NAO
NATIONAL AUDIT OFFICE

Report by the
Comptroller and Auditor General

National Savings

Developments in Financial Reporting

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This report has been prepared under Section 6 of the National Audit Act 1983 for presentation to the House of Commons in accordance with Section 9 of the Act.

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National Audit Office
Comptroller and Auditor General
20 July 1998

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Contents

Executive Summary

1 National Savings (the Agency) exist to help fund the National Debt by offering a range of personal savings products to the public. At the end of 1997-98 around £63 billion was invested in National Savings with annual transactions of over £25 billion.

Background to the Agency's Financial Reporting Problems

2 During their audit of the 1993 and 1994 accounts of Investment Deposits and Ordinary Deposits, the National Audit Office identified weaknesses in National Savings financial reporting systems. These delayed the certification of the accounts by the Comptroller and Auditor General who reported to Parliament on the weaknesses in 1996. Subsequently, in March 1997, the Committee of Public Accounts considered that the number and size of the discrepancies and unreconciled balances in National Savings' financial reporting systems was unacceptable. The Agency indicated their intention to complete their programme of action in response by 31 December 1997, and to report back to the Committee by 31 January 1998.

3 The main weaknesses identified were:

- uncertainty over the precise liability to National Savings investors due to differences between amounts disclosed in the financial accounts and those calculated by totalling customer account balances;
- unexplained balances between products;
- unreconciled discrepancies on balances owed between National Savings and their agents such as the Post Office (through whom a significant number of transactions on the Investment and Ordinary Deposits are undertaken); and
- large unexplained suspense account balances.

The National Audit Office have no reason to believe that similar weaknesses exist in the customer accounting records.

4 The Committee of Public Accounts considered that these deficiencies had arisen due to failings in National Savings accountability arrangements. They emphasised that it was the Accounting Officer's responsibility to ensure that he has mechanisms in place to provide him with assurance about the effectiveness of financial controls. They were also concerned that fraud might have been a factor in the discrepancies which have arisen. Although the Agency's work is not yet complete, this report reviews the significant actions which have been taken by National Savings to address the weaknesses identified in the Comptroller and Auditor General's earlier report. In following up the recommendations of the Comptroller and Auditor General, and those of the Committee of Public Accounts, the Agency have extended their work to encompass all of their products, as many of the problems identified in the 1996 report could only be resolved by undertaking a wider-scoped review.

Action taken by the Agency

On the liability to investors

5 National Savings are now able to reconcile the daily change in their customer and financial accounting systems. Historical differences remain, however, in the overall liability to investors on individual products. National Savings have reconstructed the financial ledgers for the 6 products handled by their Glasgow site (Investment Deposits, Ordinary Deposits, Capital Bonds, First Option Bonds, Children's Bonus Bonds and Deposit Bonds) for the period from the date each product was introduced to 31 March 1996. For products handled at their other two sites (see Figure 2) the Agency have reviewed balances for each product and compared them with independent information, such as bank statements, where available.

6 As a result of their work the Agency have identified unexplained differences on all their products. In January 1998 they reported to the Committee of Public Accounts their initial assessment of the overall discrepancies identified in respect of the position shown by their accounting records at 31 March 1996. This was

- Glasgow products – net £4.7 million liability not supported by assets;
- Blackpool products – net £1.2 million liability not supported by assets;
- Durham products – net £6.4 million surplus of assets.

7 The Agency therefore reported the net position for all products as a surplus of assets over liabilities to investors of £0.5 million, as shown in Figure 6 (see Part 2 of this report). They believe that it is appropriate to view the discrepancies together because:

- prior to 1986 the accounting system could not split values between some products and not all customer records were fully computerised;
- estimated figures were therefore used as the opening balances for the new system;
- opening balances were therefore likely to have been wrong and assets incorrectly allocated between products at that date.

8 The Agency have revised the discrepancies recorded above as a result of work since January 1998 which has increased the net position to a £0.8 million surplus of assets over liabilities. This comprises:

- Glasgow products – net £3.1 million liability not supported by assets;
- Blackpool products – net £1.2 million liability not supported by assets;
- Durham products – net £5.1 million surplus of assets.

However the Agency have yet to complete their work on suspense accounts and agents balances, and thus the final position is not yet known.

9 The National Audit Office consider that it may not be appropriate to net off the gains and losses for the following reasons:

- Although it is probable that some of these discrepancies arise from the misallocation of opening balances in 1986, the National Audit Office note that discrepancies have also arisen on products introduced since that date;
- In the case of Ordinary Deposits, monies are held by the National Debt Commissioners under the National Savings Bank Act 1971 rather than the National Loans Fund. Other products are also covered by specific legislation, usually within Finance Acts.

10 The Agency are currently considering proposals to involve the private sector in the delivery of their operations. This adds emphasis to the need for the Agency to ensure that only substantiated balances are transferred to new systems, and that adequate financial controls are built into those systems.

On the unexplained balances between products

11 National Savings have investigated the reasons for the unusually high balance, which existed between Investment and Ordinary Deposits, and tried to identify causes of the difference which existed between them. National Savings found that the unusually high balance had been caused by a failure since October 1994 to transfer cash between the two products to clear the balance owing. They have been unable to identify a conclusive reason for the remaining discrepancy of £500,000, which represents a deficit within the overall position reported above. However, the discrepancy has stabilised and the account is now reconciled on a daily basis.

On the unreconciled discrepancies which existed between National Savings and their agents

12 National Savings have established a transaction database, which enables the Agency to produce transaction reports using the accounting periods of their agents. They have also established a project board whose objective is to design or change accounting procedures to facilitate reconciling balances between the Post Office and National Savings. They have also clarified their relationships with their agents, for example setting targets for receipt of monthly certification of statements.

13 The Agency have yet to introduce a comprehensive reconciliation between internal and external records of amounts due to and from their agents. Although the Agency are now able to reconcile data input to their customer accounting system with the movement in the financial accounting system, they have yet to be able to agree data with their agents' records. In the case of their main agent, the Post Office, there was a difference of over £2.69 million at November 1997, being sums due to the Agency from the Post Office. In May 1998, National Savings and Post Office Counters Limited agreed an interim settlement of £2.25 million and have agreed further joint work aimed at resolving the remaining problems. National Savings have found resolution of these issues, which had to be tackled in collaboration with their agents, more complex than they expected. Hence they have not met their undertaking to reconcile all agents' balances exactly by the end of March 1997.

On the unexplained balances on suspense accounts

14 Significant unexplained balances exist on two of the Agency's suspense accounts which hold transactions until allocated to customer accounts. The Agency have instituted reviews of these accounts to try to identify causes of the balances, and they have introduced a transaction trail to enable individual transactions to be traced through the accounting systems.

15 The first suspense account, Unallocated Monies, holds investors' transactions until they have been allocated to products. The balance should therefore represent a liability to investors for accepted deposits and be represented by cash held in the related bank account. However at 31 December 1994, the balance showed a sum due from investors of £37 million and the related bank account was overdrawn by £28 million.

16 As a result of their investigations National Savings believe one large error of £11.7 million relating to Deposit Bonds had resulted in funds being moved incorrectly from the Unallocated Monies Bank account when no money was due. After adjusting their records the Agency believe that the remaining balance due from investors and the overdrawn bank balance offset each other. They believe that the incorrect recording of transactions to the suspense account has resulted in funds being incorrectly transferred from the Unallocated Monies account to individual products although, as the Agency reported, this cannot be demonstrated conclusively because the necessary accounting records are unavailable. At the time of their report to the Committee of Public Accounts the Agency calculated the deficit in respect of Unallocated Monies to be £3.6 million. This has since been reduced to a deficit of £3.4 million within the overall surplus position reported above.

17 The second suspense account, the Departmental Office Account, captures transactions not processed by National Savings agents, for example, direct remittances and internally generated transactions. At 31 December 1994 unsubstantiated differences on these accounts included £3 million for Investment Deposits and £11 million for Ordinary Deposits. The Agency have estimated the outstanding balance on the Departmental Office account for each product by reference to uncleared funds banked in the local bank accounts for each product. However the National Audit Office note that this analysis produces markedly different amounts for the Departmental Office account balances than those derived from the liability to investors reconstructions. The Agency attribute this to the different assumptions lying behind each of these reviews and that both exercises contain estimates. The Agency are continuing their investigations of this suspense account. Any changes arising from this work will affect the net discrepancy of £0.8 million surplus of assets identified by the Agency's reconstruction of the liability to investors.

Risk of Fraud

18 The Agency have been assisted in their work by their external consultant, KPMG, who were also asked to consider whether fraud could have contributed to the discrepancies and unexplained balances within the financial accounting systems. They concluded that:

- there were undoubtedly weaknesses in controls which could have provided the opportunity for fraud;
- in principle, fraud could have been a contributory factor for the unresolved differences in the financial accounting systems;
- any conclusions must await the completion of the additional work that they recommended in their review of the liability to investors' reconstruction reports to identify the sources of the unresolved differences which may provide further indicators as to the scope of fraud risk.

19 These conclusions are in line with the National Audit Office's assessment of the financial accounting systems. Moreover the length of time over which the problems have arisen, and the absence of transaction trails within the Agency's financial accounting records, means that proving the existence or otherwise of fraud is very difficult.

20 However the Agency also believe that their various non-accounting checks and balances make the perpetration and subsequent concealment of significant internal fraud unlikely. While they recognise that they can give no absolute assurance, they have concluded that the accounts have not been affected to any material extent by undetected fraud; and that further investigation into the possibility of undetected fraud is unlikely to significantly advance the situation.

Accountability arrangements

21 The Agency have taken action to improve accountability arrangements by reviewing the focus of the Internal Audit function; appointing a qualified accountant from the private sector as Finance Director; and reviewing the overall level of accounting resources they require. They have yet to develop fully their strategy for developing the skills of their non-accountant finance staff, a number of whom are involved in key reconciliation and control processes. These will only be effective if the staff undertaking them understand their purpose, and the action required where discrepancies arise.

Conclusions and Recommendations

22 National Savings continue to pursue their work in the above areas. The National Audit Office believe that it may nevertheless be difficult for the Agency to reach a conclusive view on the overall impact of the errors due to their extent and the time over which they have accumulated. It may therefore be necessary for the Agency to set themselves a cut-off date for further work, not least in view of the rising costs of the exercise for their own staff, and for consultants (currently £506,483 inclusive of VAT at 30 June 1998).

23 However, before making the adjustments to their financial accounting systems which would then be necessary, the Agency need to be satisfied that they have established as far as possible reasons for the discrepancies which exist. They also need to be satisfied that all discrepancies have at least stabilised even if reasons for them cannot be established due to insufficient data and the passage of time. The National Audit Office consider that it is particularly important for the Agency to establish reasons for the differences in the estimated values for the Departmental Office suspense account between the reconstruction exercise for the liability to investors, and that for the suspense account itself. Unless these can be explained, doubts exist as to the outcome of both exercises. They also consider it to be important that the Agency are able to fully reconcile balances with agents.

24 The Agency have restructured their activities between core functions such as policy making and strategic decisions, and their operational activities. To avoid any recurrence of their current problems with financial reporting, it is important that the Agency have effective communication and monitoring arrangements between their core finance staff, and operational staff who will have day to day responsibility for the processing of transactions and preparation of accounts.

25 National Savings also need to agree with the Treasury the adjustments required to the accounts of the National Loans Fund. The National Loans Fund correctly reflects the cash which has been transferred between National Savings and the Treasury. Adjustments will however be required in due course to the value of accrued National Savings transactions, comprising borrowing not yet brought to account and interest. These figures affect the Supplementary Statements to the Consolidated Fund and National Loans Fund accounts.

26 The National Audit Office recommend that the Agency should:

- consider the benefits to be derived from their continuing investigations in the context of the costs, and the likelihood that conclusive reasons for outstanding balances will be obtained;

- pursue and resolve the discrepancies in values for the Departmental Office account between their report on that account and the liability to investors reconstruction reports;

- in the absence of conclusive evidence that gains and losses are matched, consider the appropriate accounting treatment for each discrepancy separately once the amounts have stabilised;

- only transfer substantiated balances to any new accounting systems which they either develop themselves or which are provided by a third party supplier;

- address the financial training needs of their non-accountant finance staff as a matter of priority, in particular for those with responsibility for important review and control functions, for example, staff undertaking key reconciliations.

Part 1: Background

Role of National Savings

1.1 National Savings have a key role in the personal savings market having about 12% of the retail savings market in 1997-98. At the end of 1997-98 around 30 million customers had invested over £63 billion in National Savings products. The main objective of the Agency is to support the Government's funding requirement, and its policies for personal savings, by attracting and retaining investments from the retail market efficiently and cost effectively.

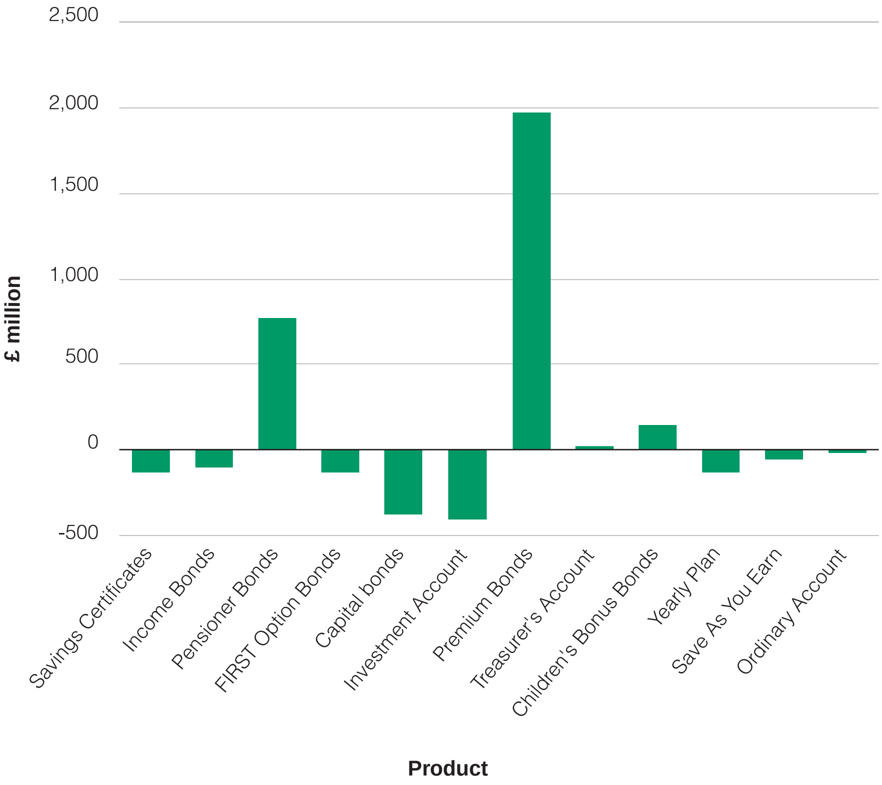
1.2 National Savings are responsible to Treasury Ministers who set an annual funding remit. The remit sets out the assumptions for the amount and cost of the funds to be raised by the Agency over the following financial year. It represents the net contribution that National Savings are expected to make to finance the Central Government Borrowing Requirement. In 1997-98 National Savings achieved a net contribution of £1.5 billion against a target of £2.0 billion. As shown in Figure 1 below the largest net contributors were Pensioners Guaranteed Income Bonds of £0.7 billion and Premium Bonds of £1.9 billion.

1.3 The Agency offer a variety of savings products to the general public. The products are managed at three sites, Glasgow, Durham and Blackpool, and are supported by the Agency's London Headquarters. Figure 2 on page 11 shows the products managed at each site, and the sums invested at 31 March 1998. For 1997-98 gross sales were £12.5 billion while repayments totalled £13.2 billion, and the Agency handles around 30 million separate transactions yearly.

1.4 The Agency employ around 4,300 staff (95% of whom are located at the 3 regional sites), and had a gross annual budget of approximately £181 million in 1997-98. The Director of Savings, as Chief Executive and Accounting Officer, is responsible for the management of all aspects of National Savings. He is supported by a Management Board comprising six other executive members and two non-executive members.

National Savings: Contributions to Government Funding by Product for 1997-98

Figure 1



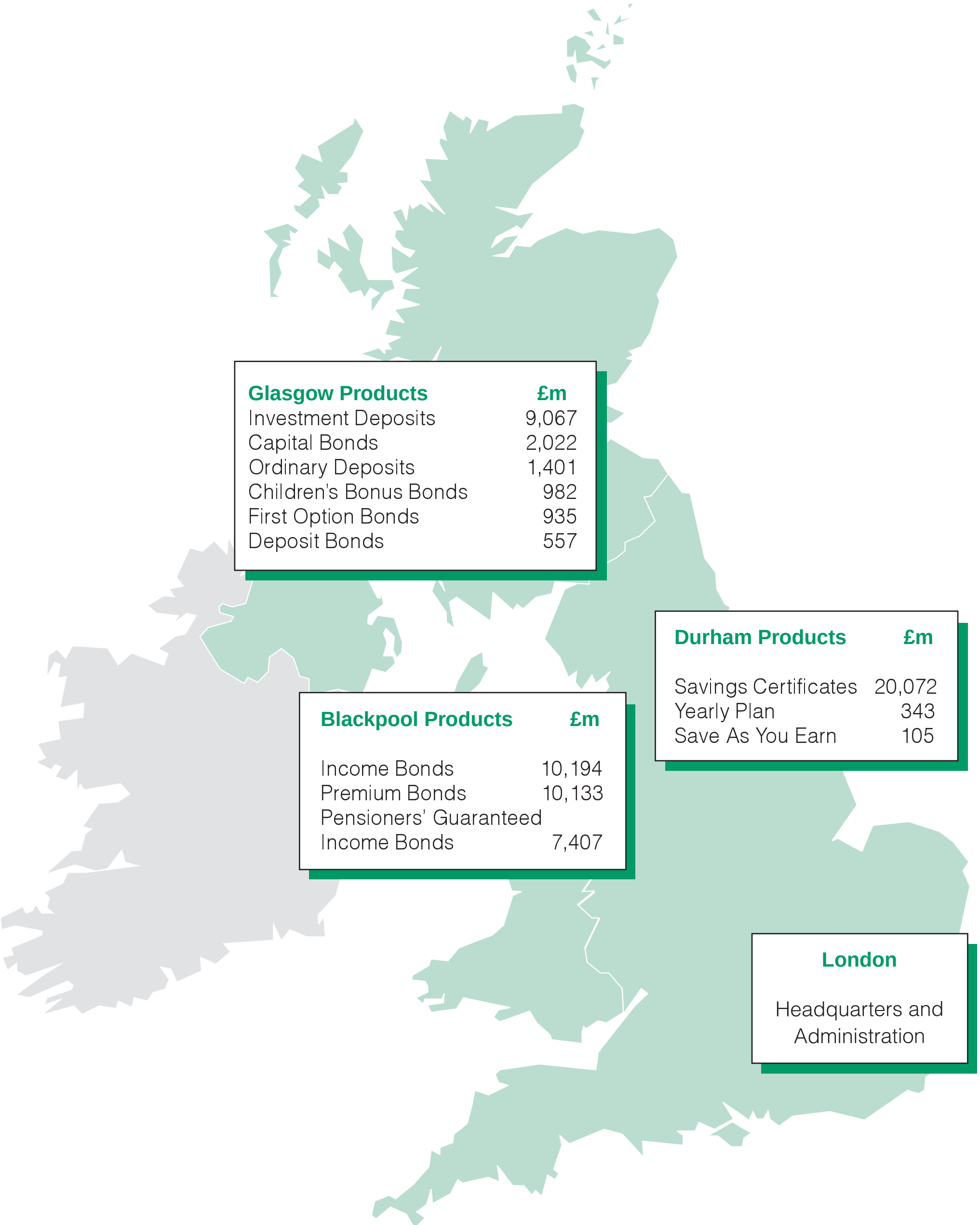
Source: National Savings

1.5 National Savings have no retail outlets and their savings activities are conducted through agents and directly with customers by post and, more recently, by phone. For deposits the most significant agent is Post Office Counters Limited which handles over 80% of the receipts for the Investment and Ordinary Deposits Accounts. Other agents include the Postal Administrations in Guernsey, Jersey and the Isle of Man. For the Treasurers' Account (part of Investment Deposits), National Savings have introduced a system to enable customers to make deposits over the telephone.

1.6 For repayments there are two significant agents: the clearing banks who process warrants issued (similar to cheques), and Post Office Counters Limited who make payments on demand to Ordinary Deposits' customers and who process warrants. Customers opening Ordinary or Investment Deposits accounts receive pass books. Whilst Ordinary Deposits' investors can withdraw small sums over the counter at Post Offices, all large withdrawals and all Investment Deposits

Figure 2

Amounts invested in National Savings' products



Note: This figure shows the amounts invested in National Savings' products at 31 March 1998 at each location.

Source: National Savings Annual Report

withdrawals are made by applying to National Savings for a warrant. Cash warrants are sent to the investor for encashment at Post Office Counters Limited. Generally crossed warrants have to be processed through other financial institutions.

1.7 Amounts received from investors for all products, other than Ordinary Deposits, are paid over by the Agency to the National Loans Fund. Those for Ordinary Deposits are passed to the National Debt Commissioners for investment in government securities. To meet withdrawals the Agency reclaim monies from the National Loans Fund or the National Debt Commissioners as appropriate. The National Loans Fund liability to investors also increases as interest is earned by investors. Interest on Ordinary Deposits is paid from funds invested with the National Debt Commissioners. Figure 3 shows the flow of funds.

Flow of funds

Figure 3

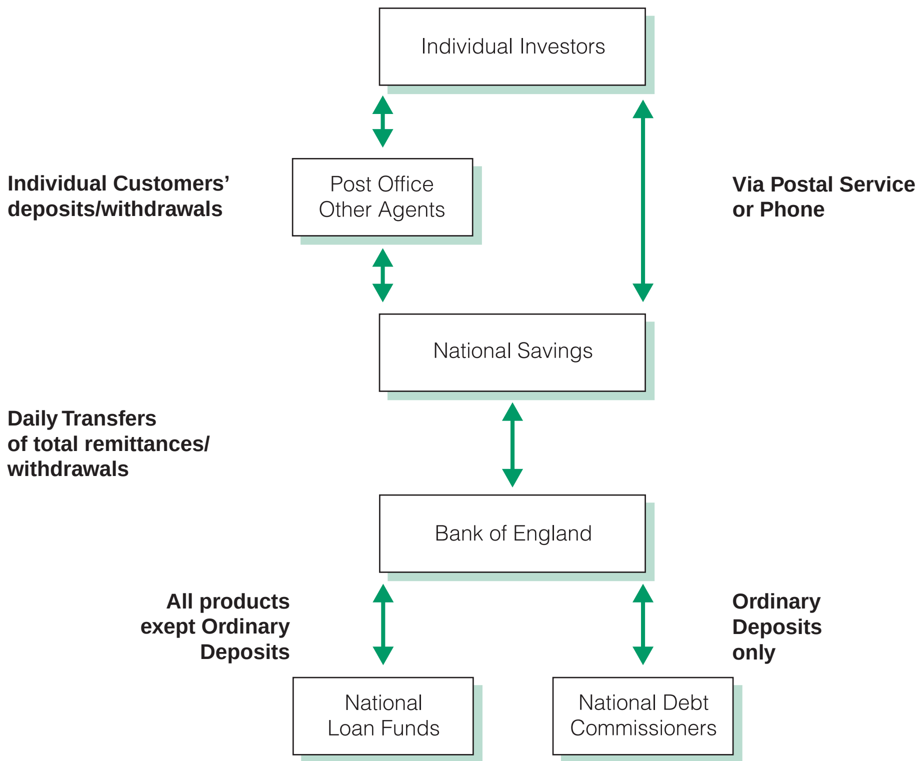


Figure 3 shows how funds are deposited by investors and repaid to them via agents or through the post. Amounts invested are paid over to the National Loans Fund or, for Ordinary Deposits, to the National Debt Commissioners.

Source: National Savings

1.8 The expenses of the Agency and the National Debt Commissioners in connection with Ordinary Deposits are also paid from funds invested with the National Debt Commissioners. Surplus income (excluding profits on realisations) is paid over to the Consolidated Fund after making any provision for depreciation in the value of investments which the Treasury may require. At 31 December 1997 provisions of £316 million existed, being the excess of assets held over the liability to investors as disclosed in the Ordinary Deposits accounts.

Accounting Systems

1.9 The Agency maintain two types of accounting system:-

- customer account recording systems which deal with the transactions and balances on individual customer accounts (hereafter referred to as the "customer accounting systems"); and

- financial accounting systems which record the total amounts invested and repaid for each product during the accounting period, the interest earned by the investors and the balances held at the end of the period. They also disclose the total liability of the Exchequer to investors at the end of the period ("the liability to investors").

1.10 The Investment and Ordinary Deposits require the Agency to process a large volume of low value transactions and their main accounting systems were developed to meet the requirement for accurate customer accounting rather than financial reporting. Up until 1995-96, there was no automated link between the main transaction processing systems which update customer accounts for individual products and the financial accounting systems from which the financial statements for each product are produced. Instead financial accounting systems were updated by manual input from daily reports summarising transactions recorded on the customer accounting system. Subsequent changes now provide an automated link but postings continue to be bulk amounts and, until recently, no analysis of these amounts was retained for more than 6 days.

1.11 The Agency have a statutory obligation to produce financial accounts for two of their products: the Investment Deposits Account which includes the Treasurers account (under the Finance Act 1980) and the Ordinary Deposits Account (under the National Savings Act 1971) and these are subject to audit by the Comptroller and Auditor General. In October 1996 the Comptroller and Auditor

General published a report (National Savings: Financial Reporting: HC9: 1996-97) drawing attention to significant shortcomings in financial accounting systems for these two products, which had delayed his certification of the accounts for 1993 and 1994.

1.12 The Committee of Public Accounts took evidence on the Comptroller and Auditor General's report in January 1997. They published a report (National Savings: Financial Reporting: Eighteenth report 1996-97: HC 214) in March 1997 in which they expressed concern at the number and size of the discrepancies and unreconciled balances which existed in National Savings' financial accounting systems. The Committee of Public Accounts noted that the Agency's target was to address the problems by the end of 1997. In the Treasury Minute response published in July 1997, the Agency indicated that they would report back to the Committee by the end of January 1998 on their progress, and the Accounting Officer did so in January 1998.

1.13 The Comptroller and Auditor General also reported on the 1995 accounts of Investment and Ordinary Deposits in July 1997 in which he noted the progress made by the Agency at that stage. Details of the key recommendations and findings from the Committee of Public Accounts' report, and the Agency's response, are shown at the Appendix to this report.

1.14 The remaining sections of this report review the actions taken by the Agency in response to the recommendations of the Committee of Public Accounts and the Comptroller and Auditor General. The report comprises:

Part 2:	Determining the precise liability of the Exchequer to National Savings' investors.
Part 3:	Improving accounting controls over balances due between products, balances with external agents, and controls over suspense accounts.
Part 4:	Other action taken by the Agency to improve accountability arrangements.

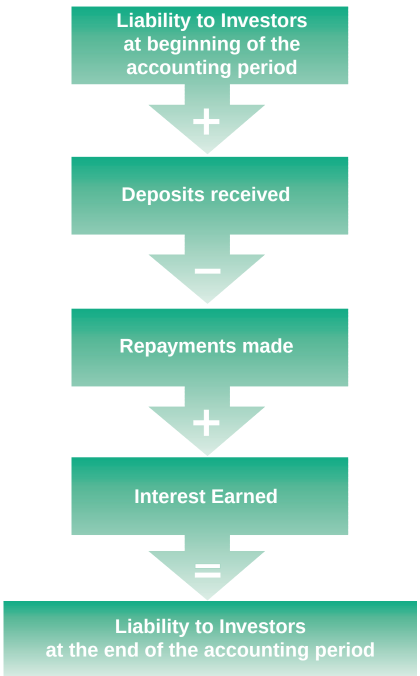
Part 2: Determining the precise liability of the Exchequer to National Savings' investors.

Introduction

2.1 This part of the report summarises the work undertaken by National Savings to meet the Committee of Public Accounts' expectation that National Savings should be in a position to establish precisely the total liability of the Exchequer to investors. The Comptroller and Auditor General's 1996 report focused on the differences which existed between the Agency's financial and customer accounting systems for the amount of the liability to investors for the Ordinary and Investment Deposits products. The Agency have extended their work to encompass the liability of the Exchequer to investors for all of their products as many of the problems identified in the 1996 report could only be resolved by undertaking a wider-scoped review. The National Audit Office supported this approach.

Background

2.2 The liability to investors (the amount owed to depositors in aggregate) in the financial accounting system comprises:



2.3 In his 1996 report, the Comptroller and Auditor General noted that the Agency had three different sources for establishing the Exchequer's liability to investors for Investment and Ordinary Deposits, and that each of these sources gave a different value as shown in Figure 4 below. The three sources were:

- the financial accounting system value calculated as set out in paragraph 2.2 above;
- an interrogation program, the Financial Analysis Suite, which totalled customer balances in the customer accounting system at the end of the year for the financial accounts; and
- a further program, the daily customer file aggregation program, which aggregated daily totals of customer balances in the customer accounting system. However, until March 1996, customer balances were calculated on a different basis to the financial accounts due to differences in the treatment of repayments and interest, and manual adjustments had to be made to bring the two bases into line.

Values for the liability to investors in Investment and Ordinary Deposits, as at 31 December 1994, as calculated by the three methods set out in paragraph 2.3 above:

Figure 4

	Financial Accounting Systems £000	Financial Analysis Suite £000	Daily Customer File Aggregation £000
Investment Deposits	9,309,844	9,311,939	9,311,797
Ordinary Deposits	1,433,998	1,434,709	1,434,539

Table1 shows that each of the Agency's methods for deriving the liability of the Exchequer to investors in Investment and Ordinary Deposits at 31 December 1994 gave a different value.

2.4 The Agency considered that the liability to investors derived from the daily customer file aggregation gave the more reliable figure, and in March 1996 they amended the daily file reconciliation procedures to produce a liability to investors value which uses the same basis as that for the financial accounts. National Savings consider that as a result the difference between the liability to investors in the customer accounting records and that in the financial accounting records has been accurately established at £781,136 for Investment Deposits and £521,496 for Ordinary Deposits. In both cases, the liability in the customer accounting system exceeds that in the financial accounting system. For Investment Deposits the additional liability may have to be met from public funds. For Ordinary Deposits the additional liability can be met from surplus funds held by the National Debt Commissioners.

Action taken by the Agency to investigate the historical discrepancies on the liability to investors

2.5 In order to investigate the historical discrepancies on the liability to investors, the Agency have undertaken a reconstruction of the financial accounting records for Investment and Ordinary Deposits. As part of their wider review the reconstruction approach was extended to all other products at the Glasgow site, and they have undertaken reviews of products at Durham and Blackpool. The aim of this work was to identify the problems existing in the financial accounting systems, and to establish that the liability to investors for each product was matched by assets held. The extent to which a product's liability to investors was not so matched would indicate the extent of the historical error in each product's financial statements. The Agency would then be able to examine the historical errors, and identify the causes of them.

2.6 The financial accounts for each Glasgow product were reconstructed for the period from the date the product was introduced to 31 March 1996. The end date of 31 March 1996 was chosen by National Savings as it was the first date at which data could be obtained from the customer accounting system on a basis consistent with the financial accounting system. Further the Agency wished to establish the position at that date to support a full audit of the accounts of all products for 1996-97. As part of this work the Agency also had to reconstruct the Unallocated Monies suspense account which holds customer funds not yet allocated to products.

2.7 The reconstructions were developed around the premise that the liability to investors should equal the sum of the funds held in the Bank of England plus those held by the National Loans Fund for all products except the Ordinary Deposits, and by the National Debt Commissioners for Ordinary Deposits, plus amounts due from agents. Each of these amounts was to be compiled by reference to third party sources to provide an essential independent check on the validity of the balances in the accounts.

Figure 5

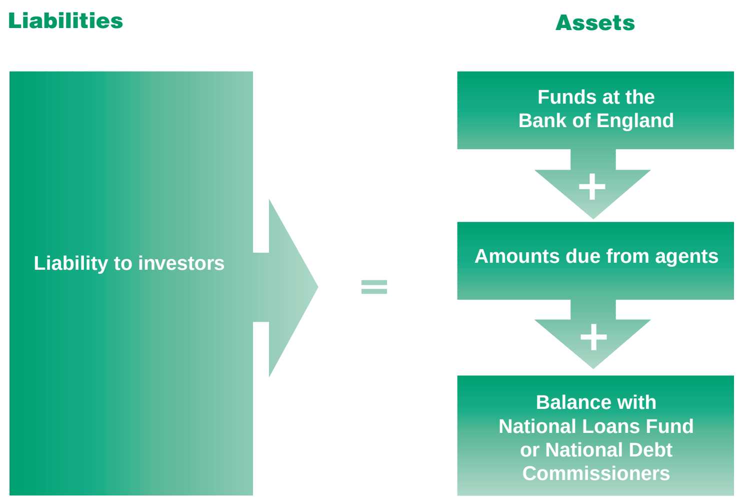


Figure 5 shows the basis of reconstruction of each product's financial accounting records.

2.8 The Agency completed their initial work on these reconstructions in November 1997. National Savings are now able to reconcile the daily change in their customer and financial accounting systems. The results of the reconstruction work confirmed that there were historical problems on the liability to investors for all products. In particular, the work showed that historical differences existed in the value of the liability between the customer accounting and financial accounting systems.

2.9 The unresolved differences identified by the reports are summarised in Figure 6 below which also show the Agency's current view of the overall position. The Agency have classified the differences under two headings:

- **the liability to investors error.** This represents the difference in the liability to investors between the customer accounting system and the financial accounting system.

- **the miscellaneous agents error.** This represents all amounts for which there was no supporting evidence including differences in relation to Post Office Counters Limited, other agents and the Departmental Office suspense account (Part 3).

2.10 Figure 6 shows the differences identified on the liability to investors and miscellaneous agents for each product. Negative figures represent gains to the Exchequer and positive figures represent losses. At the time the reconstructions were completed (November 1997), National Savings estimated an overall gain to the Exchequer of £3.9 million. However by the time of their report to the Committee of Public Accounts in January 1998, this had reduced to a gain of £0.48 million.

2.11 The extent of the error is being refined over time as further work is completed by the Agency. National Savings plan to continue to update the reconstruction work to a more current comparison with the financial accounting data in order to determine whether the differences have stabilised. This work is on-going and has already led to the identification of further revisions to the error. For example, in February 1998, National Savings informed the National Audit Office that they had identified a problem with the Savings Certificates Postpayment Suspense account (used to record outstanding warrants until cleared against customer records) which amounted to a loss of £1,303,191.69. Reconciliation between the general ledger and supporting information from other sources was first carried out in December 1997 and rolled back to October 1996. The Agency have suggested that the error identified could be due to an incorrect opening balance in April 1986, or to clerical errors in the system which was manual until 1995, or to old posting errors to the general ledger. Work on the difference is still ongoing but the Agency is encountering problems due to the lack of supporting documentation.

2.12 In May 1998, National Savings informed the National Audit Office that further work with Post Office Counters Limited had produced an interim settlement resulting in a gain of some £2.25 million, and other smaller adjustments have also been made. The interim adjustments cover identified errors falling into two categories:

- refunds made on Children's Bonus Bonds and Capital Bonds, and in the Ordinary and Investment products; and

- purchases of Pensioners Guaranteed Income Bonds, Income Bonds and Premium Bonds.

For refunds the amount paid over has had to be estimated as insufficient information is available to fully substantiate the amounts due. Work on the differences continues but the Agency are encountering problems due to the lack of supporting historical documentation.

2.13 In June 1998 a further adjustment was notified this time representing a deficit of £576,481. This resulted from the Agency discovering that one of the constituent parts of the SAYE post payment suspense account reconciliation is not accurate.

2.14 At 30 June 1998 the net amount of the error is a gain to the Exchequer of over £0.8 million but it may not be possible for the Agency to reach a conclusive view on the overall cause of the errors which exist in their financial records. This is because of the extent of those errors and the length of time over which they have accumulated.

Recommendation 1

Once the Agency have completed reviews of suspense accounts and agents' balances they should consider the benefits to be derived from their continuing investigations in the context of the costs, and the likelihood that conclusive reasons for outstanding balances and differences will be obtained.

2.15 During their work on the reconstructions the Agency identified a number of differences for which explanations could be found including: amounts transferred to other products which had not been consistently recorded between the financial accounting system and the customer accounting system; errors identified in the classification of some repayments between the two systems; and errors in the treatment of some deposits. These differences are excluded from Figure 6 opposite.

2.16 An important part of verifying the accuracy of the financial accounting systems was the check to independent sources to substantiate values. However in some instances the Agency have used their internal records of the amounts due. For example, in relation to their main agent, Post Office Counters Limited, the Agency have used their settlement records in the reconstruction process which differ from statements provided by Post Office Counters Limited. This is because Post Office Counters Limited do not maintain their records by product. National Savings also maintain that their settlement records are the main record for the cash settlements between the two bodies. However as noted in paragraph 2.12 above, the Agency have now agreed an interim settlement with the Post Office. They are also in the process of agreeing with Post Office Counters Limited a formal project to address the remaining issues and further improve financial dealings between the two organisations for the future.

2.17 National Savings believe that the unresolved differences on the liability to investors may have been due to historical errors in the calculation of interest in their financial accounting systems. As described in the Comptroller and Auditor General's 1996 report, prior to June 1995 the amount for interest in the financial accounts was derived on a number of different bases, involving some estimation and manual adjustment and National Savings consider that by their nature the calculations contained errors. To address this National Savings introduced an interest ledger system in June 1995. The ledger now provides more accurate and reliable interest information.

2.18 The National Audit Office reviewed the Agency's reconstruction work, which had been undertaken under the direct control of the Agency's Director of Finance. National Savings also asked KPMG to review the methodology, but not the amounts, underlying the reconstruction of the financial ledgers.

2.19 The National Audit Office were concerned that the work should be subject to a more in-depth process of quality control, covering the results of the work as well as the methodology. From their review KPMG concluded that the methodology was well founded although they also considered that additional work was needed to validate the sources against which the financial ledgers had been reconstructed, and hence to confirm the differences identified.

2.20 Subsequently National Savings have allocated a senior manager to carry out a review of the reports and this quality control work is in progress. The National Audit Office note that there is no evidence available to support the Agency's earlier view that errors in the calculation of interest in the financial accounting systems may be the cause of the unresolved differences in the liability to investors. In practice given the time period over which the differences have accumulated, and the lack of detailed data, it is unlikely that the Agency will be able to draw any clear conclusions as to causes.

2.21 There are a number of tasks that the Agency are still working on in connection with the reconstruction of the financial ledgers. In particular there is the additional work recommended in the KPMG review of the reconstruction reports. This relates mainly to the substantiation of key balances in the ledgers, and updating of the data. The National Audit Office support the Agency's aim of establishing a stable position on the historical discrepancies for all the products before any adjustments are made to the financial statements for each product. The Agency also intend to consult KPMG on the adjustments required once their work is complete.

Recommendation 2

In the absence of conclusive evidence that gains and losses are matched, the Agency should consider the appropriate accounting treatment for each discrepancy separately once the amounts have stabilised.

Other action taken by the Agency

2.22 In addition to reconstructing the financial accounting records for each product, the Agency also reviewed their procedures for reconciling data between their financial accounting and customer accounting systems. Their investigation of historical discrepancies has been hampered by the lack of a trail for individual transactions from the customer accounting systems to the financial accounting systems, and the Agency have taken action to introduce such a trail for the future. Both these developments should help prevent a recurrence of their past problems.

Review of reconciliation procedures

2.23 National Savings undertook a review of all their procedures which check that their financial accounting and customer accounting systems are in agreement. These reconciliation processes are an important financial control, and if working effectively should prevent the accumulation of discrepancies between the two systems and help, for example, to provide additional safeguards against fraud remaining undetected. As a result of the review National Savings identified a number of older reconciliations which had not been revised to take account of various systems changes and other developments, and these reconciliations are being replaced with more effectively targeted ones.

2.24 As explained in paragraph 2.4 above National Savings have amended their customer account processing such that the daily customer file aggregation procedure now produces a liability to investors' value on the same basis of recording customer transactions as the financial accounting system. Thus it is now possible to agree the change in liability to investors disclosed in the financial accounts with the change in the aggregate of customer balances on a daily basis for all products.

2.25 The National Audit Office are satisfied that the reconciliation process based on the daily customer file aggregation procedure has been properly established, and responsibilities assigned for both operation and review. However, this reconciliation will only be an effective control if differences are actioned promptly, and if the individuals carrying out the reconciliations understand what action is required in respect of any discrepancies. The National Audit Office noted that this did not occur for several months following the introduction of the new reconciliation procedures, although the situation has now improved. However they are concerned as to whether all staff involved in the reconciliation procedure understand its purpose, and the action required if discrepancies arise.

Recommendation 3

Senior managers at National Savings should review regularly the reconciliation between the customer and financial accounting systems to confirm that prompt and appropriate action is being taken to resolve any differences.

2.26 Following the introduction of regular reconciliations, the Agency have been able to establish that some of the discrepancies on individual product's liability to investors values have remained stable. However these reconciliations have only been fully operational since October 1997, and have now been rolled back to April 1996. Constant differences have been identified of £781,136 for Investment Deposits and £521,496 for Ordinary Deposits.

Introduction of transaction trails

2.27 In conjunction with their work on suspense accounts (see Part 3), the Agency have developed a program which enables transactions to be traced from one accounting system to another. The program was introduced in November 1997 (March 1998 for Ordinary and Investment Deposits accounts) and is designed to match transactions input to the customer accounting system with the related financial accounts postings. The Agency have been reviewing the results from this new program, and have separately reconciled all products from the transaction trail data to the input to the financial accounts.

2.28 In addition to creating a transaction trail the Agency are now able to retain data for a period of three years instead of the previous six day limit. National Savings management will therefore have more information available to enable them to identify and investigate problems which arise in their financial accounting systems in future.

Part 3: Improving accounting controls over balances due between products and with external agents, and over suspense accounts

Introduction

3.1 This part of the report covers the action taken by National Savings to rectify the lack of basic accounting controls such as the regular agreement of balances with other products and external agents, and the regular reconciliation of suspense accounts. It also covers the action taken by the Agency to investigate the discrepancies which have arisen, and to review the possibility that fraud may have been a factor, since any deficiency in financial controls inevitably increases the risk that fraud could occur and remain undetected.

3.2 This part of the report is divided into the following sections:

- interproduct balances;
- agents' balances;
- suspense accounts; and
- the Agency's review of fraud risk.

Interproduct balances

Background

3.3 Investors may instruct National Savings to move funds between the Agency's products. Such transfers of funds are commonplace and, due to timing differences in processing transactions, result in balances arising between products. The Comptroller and Auditor General's 1996 report noted that as the average value of daily transfers between Investment and Ordinary Deposits was about £20,000, the balance due between the two products should be low, and in agreement between the two accounts. However, at the end of 1994, the balances were in excess of £5 million and an unexplained difference of about £500,000 existed between them.

3.4 During the year ended 31 December 1995 the balance due between the products was reduced due to the greater value of transfers from Ordinary Deposits to Investment Deposits. At the end of November 1995, the Investment Deposits financial accounting systems recorded the sum of £2.4 million as being due to Ordinary Deposits whereas the Ordinary Deposits showed the sum of £2.9 million as being due from Investment Deposits. Nevertheless these balances were still far higher than would be expected, given the average value of daily transfers, and a net difference of around £500,000 remained.

Action taken by the Agency

3.5 National Savings have investigated the high unexplained balances appearing in the financial accounting systems. They found that while individual transactions had been correctly processed to customer accounts there had been no movement of funds between the product bank accounts since October 1994. They also found that an adjustment processed in 1994 to correct another systems error had caused an increase in the inter product balance. During December 1995 the Agency transferred £2.9 million from the Investments Deposits bank account to the Ordinary Deposits bank account to clear the balance. However, due to the absence in the past of adequate transaction trails in the financial accounting systems, the Agency cannot be certain that the cash transferred between the two products' bank balances represents valid transactions which are matched between the two products.

3.6 The Agency have also transferred the residual net difference of £500,000 to a suspense account, and are continuing to investigate its cause. The Agency's work has identified some possible causes including the failure to account for transactions on old accounts outside their current computer systems, and the inability of their systems to deal with multiple product transfers.

3.7 National Savings are monitoring the balances on the two accounts closely and are satisfied that the system is now functioning effectively on a daily basis. The National Audit Office have briefly reviewed the revised system for interproduct balances, and the early indications are that the revised procedures have improved control over current interproduct balances.

Agents' balances

Background

3.8 Generally, the value of deposits received by agents for Investment and Ordinary Deposits exceeds the value of repayments made by them hence agents owe net amounts to National Savings. National Savings main agent, Post Office Counters Limited, makes a daily transfer of an agreed sum to the Agency. Other agents make a monthly transfer based on the net value of National Savings transactions processed. In his 1996 report, the Comptroller and Auditor General noted that the Agency were unable to reconcile balances due to and from their external agents.

Balance with Post Office Counters Limited

3.9 At 31 December 1994 the amount due from Post Office Counters Limited, as recorded in the Agency's financial accounting system, was some £12 million less than both the Agency's calculation of sums due based on their computerised daily settlement system and the amount shown as due by statements (as adjusted for timing differences) provided by Post Office Counters Limited. The Agency were unable to establish whether the unexpectedly low balance in the financial accounting systems was due to errors within their computer programs in assigning transactions to agents or in accounting for monies received from the Post Office. At 31 December 1995 this difference had increased to approximately £14 million.

3.10 The Agency rely on a number of controls to ensure that all cash due to National Savings from agents has been received. One such control is the matching of data supplied by the agents' individual branches with that supplied by their headquarters; for example, individual Post Office transaction details input by National Savings are matched to weekly accounts provided by Post Office Headquarters. Where differences arise the Agency prepare and issue cash adjustment papers to the agent, and pending action on these, the difference is posted to a Cash Adjustment file. The balance on this file should represent the total of recently identified differences. The Agency believed that changes in the amount of cash adjustment papers explained all or part of the increase from £12 million to £14 million in the difference in the Post Office Counters Limited balance between 1994 and 1995.

3.11 However, as noted in the Comptroller and Auditor General's reports on the 1995 accounts of Investment and Ordinary Deposits, items on the Cash Adjustment file have not been cleared promptly, and the balance on the file cannot be fully reconciled. After taking account of correcting adjustments processed in 1996, the balance on the file at 31 December 1995 was £306,000 net or £8 million gross.

3.12 The National Audit Office reviewed the monitoring of the Cash Adjustment file and found that some of the differences appeared to date back a number of years. However, until February 1997 it was not possible to obtain a detailed analysis of the contents of the file at a given point in time which made control of the file more difficult. Further investigations by National Savings have indicated that delays occurred in the processing of cash adjustment papers by agents, but there has also been a lack of effective action by the Agency in monitoring and following up cash adjustment papers. As a result supporting documentation may no longer be available to enable the make up of the balance on the Cash Adjustment file to be fully identified and cleared.

3.13 The failure to clear cash adjustment papers promptly with external agents has made it difficult to agree balances due from them and could have resulted in cash not being received from agents or monies due to agents for withdrawals being understated. The Agency believe this risk is low particularly in relation to their main agent, the Post Office, as they receive daily round sum settlements from the Post Office based on National Savings' records of transactions processed. However, the Agency do not agree periodically a final settlement with the Post Office for transactions, and they have acknowledged the need to improve controls over the Cash Adjustment file to ensure that the balance, and hence monies outstanding or due, can be agreed with Post Office Counters Limited. As part of these improvements, National Savings have put in place additional arrangements with the Post Office for handling any Cash adjustment papers which are one year old.

Action taken by the Agency

3.14 To address the problems associated with agreeing amounts due from Post Office Counters Limited the Agency set up a Post Office Reconciliation Project Board. The objective of the project was to design or change accounting procedures to produce sufficient management information to facilitate the formalisation of a reconciliation between National Savings' and Post Office Counters Limited' records. Much of the project was focused on an information systems solution, but in practice the team were also required to investigate and resolve the accounting problems underlying the reconciliation. In particular they were required to establish the size, and the reasons behind, the differences between the balance reported by their financial accounting systems and that derived from the Agency's manual calculation of the balance due from Post Office Counters Limited.

3.15 The main changes introduced are shown in figure 7 below:

Procedural changes on Agents' Balances

Figure 7

Internal changes	External changes
■ Establishment of a transaction database. This holds details of all agents' transactions and is compiled from initial input to the customer accounting system. It allows National Savings to produce transaction reports which match agents' reporting periods, which was a problem identified in the Comptroller and Auditor General's 1996 report.	■ National Savings have agreed with Post Office Counters Limited that, from March 1998, there will be, a quarterly exercise to review outstanding reconciliation adjustments or queries that are over 12 months old. All those which have not been solved by that time will be underwritten by Post Office Counters Limited.
■ Introduction of a comprehensive internal reconciliation process between the Agency's records and the Post Office "the cross file reconciliation". (see figure 8)	■ National Savings have clarified the relationship between themselves, Post Office Counters Limited and individual Postmasters. The Agency has confirmed that they have a contractual relationship with Post Office Counters Limited and not with individual postmasters. This part of the chain is internal to Post Office Counters Limited.
	■ Post Office Counters Limited are now required to provide explanations for all adjustments made to their records. The aim is to enable National Savings to mirror these changes to update the Cash Adjustment file to match Post Office Counters Limited' records of the balance due.

Figure 7 shows the changes made or planned within National Savings, and between National Savings and Post Office Counters Limited, to facilitate the agreement of monies due between them.

3.16 The most significant internal change has been the introduction of the cross file reconciliation but this is not yet fully operational. The objective of the reconciliation is that:

Movement in customer balances due to Post Office transactions = **Movement in Post Office balances in the financial accounting system** = **Post Office Counters Limited records**

3.17 There are three parts to the reconciliation as shown in Figure 8 below. Once all three are completed it will enable a comprehensive reconciliation of the sums due between the two parties, and as shown in each accounting system within National Savings.

Post Office Reconciliation

Figure 8

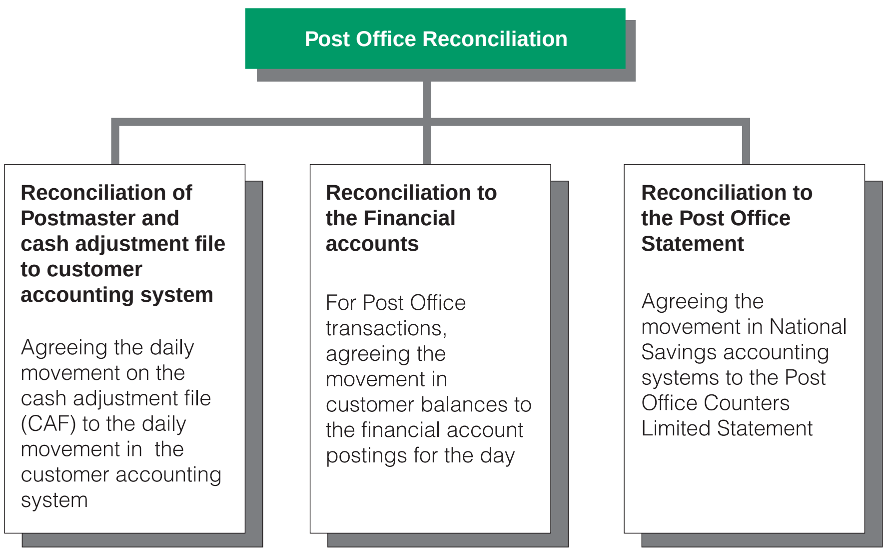


Figure 8 shows the elements of National Savings' reconciliation of their information to that provided by the Post Office to be used for agreeing monies due between the two organisations.

3.18 The National Audit Office found that National Savings have introduced two elements of the cross file reconciliation as follows:

- **Reconciliation of the Postmaster and Cash Adjustment file to the customer accounting system.** This has been implemented since July 1997 on a daily basis. However at the end of November 1997 four discrepancies existed totalling £98,450 (gross). National Savings have worked back this reconciliation to March 1996 to reconcile the outstanding differences;

- **Reconciliation to the financial accounts.** This has been implemented since October 1997.

3.19 The introduction of these two elements of the new reconciliation procedure has enabled the Agency to reduce the unexplained difference of £14 million at 31 December 1995 between the Agency's financial accounting systems and their records of the amount due from Post Office Counters Limited based on the Agency's settlement records to around £800,000. This figure continues to fluctuate and its accuracy has not yet been confirmed with the Post Office.

3.20 At present the third part of the reconciliation, namely the agreement of the balance due with Post Office Counters Limited' statement, has yet to be implemented successfully. There is a significant discrepancy between National Savings and Post Office Counters Limited' records of the balance to be settled by the Post Office. The difference between the two, which covers all National Savings products, has fluctuated over the twelve months to November 1997 at between £1.9 million and £2.9 million. On two exceptional occasions the difference was in excess of £4.1 million. The difference appears to be increasing slowly with a balance at 5 November 1997 of over £2.69 million (which is reduced by the interim adjustment of £2.25 million outlined at paragraph 2.12). The balance represents money owed to National Savings by Post Office Counters Limited.

3.21 The work undertaken by the Agency on reconciliation procedures for agents' balances has identified a number of reasons why differences have arisen. Within National Savings the problems appear to lie with the coding of transactions. The Agency believe, in particular, that poor internal procedures for the coding of cash refunds by warrants, have led to them not being included in the calculation of Post Office Counters Limited' liability to National Savings. However the full reasons for the differences have yet to be established, and this is delaying any final agreement between the two organisations. National Savings have found resolution of these issues more complex than they expected and hence they have not met their undertaking to reconcile all agents' balances exactly by the end of March 1997.

3.22 As part of their ongoing work on the balance with their main agent, National Savings have sought agreement with Post Office Counters Limited on the treatment of outstanding cash adjustment papers. They have agreed that all the cash adjustment papers raised prior to 1 January 1996 are to be deleted from National Savings records and the amount involved of £82,544 gross and £39,078 net is to be settled by Post Office Counters Limited.

3.23 In the future Post Office Counters Limited are to introduce counter automation for National Savings products, and this ought to make full reconciliation of sums owing between National Savings and the Post Office easier. Postmasters will enter data about transactions at the time they are undertaken, and the system will have a direct link to National Savings. The Agency will therefore have full and current information about transactions thus simplifying reconciliation procedures between the two organisations' records. In the interim the Agency have agreed to undertake further joint work with Post Office Counters Limited aimed at resolving the remaining problems.

Other agents' balances

3.24 In his 1996 report the Comptroller and Auditor General drew attention to the differences which existed on other agents' balances for Ordinary and Investment Deposits. At 31 December 1994, statements from the Postal Administrations in Jersey, Guernsey and the Isle of Man showed an overall balance due to National Savings of some £353,000 greater than that shown in National Savings' accounting records.

3.25 The Agency now has in place a reconcilation process for all 3 minor Agencies. This confirms a constant discrepancy of £268,242 in National Savings records when compared to the Agents' records and includes the balances in the Cash Adjustment File. These reconciliations are completed on a weekly basis. The National Audit Office are concerned however that discrepancies identified through these reconciliations, are not being followed up (with corrective action being taken as necessary) as the Agency are currently in the process of training newly recruited staff to undertake these procedures.

3.26 However, as with Post Office Counters Limited, they have yet to be able to agree fully their minor agents' balances. The reconstruction exercise at 31 March 1996 identified some overstated discrepancies for minor agents, for example, a £14 million difference for the Guernsey Post Office for Glasgow products. This exceptional discrepancy, which has since been corrected, was caused by a failure to process an amendment to the financial accounting system.

Recommendation 4

National Savings should introduce a system of periodic settlement of sums due between them and their main agent, Post Office Counters Limited, in addition to their current daily settlement based on estimated flows. The lack of periodic settlement in the past allowed problems to go unresolved and errors to accumulate.

Suspense Accounts

Background

3.27 At 31 December 1994 significant unexplained balances existed on two suspense accounts. One, Unallocated Monies, holds transactions until they have been allocated to products. The balance on this account should therefore represent a liability to investors for accepted deposits, and be represented by cash held in the related bank account. At 31 December 1994, the financial accounting system showed an amount owed by investors of £37 million on the Unallocated Monies account and the related bank account was overdrawn by £28 million. However, investors cannot owe money to the Agency since their accounts are not credited until the money has been received.

3.28 At 31 December 1995, the Unallocated Monies account recorded an amount of £33.7 million as being owed by investors, and the overdrawn bank balance was just over £30 million. The Agency consider that they have identified causes for a significant part of the balances. In particular, they believe that one error, relating to Deposit Bonds, had resulted in funds being moved incorrectly from the Unallocated Monies bank account when no cash movement was due. In January 1997 the Agency transferred £11.7 million from Deposit Bonds to Unallocated Monies to correct what they believed to be the amount of the error. Whilst the National Audit Office have been able to agree the principle behind the transfer of funds, because of the absence of a complete transaction trail the value of the adjustment cannot be proved conclusively. It is intended that the Departmental Office Accounting Section will match funds to transactions in the future.

3.29 The second suspense account, the Departmental Office account, captures transactions not processed by National Savings' agents, for example, direct remittances. The account also handles internally generated transactions. However at 31 December 1994 the Agency were unable to substantiate fully the balances on the Departmental Office suspense account for either Investment Deposits or Ordinary Deposits. The unsubstantiated balances amounted to £3 million and £11.1 million respectively at that date.

3.30 In his report on the 1995 accounts of Investment and Ordinary Deposits, the Comptroller and Auditor General drew attention to the failure by the Agency to clear promptly cash adjustment papers in respect of the Departmental Office account. In the case of the Departmental Office account, cash adjustment papers are internally generated documents, which match the transaction undertaken and the cash received. As with cash adjustment papers in respect of external agents' transactions, supporting documentation may no longer be available to enable the make up of the Departmental Office cash adjustment papers to be fully identified and cleared.

3.31 The Agency believe that a systems error rectified in 1992 in respect of First Option Bonds contributed to the accumulation of uncleared cash adjustment papers for the Departmental Office account, and during 1996 the Agency wrote off cash adjustment papers totalling £1.6 million gross, £93,000 net, to correct this. However in the absence of supporting papers for older items on the Cash Adjustment file the Agency have not been able to reach a conclusion on the treatment of outstanding items.

Action taken by the Agency

Unallocated Monies

3.32 The Agency carried out a brief review of the Unallocated Monies bank account and the Unallocated Monies suspense account. They concluded that it was not possible to match funds going through the Unallocated Monies bank accounts to processed transactions on an individual basis.

3.33 Early action was therefore taken to revise their accounting procedure to enable them to match funds going through the account to underlying customer accounts. An urgent review of the bank account was also completed with the objective of ensuring the reasonableness of current changes in bank balances until new systems to achieve better control over the account are introduced.

3.34 In their reply to the Committee of Public Accounts National Savings indicate that they believe that the amount owing from investors of £37 million and the overdrawn bank account of £28 million offset one another. However this cannot be demonstrated conclusively because records supporting funds transfers from Unallocated Monies to other Glasgow products are no longer available. The Agency's work suggests that this situation is due to the incorrect processing of encashed warrants from banks.

3.35 The Agency reported to the Committee of Public Accounts that the Unallocated Monies account was understated by £34.1 million and the corresponding bank balance by £30.5 million. They believe that correcting the accounting records for these understatements would mean that the Unallocated Monies suspense account would be reduced to about £3.6 million, while the associated bank balance would show a very small positive balance. In total they believed that this implied a loss to the Exchequer of £3.6 million within the overall surplus, although subsequent work by the Agency has reduced this to £3.4 million.

Departmental Office Account

3.36 A broad review of Glasgow's Departmental Office procedures was completed by the Agency in October 1997. This review examined procedures for processing sales, aftersales queries and adjustments to customer accounts, and assessed the control over the clearing accounts. As a result, in November 1997 National Savings introduced a new computer program to track individual transactions through the system, and supported this with improved clerical and management controls although these are not yet operational. Since that date the Agency have been trying to substantiate the balances on the Departmental Office account for each product.

3.37 As indicated at paragraph 3.30 the number of unsupported internal cash adjustment papers have contributed to the problems of the Departmental Office account. The Agency has been able to adjust some 1,150 out of around 1,300 cash adjustment papers leaving 149 outstanding with a value of approximately £331,000 gross, £35,000 net.

3.38 National Savings' review calculates the outstanding balance on the Departmental Office account by reference to uncleared funds banked in the local bank accounts for each product. However the National Audit Office note that this calculation produces markedly different balances for each product's Departmental Office account from those calculated by National Savings in their reconstruction of the liability to investors for each product (see Part 2: paragraphs 2.5 to 2.17). These differences are shown in Figure 9 below.

3.39 National Savings attribute these inconsistencies to differences in the assumptions used in each exercise, and to both exercises including estimates. They also note that the Departmental Office account figures in the calculations based on local bank records were intended to add weight to the recommendations made as a result of the work, rather than to be soundly based calculations. The Agency need to complete their work in this area to resolve these inconsistencies and to determine which figures are the more reliable.

3.40 Any changes arising from this work will affect the net discrepancy identified by the Agency's reconstruction of the liability to investors. Specifically, they would alter the amounts included under Miscellaneous Agents in Figure 6, and so would change the overall discrepancy of £827,000 surplus of assets currently shown in Figure 6. It is therefore essential that explanations are sought for the differences in Figure 9. The Agency also need to complete their investigations into the Departmental Office account balances before they decide the appropriate action to correct their accounting records once the size of the discrepancy has finally been determined.

Recommendation 5

National Savings should pursue and resolve the discrepancies in values for the Departmental Office account between their report on that account and the liability to investors reconstruction reports as until these are resolved doubts will remain as to the reliability of the outcome of both these reports.

Figure 9

Differences between the value of the Departmental Office account for each product in the Local Bank Account compared to the Reconstruction Reports

Product	**Per local bank records at 31.03.96** £	**Per reconstruction reports at 31.03.96** £	**Difference** £
Annuities & Insurance	89.67	104.47	14.80
Children's Bonds	(1,545,495.06)	1,016,390.66	2,561,885.72
Capital Bonds	348,370.77	40,339.68	(308,031.08)
Deposit Bonds	3,031,190.40	(29,590.47)	(3,060,780.87)
FIRST Option Bonds	3,071,482.18	3,251,125.39	179,643.21
Gift Tokens	(254,933.13)	600.25	255,533.38
Investment Deposits	15,956,291.55	4,408,125.40	(11,548,166.15)
Ordinary Deposits	(14,981,216.72)	185,295.37	15,166,512.09
Savings Stamps	(2,030.14)	(528.21)	1,501.93
Unallocated Monies	(10,406,721.43)	(2,069,689.07)	8,337,032.36
TOTAL	**(4,782,971.91)**	**6,802,173.48**	**11,585,145.38**

Source: National Savings

3.41 In order to improve future accounting for Departmental Office account transactions and funds, the Agency established a Departmental Accounting Section (DAS) at Glasgow in November 1997. The role of this Section is to agree the value of transactions processed with the value of cash received, for each Branch within National Savings dealing with Departmental Office account transactions, and in total. Any outstanding balance should be represented by sums banked in respect of unprocessed transactions.

3.42 At the end of January 1998 the Departmental Accounting Section had yet to agree an opening balance on the Departmental Office account either for any product or for the Glasgow site as a whole. The Agency informed the National Audit Office that this delay was due to difficulties experienced in obtaining sufficient detail on the source of Investment and Ordinary Deposits transactions. The Agency intended to complete this work by the end of March 1998. Only once this work is complete will the Agency be able to establish the residual error in the Departmental Office account balances for each product.

3.43 The review of the Departmental Office account and Unallocated Monies accounts is not final, and National Savings have yet to complete their internal quality control of the project. In addition they are seeking advice and guidance from KPMG, on possible courses of action to investigate the discrepancies.

Review of fraud risk

3.44 The Agency asked their external consultant, KPMG, to review their financial accounting systems to consider whether fraud could have contributed to the discrepancies and unexplained balances within those systems. KPMG agreed with the conclusion of the Committee of Public Accounts that the absence of basic controls greatly increased the risk that fraud could occur and remain undetected. In particular, they concluded that:

- there were undoubtedly weaknesses in controls which could have provided the opportunity for fraud;
- in principle, fraud could have been a contributory factor for the unresolved differences in the financial transaction accounting system;
- any conclusions must await the completion of the additional work that they recommended in their review of the liability to investors' reconstruction reports to identify the sources of the unresolved differences which may provide further indicators as to the scope of fraud risk.

3.45 These conclusions are in line with the National Audit Office's assessment of the financial accounting systems. Moreover the length of time over which the problems have arisen, and the absence of transaction trails within the Agency's financial accounting records, means that proving the existence or otherwise of fraud is very difficult.

3.46 The Agency believe that their various non-accounting checks and balances make the perpetration and subsequent concealment of significant internal fraud unlikely. While they recognise that they can give no absolute assurance, they have concluded that the accounts have not been affected to any material extent by undetected fraud; and that further investigation into the possibility of undetected fraud is unlikely to advance the situation significantly.

3.47 The Agency are, however, undertaking further work on, for example, dormant accounts and controls surrounding amendments to data. Although the Agency has no evidence that fraud has actually occurred, these were identified as areas potentially suceptible to fraud in an Internal Audit review. The Agency are also continuing their investigations into suspense accounts and agents' balances.

Part 4: Other action taken by the Agency to improve accountability arrangements

Introduction

4.1 This part reviews other action taken by the Agency in response to the Committee of Public Accounts' concerns over the Agency's accountability arrangements.

Background

4.2 In their report, the Committee of Public Accounts emphasised that it was the responsibility of the Accounting Officer to ensure that appropriate financial controls were in place and operating effectively. He should also ensure that he has mechanisms in place to provide him with assurance about the effectiveness of those controls. Such mechanisms include clearly defined responsibilities for accounting activities, an effective review function for financial controls such as internal audit, and responsibilities allocated on the basis of evidence of appropriate skills and experience.

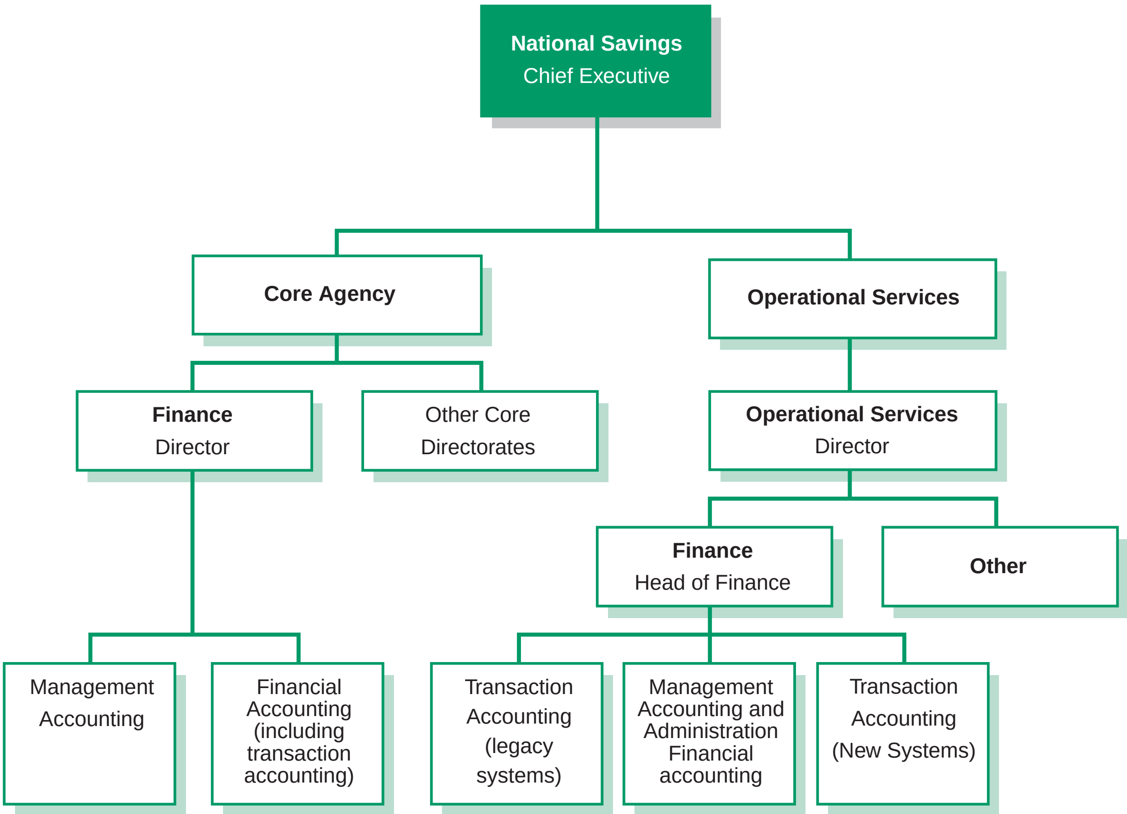
Action taken by the Agency

Organisational Changes

4.3 Since the publication of the Comptroller and Auditor General's 1996 report there have been some significant organisational changes within National Savings. The Agency have divided their activities into Core and Operational Service Divisions. The core covers main policy making and strategic decisions. The Operations Service Divisions cover all of the operations and non-core processes. Figure 10 below sets out the structure of the finance functions within the new organisational structure.

Figure 10

Revised Organisational Structure at National Savings



4.4 Under the new structure the Agency have defined lines of management responsibility for financial controls. Specifically they have:

- appointed a head of finance for the Operational Services Division. This replaces the previous structure where responsibility for finance was divided between National Savings sites;

- conducted a review of accounting policies and standards which they intend to use to set out responsibilities between Core Finance and the Operational Services Division, together with the mechanisms to ensure that control standards are met; and

- issued a working draft of a formal Service Level Agreement between the Core and the Operational Services Division.

4.5 The National Audit Office believe that a contributory factor to the problems was a lack of effective communication between Head Office finance staff and the Glasgow finance staff in particular, and insufficiently detailed monitoring by Head Office Finance Staff of the activities of site finance functions. They note that the responsibility for ensuring that effective financial controls are in place, and that they operate, remains with the Finance Director, and ultimately the Accounting Officer.

Recommendation 6

Although the Agency have split their finance responsibilities between core and operations, those with core finance responsibilities should actively monitor the Operations Finance staff to ensure that they receive early notice of any problems arising.

Review of accountancy resources

4.6 National Savings have acknowledged that the shortage of accountancy staff in the past has meant that insufficient resources have been available to concentrate on development work. Instead resources were devoted to solving the most pressing problems. Until 1979 the Agency had just two accountants. Subsequent reviews and in house training brought the number up to 10 in 1993. However the Agency recognised that this was not sufficient, and the Committee of Public Accounts were also concerned at the Agency's lack of senior finance staff with appropriate accountancy qualifications. They requested the Agency to act on the recommendations of their own review of their needs for suitably qualified accounting staff, and those of their recruitment programme.

4.7 The Agency have reviewed the level of accountancy resources and confirmed that their objective is to increase the number of qualified accounting staff to around 30. They currently have 19 qualified staff, and a further 22 staff undertaking professional training. National Savings have recruited four accountants within the last six months. These include a new Finance Director who is a qualified accountant recruited from the private sector.

4.8 The Agency have carried out an organisational review to identify the posts which should be filled by people with a full accountancy qualification and this is now a requirement of the appointment process to those posts. The balance of posts requiring a full accountancy qualification between site locations has been improved as a result as shown in Figure 11 below, although Blackpool remains low:

The location of qualified accountants in National Savings

Figure 11

	31 Dec 96	**31 May 98**
London	5	6
Glasgow	8	7
Durham	1	4
Blackpool	1	2
Total	**15**	**19**

4.9 The Agency have identified eleven specific posts where the postholder should be a qualified accountant, and a further seven posts where the postholder should be either a qualified accountant or have a sound knowledge of the subject area. Qualified or part-qualified accountants occupy all but two of these 18 posts. The National Audit Office, note however, that within the Operational Services Division, the key post of Head of Finance has not been identified as requiring a qualified accountant as the post has wider personnel and management responsibilities.

4.10 In 1994 the Agency reviewed and identified the training needs of their non-accountant finance staff. The National Audit Office found that some of the needs identified in that report have still not been met; in particular the recommendation for a course in double entry bookkeeping. Following the Agency's recent reorganisation, a training officer for finance staff in the Operational Services Division has been appointed. The training officer is responsible for drawing up training plans. It is essential that the Agency address the training needs of their non-accountant finance staff urgently, particularly for those holding key finance posts with responsibility, for example, for key reconciliation procedures.

Recommendation 7

The Agency should address the financial training needs of their non-accountant finance staff as a matter of priority; in particular for those key finance posts with responsibility for important review and control functions, for example, staff undertaking key reconciliations.

4.11 Most of the Agency's trainee accountants will not qualify until the year 2000. It is not clear therefore whether the benefit of the training will be felt in the short term. The majority of those studying for the professional accountancy qualification are existing staff in relatively junior positions within the organisation, and it may be difficult for them to raise and influence accounting issues whilst in these positions.

Accounts for all National Savings' products

4.12 National Savings are required by statute to produce audited accounts for only two of their products: the Ordinary Deposits and the Investment Deposits Accounts. The Committee of Public Accounts were concerned that the Agency were not therefore formally accountable for their other fourteen products. They recommended that accounts be produced and audited by the Comptroller and Auditor General from 1996-97 onwards.

4.13 National Savings have produced an account covering all their products for 1996-97 although this account has yet to be fully completed. National Savings and the Treasury have agreed that these accounts should be audited by the Comptroller and Auditor General by agreement. They do not propose to make the audit of National Savings' products a statutory requirement.

4.14 The Committee of Public Accounts also recommended that the accounting year end of Investment and Ordinary Deposits be amended from 31 December to 31 March to bring it into line with the financial year. Provision has been made in the Finance Bill to enact such a change with a fifteen month accounting period to 31 March 1999.

Enhancement of the role of Internal Audit

4.15 The Agency have recognised the need for their Internal Audit function to place greater emphasis in their work on the provision of assurance to the Accounting Officer about the operation of financial controls within the Agency. New audit procedures have been introduced which are aimed at reviewing the controls in the financial accounting and reporting system. These will also address the need for Internal Audit to provide the Accounting Officer with an annual opinion on the adequacy of financial controls in accordance with general Treasury guidance.

4.16 In addition the Agency have strengthened the role of their Audit Committee. The Committee is now established as a Committee of the full Board of National Savings. A non-executive director has been appointed to the Committee and he reports issues from Audit Committee meetings to the Board. The Treasury and the National Audit Office have permanent invitations to attend Committee meetings. It is planned that the Audit Committee will formally approve the accounts of National Savings.

Future developments

4.17 The Agency has been through a number of significant changes over the last two years, a key one being the split into core and operational functions. They are currently considering proposals to involve the private sector in the delivery of their operations. This project is being undertaken in conjunction with their Business Process Re-engineering project which has an objective of moving towards a common accounting system across all products by the year 2000. The Agency intend to commission KPMG to report on the controls that are being built into the new system and on those that are in legacy systems that must operate in the meanwhile.

4.18 The age of some of the Agency's current systems means that they are not all year 2000 compliant. There is a risk therefore that at that date, National Savings' systems may not be able to function fully. In response to this threat, the Agency have commenced a project to review and revise all their computer systems. They plan to complete this work by the end of 1998. The Agency employed an external consultant to review the project. The consultant reported that they had no major concerns about the methodology used or in relation to Year 2000 issues.

Recommendation 8

Only substantiated balances should be transferred to any new accounting systems, which National Savings develop themselves or which are provided by a private sector supplier, and that adequate financial controls are built into those systems.

Appendix

National Savings replies to PAC Recommendations

Table overleaf.

Figure 6

Table showing change in differences identified since the reconstruction exercise

	LTI Differences £	Miscellaneous Agent £	Net position at reconstruction £	Revisions to LTI £	Revisions to Misc Agent £	Net Position at 31 Jan 98 £	Revisions to LTI £	Revisions to Misc Agents £	Position at 30 June 1998 £
Glasgow products									
Annuities	0.00	1,414.41	1,414.41	0.00	0.00	1,414.41	0.00	0.00	1,414.41
Childrens Bonds Bonus	-207,773.30	-1,792,212.58	-1,999,985.88	34,212.66	-33,524.96	-1,999,298.18	0.00	0.00	-1,999,298.18
Capital Bonds	0.00	-1,456,818.16	-1,456,818.16	0.00	-75,102.94	-1,531,921.10	0.00	0.00	-1,531,921.10
Deposit Bonds	-545,828.03	-11,876,695.58	-12,422,523.61	478,530.61	1,438,579.61	-10,505,413.39	0.00	0.00	-10,505,413.39
First Option Bonds	3,855.00	2,733,003.49	2,736,858.49	0.00	77,423.16	2,814,281.65	0.00	0.00	2,814,281.65
Gift Tokens	0.00	-252,115.84	-252,115.84	0.00	0.00	-252,115.84	0.00	0.00	-252,115.84
Investment Account	781,136.25	-5,613,391.03	-4,832,254.78	0.00	375,371.14	-4,456,883.64	0.00	2,548.32	-4,454,335.32
Ordinary Account	521,495.54	-16,577,027.49	-16,055,531.95	0.00	943,268.21	-15,112,263.74	0.00	0.00	-15,112,263.74
Savings Stamps	0.00	-2,482.92	2,482.92	0.00	0.00	-2,482.92	0.00	0.00	-2,482.92
Unallocated Monies	34,103,845.62	994,363.36	35,098,208.98	0.00	676,011.75	35,774,220.73	0.00	-1,611,483.72	34,162,737.01
Sub total	34,656,731.08	-33,841,962.34	814,768.74	512,743.27	3,402,025.97	4,729,537.98	0.00	-1,608,935.40	3,120,602.58
Durham Products									
Savings Certificates	-10,397,538.27	4,724,224.51	-5,673,313.76	-449,386.53	0.00	-6,122,700.29	-597,329.18	1,294,122.16	-5,425,907.31
Save as You Earn	-111,766.33	0.00	-111,776.33	0.00	0.00	-111,766.33	0.00	576,480.77	464,714.44
Yearly Plan	-197,108.63	62,603.59	-134,505.04	0.00	0.00	-134,505.04	0.00	-4,237.35	-138,742.39
Treasurers Account	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Unallocated Monies	0.00	0.00	0.00	0.00	0.00	0.00	0.00	9,893.01	9,893.01
Sub total	-10,706,413.23	4,786,828.10	-5,919,585.13	-449,386.53	0.00	-6,368,971.66	-597,329.18	1,876,258.59	-5,090,042.25
Blackpool Products									
Premium Bonds	6,924.63	42,722.96	49,647.59	0.00	0.00	49,647.59	-8,363.63	157.00	41,440.96
Pensioners Bonds	0.00	-57.50	-57.50	0.00	0.00	-57.50	0.00	57.50	0.00
Marketables	406,025.41	-135,348.11	270,677.30	0.00	0.00	270,677.30	0.00	-9,052.69	261,624.61
Income Bonds	-438,499.21	1,277,021.69	838,522.48	0.00	0.00	838,522.48	0.00	0.06	838,522.54
British Savings Bonds	0.00	290.00	290.00	0.00	0.00	290.00	0.00	-290.00	0.00
Unallocated Monies	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Sub total	-25,549.17	1,184,629.04	1,159,079.87	0.00	0.00	1,159,079.87	-8,363.63	-9,128.13	1,141,588.11
Total	**23,924,768.68**	**-27,870,505.20**	**-3,945,736.52**	**63,356.74**	**3,402,025.97**	**-480,353.81**	**-605,692.81**	**258,195.06**	**-827,851.56**

PAC Recommendation	Treasury Minute	National Savings Reply to PAC	NAO Report paragraph
On financial accounting problems at the agency:			
1. We consider that the number and size of the discrepancies and unreconciled balances which have been shown to exist in National Savings' financial accounting systems are unacceptable... It is essential that the agency should now discharge their responsibilities for accurate financial reporting to Parliament.	PAC conclusions 1 to 3: The Agency acknowledges that insufficient priority has been given to the investigation and resolution of discrepancies and unreconciled balances in the past. The Agency have put in place an urgent programme of work investigate the discrepancies and unreconciled balances. This work includes examination of whether there is any evidence that fraud has been or might have been a contributory factor. The Agency's programme of work, which they have discussed with the National Audit office, is structured to meet the commitment to complete the investigations not later than 31 December 1997.	The Agency has introduced new IT systems and revised reconciliation procedures which enable it to reconcile the Liability to Investors, as disclosed in the financial accounts with the aggregate of customer account balances on a daily basis. These reconcilations have been carried out regularly for current transactions since July 1997, and have also been performed retrospectively to March 1996. The Agency has identified a constant difference of £781,000 for the Investment Account and £521,000 for the Ordinary Account and therefore concludes that the causes of these differences have now been rectified. In each case the liability in the financial accounts is less than that of the aggregate customer records, and the differences is therefore a potential loss to the Exchequer (para 9).	2.5 2.22
		On interproduct balances: National Savings has reviewed the system which supports the recording of transfers between the two products and the associated movement of funds. The system now improved controls and ensures regular reconciliation of balances. Probable causes of the unexplained difference of £500,000 between the two accounts mentioned in the C&AG's report have been identified and corrective action has been specified. This remaining balance of £500,000 will be transferred to a suspense account pending the outcome of the discussions with the Treasury (para 11).	3.3
2. The Agency's accounts show that the amount due from Post Office Counters Limited is some £12 million less than is shown by other calculations and by statements provided by Post Office Counters Limited and that one of the other Agency's accounts showed an amount owed by investors of £37 million although depositors cannot owe money to the Agency.	See above.	From January 1997 National savings have introduced regular reconciliation of POCL records to a supporting record outside the financial accounting system to improve control over current transactions and subsequently extended the reconciliation to the financial accounts. Certain transactions types have been treated differently by National Savings and POCL in their respective financial accounts, and discussions are on-going. Following agreement, National Savings believes full control over current transactions will exist. Resolution of these issues has been more complex than initially thought and it is acknowledged that balances have not yet been reconciled (para 12).	3.14 3.8

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PAC Recommendation	Treasury Minute	National Savings Reply to PAC	NAO Report paragraph
		The Agency has also held discussions with each minor agent, and introduced similar improvements to systems and control procedures, from January 1997. It is finalising reconciliations between the agents' statements and National Savings' financial accounting records to establish the extent of any historical differences between the two sets of records (para 14).	3.24 - 3.26
3. The Agency should investigate fully the discrepancies …and … establish whether fraud has been, or might have been, a contributory factor. These investigations should receive high priority … to meet their commitment to complete them by the end of 1997.	See above		3.44 - 3.47
On the causes of the accounting problems:			
4. Financial control within the Agency's financial accounting systems has been seriously inadequate. We note that the Agency placed importance on accurate accounting for individual customer transactions, and on seeking to ensure that individual customers' accounts are correct. We are concerned that the Agency failed to recognise the importance of … having a complete transaction trail from the customer accounting systems to the financial accounting systems.	The Agency regards the Committee's criticisms very seriously. It remains committed to accurate accounting at individual customer level, which is vital for the conduct of its business. It has introduced a transaction trail from the customer accounting system to the financial accounting systems for the Ordinary and Investment Account and will introduce trails for other products where there are similar problems. It intends to ensure that such trails are built in at the outset to all new systems.	The Agency has improved systems to provide a transaction trail from the Agency's transaction processing system to the financial accounting systems (para 29).	2.23 - 2.28
5. The Agency failed to apply basic accounting controls … The absence of such controls leads to a greatly increased risk that fraud could occur and remain undetected. We … draw only limited assurance from the Agency's evidence that the level of detected fraud in recent years has been low. We note the Accounting Officer's assurance that procedures to reconcile balances with external agents will be in place by the end of March 1997.	The Agency accepts the need to apply sound accounting controls and their value in preventing fraud. It now has in place arrangements that allow regular reconciliation of individual customer accounts to the financial accounting totals for all products and the regular agreement of balances with other products. It has introduced new systems to allow it to reconcile balances with external agents. It has carried out work to achieve regular reconciliation of suspense accounts. Current transactions on the unallocated monies account are now reconciled regularly. A review to achieve reconciliations for the associated bank account and Departmental Office Account was completed by March 1997 and identified further systems improvements are required. That work is urgently in hand to ensure that the Agency meets its commitment to resolve all these issues by 31 December at the latest.	The Agency carried out a review of the controls over the Departmental Office Account. As a result they introduced in November 1997 a new IT system to track individual transactions. The new system includes improved clerical and management controls. The Agency has worked since November 1997 to substantiate the balances in this account for each product (para 15, exclu first sentence).	3.36 - 3.43 3.22 - 3.31

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PAC Recommendation	Treasury Minute	National Savings Reply to PAC	NAO Report paragraph
		A new account structure for unallocated monies liability to investors has been established to reconcile underlying customer ledgers and to ring fence the balances in old accounts for investigation. No problems have arisen with the reconciliation since March 1996. An urgent review of the associated bank account was also completed to ensure the reasonableness of current changes to the balances until new systems to achieve better control are introduced (para 16).	3.32 - 3.33
		The work of the Agency has indicated that this structure arose because transactions were incorrectly transferred from Unallocated Monies to product accounts. Incorrect transfers from Unallocated Monies to products affect both the liability to investors and bank balances within unallocated monies. The Agency believes that the balance on the account (£37 million) and the balance on the bank account (£28 million overdrawn) offset one another, but this cannot be proven conclusively (para 17).	3.34 - 3.35
		National Savings has identified weaknesses which could have provided the opportunity for fraud but the risk of exploitation has proved difficult to quantify. The greatest risk identified relates to the transactions through the Departmental Office account where some unresolved differences between cash and transactions have not been investigated and had been allowed to build up over a period of years. However there is no evidence of fraud (para 25).	3.44 - 3.47
		A National Savings senior Accountant was dismissed because of his conduct as Treasurer of the Glasgow Office's Sport and Social Association. This has been investigated and no evidence of fraud was found (para 28).	
6. The Accounting Officer should ensure that there are mechanisms in place to provide him with assurance that the financial controls are operating effectively.	See replies to conclusions 1 - 3. Improved mechanisms have now been put in place to provide the Accounting Officer with assurance that financial controls are operating effectively. These include regular reports from the Finance Director to the Board, and an enhanced role for the Agency's audit committee and internal audit unit in considering the effectiveness of financial controls.	The Finance Director now provides a monthly report to the National Savings Board which sets out progress in resolving issues raised in the PAC report and other issues of importance. Internal Audit's role in reviewing the operations of financial control has been strengthened (para 32, exclu first sentence).	4.3 - 4.5 4.15 - 4.16

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PAC Recommendation	Treasury Minute	National Savings Reply to PAC	NAO Report paragraph
		The Agency have clarified lines of responsibility for financial controls. A customer/provider relationship between the care Agency and Operations Division who handle customer transactions and product accounting will be set up. Accounting policies and standards have been setting out the responsibilities between core finance and operations and the mechanisms to ensure that control standards are met. A post of head of Operations Finance has been created. This has replaced the previous structure where responsibility for financial reporting/control was divided between sites (30).	4.4
		The Audit Committee is now a Committee of the full board. It meets quarterly and considers reports from the Finance Director, Internal Audit and the National Audit Office. It formally approves the accounts. A non-Executive Director has been appointed as a member of the Committee and reports from meetings to the main Board. The Treasury and the NAO have permanent invitations to the Audit Committee (para 33).	4.16
7. The Treasury should ensure that accounts are produced for all National Savings products and for arrangements to be made for the C&AG to audit the accounts.	The Treasury accepts this recommendation. It has been agreed that the accounts for all products will be audited by the Comptroller and Auditor general from 1996-97 onwards.	It has been agreed that the accounts for all National Savings products will be produced and audited by the Comptroller and Auditor General from 1996-97 onwards (para 34).	4.12 - 4.14
On corrective action taken and planned by the Agency:			
8. The Agency should determine the precise liability of the Exchequer to investors. We note the Agency's commitment to modernise computer systems.... We look to the Agency to give priority to financial reporting considerations in developing the new systems.	The Agency accepts the need to determine the precise liability of the Exchequer to National Savings investors. The programme of corrective action is designed to achieve this. The Agency are giving high priority to the importance of financial reporting consideration in the development of new computer systems.	The Agency accepts the need to determine the precise liability to investors and have taken steps noted in above to address the issue (para 35, first sentence).	2.5 - 2.21
9. The Agency intends to act on all of these recommendations ...by the end of 1997. We shall wish to be satisfied that these recommendations have been implemented within that timescale, and that the necessary improvements in financial controls have been achieved.	The Agency are committed to acting on all of the recommendations contained in the Comptroller and Auditor General's report by the end of 1997. The Agency's programme of corrective action is scheduled to achieve the improvements within that timescale. The Agency will report back to the Committee by 31 January 1998.	Our report outlines progress made. Action on all the recommendations is complete or nearing completion. However the Agency did not succeed in completing all the work by 31 December 1997. The main outstanding balances are with the Post office and other agents and to complete the development of new controls over the Departmental Office suspense ledger (para 3).	3.21 - 3.23 3.24 - 3.26 3.36 - 3.43

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PAC Recommendation	Treasury Minute	National Savings Reply to PAC	NAO Report paragraph
10. We expect the Agency to fulfil their intention to produce audited accounts for all National Savings products from the 1996-97 financial year and suggest the reporting period for the Investment Deposits and Ordinary Deposits accounts be changed from the calendar to the financial year.	The Agency fully intend to produce audited accounts for all National Savings products from the 1996-97 financial year onwards. They have agreed the format of such accounts with the Treasury and National Audit Office...They are pursuing the Committee's suggestion to change the reporting period for the Investment Deposits and ordinary Deposits from the calendar year to the financial year. This will require legislation.	Accounts have been produced and are undergoing audit. The accounts will be revised, in consultation with the NAO, when agreement has been reached with the Treasury on the correct treatment of the various differences referred to in our report. The Agency is continuing to pursue the Committee's suggestion to change the reporting period for these accounts to the year to 31 March (para 37).	4.13
11. We are concerned at the lack of senior finance staff worth appropriate accountancy qualifications. We expect the Agency to act on their review of National Savings needs for suitably qualified accounting staff and of their recruitment programme.	The Agency are taking steps to increase the number of qualified accounting staff to around 30 in line with the conclusions of their review. They have identified eight internal staff to commence accountancy training and are in the process of appointing two accountants to fill more senior positions.	National Savings has continued to take steps to increase the number of qualified staff to around 30. The current number of qualified accounting staff is 18. They include a new Finance Director who took up post on 8 December 1997 (para 38 - 39).	4.6 - 4.11