff have set-up vendors on the system since April 2004.</p> <p>Three staff have rights to set-up vendors and process payments.</p>	Wide access to set-up vendors increases the risk of unauthorised or incorrect vendors being entered onto the system and may also lead to inappropriate payments being made. This in turn increase the risks of fraud or error.	Access to set-up rights should be restricted to selected staff and this should be reviewed regularly.

No	Description	Implication	Recommendation
9	<p>The purchasing system used by the PCT is independent to the ledger. The system has an interface with Accounts Payable which is performed weekly and reconciled monthly.</p> <p>Testing of the reconciliations identified that no reconciliations had been performed during the year until August 2005. Reconciliations between Accounts Payable Controls Account and the Cash Book had not been reviewed since September 2005.</p>	<p>There is a risk that errors on the ledger will not be identified and rectified in a timely manner resulting in errors in the financial statements</p>	<p>Monthly reconciliations should be performed between the purchasing system and the ledger. The same should be carried out between the Accounts Payable Control Account and the Cash Book.</p> <p>These reconciliations should be reviewed independently in a timely manner.</p>
10	<p>Our review of disposals made by the PCT during the year indicated that the PCT did not have a record of authorisation for disposal. We understand that the PCT does not always have the original documents for assets because they were inherited from predecessor organisations.</p>	<p>The legal and financial details of assets disposed of may be unknown, leading to the PCT breaching obligations and potentially incurring financial liabilities.</p>	<p>Management should ensure that documentation for all disposals is available.</p>
11	<p>Agenda for Change charges accrued during the year (approved by the panel) are not being included as utilised/accrued charges on the original provision for the following reasons:</p> <p>Payments may not be accepted by the recipient; and Cash has not been paid.</p> <p>In addition the accrued charges breakdown includes of £70k for provision for appeals which is calculated based on the difference between the accrued charges and the prior year provision.</p>	<p>Agenda for Change provision may be understated.</p>	<p>Management should ensure the process for accounting for Agenda for Change is reviewed. The calculations should be based on data from the HR department and in line with the accounting principles in the Manual for Accounts.</p>
12	<p>The uplift on the premature retirement provision is not being calculated on a named individual basis, but is calculated using the average of all participants. This will not give as accurate a provision estimate.</p>	<p>The provision may not be as accurate as it could be.</p>	<p>Management should ensure that the uplift to the provision and other calculations relating to premature retirement are in line with the Manual for Accounts.</p>
13	<p>Bank reconciliations for Patients' Monies were completed in May, one month after the year end.</p>	<p>Management may not have an up to date view of the balance of Patients' Monies at year end.</p>	<p>Management should ensure that bank reconciliations are completed on a timely basis, no more than two weeks after the month end.</p>

No	Description	Implication	Recommendation
14	<p>PwC were initially informed that the PCT does not hold contracts for all Private Care Homes and care providers that provide services to Brent PCT.</p> <p>In response to the issue raised by PwC, a trawl of the creditors system and other records of care homes used and the amounts specified by the contracts (per the commissioning department's records) was performed. This was compared to the amounts on the ledger to ascertain completeness; no exceptions were noted.</p>	<p>PwC were unable to agree payments made for Private Sector care arrangements to contracts held with Care Homes. We were also unable to establish easily the completeness of expenditure as the PCT was unable to provide a detailed listing of all care homes that provided services in the 2005/06 financial year.</p>	<p>We recommend that the PCT has up to date contractual records for all services received by the PCT.</p>

No	Description	Implication	Recommendation
15	<p>A bad debt provision of £54k has been reported in the Balance Sheet. A breakdown was obtained and it was noted that the balance comprised 6 invoices with values between £50 and £20,447. Upon further examination, it was noted that the invoices were for services provided between April 2005 and October 2005.</p> <p>No provision was made for 4 other aged debts.</p>	<p>The PCT's provision for bad debts may be understated.</p>	<p>The PCT to consider using a statistical method to calculate provision for bad debts by taking a proportion of the invoices where collection is unlikely, possibly based on ageing of debtors.</p>
16	<p>Upon review of the aged debtor listing and detailed review of the invoices that have been included in the bad debt provision totalling £54k, it was noted that the invoices were raised between April and October 2005. These however appeared on the aged debtor listing within 0 to 30 days although these invoices were more than 90 days old.</p>	<p>Inability to accurately reflect the age of debts will affect the identification and provision for doubtful/irrecoverable debts.</p>	<p>The aged debtor analysis should be reviewed and the way in which it is prepared amended to give an accurate reflection of the age of the debtor balances.</p>
17	<p>Through the cut-off testing undertaken, we noted that invoices received/raised by Brent PCT do not always contain sufficient information to easily determine the dates the services were delivered/received.</p>	<p>Inability to accurately assess year-end cut off in the absence of service delivery dates.</p>	<p>Accounts payable/receivable staff should ensure that adequate information is included with regards to the dates which the services are delivered/received. This will help to ensure that transactions are included in the correct periods.</p>

No	Description	Implication	Recommendation
18	<p>Agency cost accruals of £137k for 05/06 had been calculated on the basis of unmatched timesheets as at 31/03/06. This figure did not reflect the amounts owed by the PCT per the supplier statements. (£169k),</p> <p>No reconciliation has been prepared between the two figures, therefore the £137k figure was not fully supported. PCT finance staff informed us that the supplier statements are usually overstated, as they include incorrect and duplicate timesheets.</p>	<p>The agency costs accrual may be misstated.</p>	<p>Management should ensure that all accruals are based on a record of liabilities, for example purchase order or estimated based on prior usage information. Where there is conflicting evidence the position should be reviewed and reconciled and the final decision clearly documented. This should be reviewed and signed off by senior staff.</p>
19	<p>Brent PCT receive monthly statements from the PPA for prescribing costs. These are entered onto the ledger and a reconciliation performed between the statement and the ledger to ensure the details are entered accurately and completely on the ledger.</p> <p>Testing of reconciliations identified no reconciliations were performed in the financial year until August 2005.</p> <p>At the time of the interim visit in February, no reconciliations had been reviewed since September 2005.</p>	<p>There is a risk that errors on the ledger will not be identified and rectified in a timely manner resulting in errors in the financial statements.</p> <p>The lack of timely independent review results in errors remaining unidentified.</p>	<p>Monthly reconciliations should be performed between the PPA statements and the ledger to ensure details are entered accurately and completely.</p> <p>These should be performed accurately using the figures from the PPA statement and executed in a timely manner to ensure any discrepancies are identified and rectified in a timely manner.</p> <p>Once completed the reconciliations should be independently reviewed in a timely manner.</p>

*In the event that, pursuant to a request which you have received under the Freedom of Information Act 2000 (as the same may be amended or re-enacted from time to time) or any subordinate legislation made thereunder (collectively, the "Legislation"), you are required to disclose any information contained in this report, we ask that you notify us promptly and consult with us prior to disclosing such information. You agree to pay due regard to any representations which we may make in connection with such disclosure and to apply any relevant exemptions which may exist under the Legislation to such information. If, following consultation with us, you disclose any such information, please ensure that any disclaimer which we have included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.*

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